PUBLIC SECTOR FINANCIAL MANAGEMENT PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

PFM 1: PUBLIC SECTOR ACCOUNTING

MONDAY 12 JUNE 2023

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.

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Section A

This question is compulsory and must be attempted.

<u>QUESTION ONE</u> – (COMPULSORY)

You have just been recently posted to the Ministry of Finance and National Planning under the Office of the Accountant General and particularly in the department of Financial Reporting and Information System. The department is responsible for the consolidation of government accounts. You have been presented with the following information for the year ended 31 December 2022.

	K'Million
Salaries – Super scale	6,760
Salaries – Division I & II	2,010
Salaries – Division III	230
Administrative cost	3,350
Conferences and seminars	1,260
Fines	150
Foreign travel	750
Fees and charges	310
Social benefits	1,040
Fuel levy	700
Domestic debt interest	1,450
Grants	430
External debt interest	1,740
Purchase of vehicles	250
Treasury bills	11,120
Purchase of equipment	410
Government bonds	13,460
Euro bonds	7,460
Bilateral and multilateral debt	19,660
Construction of infrastructure	560
Cash and bank	2,470
PAYE	7,330
Corporation tax	5,010
VAT	2,320
Other expenditures	910
Accumulated fund	44,760

Additional information:

1. The current chart of accounts based on the Government Financial Statistics (GFS) 2001 is used to classify revenues and expenditure.
2. VAT of K50m was due to Government but was not received by Government as at 31 December, 2022.
3. A grant agreement signed in 2021 by the Government of the Republic of Zambia and the American Embassy for the purchase of various medical supplies for Matero Health Centre was received and paid for in November 2022.

Required:

(a) Prepare the trial balance of the consolidated fund for the year ended 31 December 2022 for the Government of the Republic of Zambia. (13 marks)

(b) Prepare the Statement of Financial Performance for the consolidated fund for the year ended 31 December 2022 for the Government of the Republic of Zambia. (20 marks)

(c) Briefly describe how the Government of the Republic of Zambia accounts for revenues and expenditures. (7 marks)

[Total: 40 Marks]

SECTION B

There are FOUR (4) questions in this section.

Attempt any THREE (3) questions.

<u>QUESTION TWO</u>

Public sector accounting ensures that public sector authorities have an obligation to account for what has been done (or not done) with the resources entrusted to their care because of responsibility they have been given.

Public sector accounting, puts in place a framework for budgeting for revenue and expenses, executing the budget and producing financial reports to ensure revenue and expenditure are well accounted for.

Required:

(a) Explain five (5) objectives of public sector accounting. (10 marks)

(b) Identify five (5) users (2 internal users, 3 external users) of public sector financial information and their information needs. (10 marks)

[Total: 20 Marks]

<u>QUESTION THREE</u>

In Zambia, the Ministry of Finance and National Planning is responsible for revenue generation, allocation and accounting. Budget Office is responsible for coming up with revenues, allocation and mobilization of revenues while the Office of the Accountant General is responsible for accounting for both revenues and expenditures and for formulating and enforcing financial management guidelines.

In preparing accounts, officers working in the public sector need to adhere to certain principles that guide the preparation of accounting information.

Required:

(a) Briefly explain the following as they relate to resource mobilization and utilization.

(i) Public debt (3 marks)
(ii) Public revenue (3 marks)
(iii) Public expenditure. (3 marks)
(iv) Public sector financial management. (3 marks)

(b) Explain the following as applied in public sector accounting, giving a practical transactional example of each.

(i) Comparability (4 marks)
(ii) Periodicity concept (4 marks)

[Total: 20 Marks]

QUESTION FOUR

The International Public Sector Accounting Standards Board (IPSASB) has developed a conceptual framework for General Purpose Financial Reporting by public sector entities. The conceptual framework provides the basis for ensuring that financial reports are of the attributes that make information useful to users and support the achievement of objectives of financial reporting. In addition, the conceptual framework aids the development of International Public Sector Accounting Standards (IPSASs) and the required guidelines.

Required:

(a) Briefly explain the five (5) qualitative characteristics of useful financial information. (10 marks)
(b) Identify and explain two (2) key constraints on information included in General Purpose Financial Reports. (5 marks)
(c) Explain the five (5) elements of Financial Statements in the public sector. (5 marks)

[Total: 20 Marks]

QUESTION FIVE

(a) An Integrated Financial Management Information System (IFMIS) is a computer-based, inter-related set of sub-systems used to plan, process and report on financial resources in a broad spectrum of financial management areas.

Required:

Explain how IFMIS is used in the management of public debt. (5 marks)

(b) The regulation of the conduct of professional accountants has been under spotlight in the recent past following adverse audit reports from various ministries. The International Accounting Education Standards Board (IAESB) adopted IES 4 professional values, Ethics and Attitudes.

Required:

Explain the five (5) fundamental principles of professional ethics, giving practical examples of actions that entail breach of the principle by a professional accountant. (15 marks)

[Total: 20 Marks]

END OF PAPER

PFM 1: PUBLIC SECTOR ACCOUNTING SUGGESTED SOLUTIONS

SOLUTION ONE

(a) **Trial balance of the consolidated fund for the year ended 31 December 2022 for the Government of the Republic of Zambia.**

	K'million	K'million
Salaries – Super scale	6,760	
Salaries – Division I & II	2,010	
Salaries – Division III	230	
Administrative cost	3,350	
Conferences and seminars	1,260	
Fines		150
Foreign travel	750	
Fees and charges		310
Social benefits	1,040	
Fuel levy		700
Domestic debt interest	1,450	
Grants		430
External debt interest	1,740	
Purchase of vehicles	250	
Treasury bills		11,120
Purchase of equipment	410	
Government bonds		13,460
Euro bonds		7, 460
Bilateral and multilateral debt		19,660
Construction of infrastructure	560	
Cash and bank	2,470	
PAYE		7,330
Corporation tax		5,010

VAT		2,320
Other expenditures	910	
Accumulated fund	44,760	
	67,950	**67,950**

(b) **Statement of financial performance for the consolidated fund for the year ended 31 December 2022.**

Details	**K'million**	**K'million**	**K'million**
Revenues			
Tax Revenue			
PAYE	7,330		
Corporation tax	5,010		
VAT	2,320		
		14,660	
Non-tax revenue			
Fines	150		
Fees and charges	310		
Fuel levy	700		
		1,160	
Domestic and external financing			
Treasury bills	11,120		
Government bond	13,460		
Euro bonds	7,460		
Bilateral and multilateral debt	19,660		
		51,700	
Grants			

Grant		430	
Total revenues			**67,950**
Expenditures			
Uses of goods and services			
Administration cost	3,350		
Conferences and seminars	1,260		
Foreign travel	750		
		5,360	
Personal emoluments			
Salaries - Super scale	6,760		
Salaries – Division I&II	2,010		
Salaries – Division III	230		
		9,000	
Financial charges			
Domestic debt interest	1,450		
External debt interest	1,740		
		3,190	
Non-financial assets			
Purchase of vehicles	250		
Purchase of equipment	380		
Construction of infrastructure	560		
New health equipment - Matero	30		
		1,220	
Other expenditures **Social benefits**		910 1,040	

Total expenditure			**20,720**
Surplus			**47,230**

(c) **How the Government of the Republic of Zambia accounts for revenues and expenditure.**

- After the Zambia Revenue Authority and other collecting agencies have collected tax and non-tax revenue, it is transferred into the consolidated account at Bank of Zambia.
- The expenditure documents are sent to the Ministry of Finance and National Planning for consolidation.
- Accounting for both revenue and expenditure involves making the list of income and expenses recorded when a cash transaction occurs.
- Transactions are entered into the books of accounts. Thus, the rules of debit and credit depend on the nature of an account.
- All the accounts are classified into assets, liabilities, income/revenues, expenses, capital gains/losses.
- Transactions are then entered into the sub-ledgers
- General ledger contains all the accounts for recording transactions.

SOLUTION TWO

(a) **The main objectives of public sector accounting include:**

- Providing how actual performance may be compared with targets so as to ascertain to what extent the public receives value from those that are tasked with the responsibility to serve them,
- Highlighting the various sources of revenue and the expenditure to be incurred,
- Facilitating the appraisal of management over their stewardship,
- Ensuring that public services are rendered in a cost-effective manner, that is, costs are matched by the equivalent benefits accruing to beneficiaries of services,
- Identifying the sources of funding capital projects,
- Evaluating the economy, efficiency and effectiveness with which public sector organization pursue their goals and objectives.
- Providing solutions to various bottlenecks and/or problems identified,
- Providing the details of outstanding long term commitments and financial obligations,
- Assisting planning and control of service provision,
- Enhancing the appraisal of the efficiency of management.
- Providing the basis for decision making,
- Ascertaining the legitimacy of transactions and their compliance with established norms, regulations and statutes.

(b) **Internal users and their information needs**

Internal users of financial information are individuals with a direct bearing on the operations of government. These include:

- The president and ministers
- The National Assembly/parliament
- Regulatory and oversight bodies, audit institutions etc.
- Top public administrators such as permanent secretaries, heads of departments
- Chief executives of parastatals
- Labour unions

This group's information needs include:

- Information for smooth running of their operations and this information is required to make business decisions
- Information to provide them with a more comprehensive view of the public sector financial position and financial analysis.
- Information is required in order to ascertain the various levels of regulatory compliance and whether actual expenditure is in line with budget
- Information to ascertain the adequacy of safeguards for protection of public resources.

External users and their information needs

External users are individuals or institutions with no direct bearing on the operations of the government. They include:

- Members of the public
- Companies doing business with government
- Foreign countries
- Financial institutions such as World Bank, IMF, Commercial Banks etc.
- Creditors, both local and foreign
- Investors
- Researchers
- Political parties, trade unions, civil society organizations

The group's information needs are:

- Information to determine viability of public sector institutions and the efficiency and effectiveness of management.
- Financial institutions and investors use financial information to make decisions about doing business with public sector institutions or whether to invest in government bonds or treasury bills
- Rating agencies use this information to assign credit ratings.

SOLUTION THREE

(a)

(i) **Public debt**

Public debt or government debt or sovereign debt is debt owed by the central government. Government debt may also refer to the debt of the state, municipal or local government.

The government usually goes into borrowing when its expected revenue is less than expected expenditure in any budget year so that the debt is used to finance the budget.

Government debt is a one way of financing the government budget, and hence its operations.

Government usually borrows by issuing securities such as government bonds and treasury bills. It may also borrow from the world bank or international financial institutions.
In a broader perspective, government debt may include all other liabilities of the state including outstanding pension payments.

(ii) **Public revenue**

This refers to revenue received by the government from various sources such as taxes levied on the incomes and wealth accumulation of individuals and corporations and on the goods and services produced, exports and imports, non-taxable revenue sources such as fees, charges, fines etc. Government or public revenue also includes income generated by government owned enterprises, Central Bank and capital receipts in the form of external loans and debts from international financial institutions.

Public revenue is used by the government to finance public administration's operations.

(iii) **Public expenditure,**

Public expenditure is spending made by the government of a country on public goods and services such as roads, railway lines, telecommunications, other infrastructures etc. public expenditure is aimed at providing maximum welfare to the people unlike private spending that aims at maximizing profit and shareholder wealth.
Public expenditure may be called real spending. This involves spending by the government to buy goods and services, for example, medicines for hospitals, desks

for schools, houses for law enforcement departments such as Zambia Air Force (ZAF), Zambia Army (ZA), Zambia National Service (ZNS), Zambia Police (ZP) etc. Other public spending may be called transfer payments. This may include unemployment benefits, child benefits, state pension, investment grants etc. transfer payments are so called because it transfers income from one group of people (tax payers) to another group of people.

(iv) **Public sector financial management**

This basically deals with all aspects of resource mobilization, allocation and expenditure management in government. Just as managing finances is a critical function of management in any organization, public finance management is an essential part of the government's governance processes.

Public finance management includes resource mobilization, prioritization of programs, the budgetary process, efficient management of resources and exercising control by checking that resources allocated to various projects are being utilized as per intended plans.

Rising aspirations of people are placing more demand on financial resources. Further, the emphasis of the citizenry is on value for money, thus making public finance management increasingly vital.

The following subdivisions form the subject matter of public finance (add required content).

(b) (i) **Comparability**

Comparability is an accounting information characteristic to enhance their usefulness to users of accounts. It entails that financial information from one period to another must have been prepared on the same basis, using same accounting policies if performance from one period to another is to be fairly measured.

Practical example

If government measures its inventories of materials in one year using FIFO method, it needs to maintain the same method for subsequent years unless changing makes information more reliable.

(ii) **Periodicity concept**

This concept states that while true performance of the public sector can best be measured at the end of its lifespan, there is need to measure performance at some agreed time intervals as waiting for end of government lifespan may be impracticable for purpose of continuous improvement of public sector operations.

Practical example

Public sector requires quarterly performance reports from line ministries. Some activities have seasonal characteristics control of such factors is often elusive. Reporting performance on quarterly basis would improve control.

SOLUTION FOUR

(a) **Five (5) qualitative characteristics of useful financial information.**

(i) **Understandability**
Taking into account that users have a reasonable knowledge of business and a willingness to study information with reasonable diligence, the General-Purpose Financial Reports (GPFRs) of public sector should be prepared in such a way as to be easily understood and meet the needs of the users.

This can be enhanced when information is classified, characterized and presented in the manner that avoids use of words that are too technical.

All efforts should be made to represent economic and other phenomena included in GPFRs in a manner that is understandable to a wide range of users. However, information should not be excluded from GPFRs solely on grounds of being complex or too difficult for users to understand.

(ii) **Comparability**
Comparability enables users to identify similarities in, and differences between, two sets of phenomena. Consistent application of accounting principles, policies and basis of preparation to prospective financial and non-financial information and actual outcomes will enhance the usefulness of any comparison of projected and actual results.

Inconsistent methods of accounting for similar transactions will render the financial results incomparable.

(iii) **Timeliness -** Every time financial statements are to be prepared, they need to be prepared more quickly in good time for their use for specified decisions to be passed. It means having information available for users to use before it loses its capacity to be useful for accountability and decision-making purposes.
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.

(iv) **Verifiability**
Verifiability is a quality of information that helps assure users that information in GPFRs faithfully represents the economic phenomena that it purports to represent.

Financial statements need to be supported by written or verbal representation for them to be deemed valid and hence useful.
It implies that different knowledgeable and independent observers could reach general consensus, although not necessarily complete agreement, that either the information is free from material error or appropriate recognition, measurement, or representation method has been applied.

(v) **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.

(vi) **Faithful representation –** Information should represent economic reality or phenomena that it purports to represent It must be complete, neutral and free from material error. Substance over form is implied.

(b) **Key constraints on information included in General Purpose Financial Reports.**

(i) Materiality
(ii) Cost benefit
(iii) Balance between the qualitative characteristics.

(c) **The elements of financial statements are as follows:**

Asset	Present resources controlled by a public sector entity. For example buildings, roads, motor vehicles etc.
Liability	Present obligation of a public sector entity whose settlement will result in the outflow of economic benefits. For example, outstanding pension payments, outstanding salaries, outstanding loans, water and electricity bills etc.
Income	Increase in economic benefits during an accounting period. For example, cash collected or expected to be received in form of aid, tax revenue and other fees and charges.
Expenses	Decrease in economic benefits during an accounting period. For example expenditure on wages and salaries on government employees, spending on electricity and water etc.
Accumulated fund	The difference between the total assets and total liabilities of a public sector entity

SOLUTION FIVE

(a) **public debt management**

- Dealing with complex concerns requiring highly trained staff and software to manage the debt.
- Debt management has an integral relationship with IFMIS as it often provides budget resources to carry out such capital intensive programs. Working out what money is due for repayment and when, needs to be built into the budget planning and cash flow projections to ensure that funds are available and that penalties for late payment are avoided.
- The accounting function records the transactions that that reduce or increase debt, reports on debt transactions and provides consolidated report on debt liability.
- At the same time, actual payment takes place in the cash management system.
- Facilitate record keeping on debt.
- Makes it easy to track the debt levels.
- Enhances audit trails.

(b) **Five fundamental principles:**

(i) **Integrity**

This principle entails that a professional accountant should be straight forward and honest in all professional and business relationships. It also implies fair dealing and truthfulness

Actions that entail breach of principle

When an accountant presents false information in accounts with full consent of its falsehood or omits information from accounts knowing very well that users are likely to be misled by such omission.

(ii) **Objectivity**

A professional accountant should not allow bias, conflict of interest or undue influence of others to override professional or business judgements. This means that an accountant is obliged not to compromise their professional or business judgement because of influence of others especially their supervisors

Actions that entail breach of principle

If a supervisor to an accountant is entitled to a bonus based on a particular performance of the reports and entices the accountant to massage figures with a promise to share bonus with them. The accountant ought to apply all means at their disposal to get themselves out of the situation as prescribed by IES 4.

(iii) **Professional competence and due care**

A professional accountant has a continuing duty to maintain professional knowledge and skill at the level required to ensure that a client or employer receives competent professional service based on current developments in practice, legislation and techniques. A professional accountant should act diligently and in accordance with applicable technical and professional standards when providing professional service.

Actions that entail breach of principle

An accountant who shows ignorance of technical knowledge and or advises client wrongly purporting to be reporting the truth.

(iv) **Confidentiality**

A professional accountant should respect the confidentiality of information acquired as a result of professional and business relationships and should not disclose any such information to third parties without proper and specific authority unless there is a legal or professional right or duty to disclose. It further says that confidential information acquired as a result of professional and business relationships should not be used for the personal advantage of the professional accountant.

Actions that entail breach of principle

When a professional accountant discloses information to third parties without consent from business or if such information is used for accountant's own personal gain.

(v) **Professional behavior**

A professional accountant should comply with relevant laws and regulation and should avoid any action that discredit the profession. The principle of professional behavior imposes an obligation on professional accountants to comply with relevant laws and regulations. For instance, in marketing and promoting themselves and their work, professional accountants should not bring the profession into disrepute.

Actions that entail breach of principle

If an accountant makes exaggerated claim for services rendered, the qualifications they possess or experience gained.

END OF SOLUTIONS

PUBLIC SECTOR FINANCIAL MANAGEMENT PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

PFM 2: LEGAL ASPECTS OF PUBLIC SECTOR FINANCE AND ADMINISTRATION

FRIDAY 16 JUNE

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

INSTRUCTIONS TO CANDIDATES

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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.

<u>QUESTION ONE</u> – (COMPULSORY)

(a) Gandhi defines Law as, "a body of rules laid down for guidance of human conduct imposed by some authority which makes it a command of the authority and is enforced." In harmony with the above definition, discuss the functions of Law in society.

(15 marks)

(b) It is said that, "the Constitution is a **Special Act** as it is a contract between the governor and the governed." Putting into contemplation the above statement, explain what makes it special. (15 marks)

(c) The Constitution of Zambia has established three (3) institutions which are collectively known as Government. Each of the three (3) are established under a separate part of the Constitution and they all perform distinct functions. Give a concise explanation of the functions of these institutions. (10 marks)

[Total 40 Marks]

SECTION B

There are FOUR (4) questions in this section. Attempt THREE (3) questions.

QUESTION TWO

(a) Describe the nature of an administrative body/agency. (5 marks)

(b) Identify at least two (2) administrative agencies and their sources of power. (5 marks)

(c) Explain the importance of the administrative agencies identified in (b) above in public sector finance and administration. (5 marks)

(d) Define judicial review and explain briefly its relevance in public sector finance and administration. (5 marks)

[Total: 20 Marks]

QUESTION THREE

Give a detailed explanation of the Legal Regulatory Framework of the following:

(a) The Zambia Revenue Authority (10 marks)

(b) The Public Procurement Authority (10 marks)

[Total: 20 Marks]

QUESTION FOUR

(a) Discuss in detail the differences between constitutional law and administrative law. (10 marks)

(b) Explain the meaning of "public body" for judicial review purposes. (10 marks)

[Total: 20 Marks]

QUESTION FIVE

(a) Making reference to decided cases, discuss the principle of judicial review. (5 marks)

(b) Discuss the brief facts of the case of R **v Panel on Mergers and Takeover ex parte Detafin.** (5 marks)

(c) Explain the three (3) grounds on which an application for judicial review would be brought before the courts of law? (5 marks)

(d) Write notes on how the following remedies operate in judicial review applications.

(i) Certiorari (quashing order) (2½ marks)

(ii) Mandamus (mandatory order) (2½ marks)

[Total: 20 Marks]

END OF PAPER

PFM 2: LEGAL ASPECTS OF PUBLIC SECTOR FINANCE AND ADMINISTRATION SUGGESTED SOLUTIONS

SOLUTION ONE

(a)

(i) To promote Justice
(ii) To preserve peace and order.
(iii) To enforce morality

(b)

(i) Its creation
(ii) It is an important document of a state
(iii) It is the Supreme law

(c)

Functions of the **Executive**

(i) Execute laws made by the legislature.
(ii) Formulate laws for the approval of the legislature.
(iii) To prepare the budget for the approval of the legislature and determine the rates of taxation and other revenue rising.
(iv) To handle foreign policy and relations.
(v) The operational command of the military.

Functions of the **Judiciary**

(i) Interpret laws which apply to Zambia (Constitution and Statutes).
(ii) Insure impartial justice under the law.
(iii) Provide mechanism for dispute resolution.
(iv) Administration of justice through resolving disputes between individuals or between individuals and the state.

Functions of the **Legislature**

(i) Make new laws.
(ii) Amend existing laws.
(iii) Repeal laws
(iv) Approve appointments made by the Executive.

Approve the budget prepared by the executive.

SOLUTION TWO

(a) Administrative agencies, also known as administrative bodies are defined as, government bodies created by statute with functions of performing public administrative functions. These bodies are created to bring about efficiency in the delivery of public administrative functions by the executive arm of government whose function is to perform administrative functions.

(b) (i)There are a number and any one properly identified as an administrative body suffices otherwise mainly would be; the Zambia Revenue Authority whose source of power is the Zambia Revenue Authority Act Cap 321. The Act provides for the establishment of the Authority, provides for its legal framework, the governing board, the functions and powers it has in the execution of its functions. The Authority has been given all the powers of raising the revenue of the country and in so doing it is to perform those functions in accordance with the Act of Parliament establishing it. Anything the Authority does which is not meant for the authority to do therefore is ultra vires and would be adjudged null and void by the courts.

(ii) The Public Procurement Authority (formerly Zambia National Tender Board) established under the Public Procurement Act Cap 309. The PPA is another one of the bodies established to perform public administrative functions of procuring services on behalf of the government. Previously the functions performed by this body were done under the Ministry of Works and Supply but in order to bring efficiency in public sector procurement, the Authority which was a board in the Ministry was established with the main purpose of ensuring transparency, accountability in public sector procurement and regulate and control practices in public procurement so as to promote integrity, fairness and public confidence in the procurement process in the public sector.

(c) The Zambia Revenue Authority and the Public Procurement Authority are very important in public sector finance and administration. First, the Zambia Revenue Authority raises all the public funds for use by the government. The government not being a profit making body relies on taxes for all governmental functions. The authority is therefore an important partner in the raising of revenue to enable the government deliver services such as health, education etc to the people. Without the authority therefore it would be very difficult for the government to collect the public sector finances needed to executive all administrative functions performed by the executive. The Public Procurement Authority is cardinal in that it has made the use of public funds to be transparent and created some level of accountability in the manner government officials spend funds. As a body regulated by law, the authority is guided by the principles of fairness, promotion of integrity thereby building confidence in the general public that monies collected in taxes may be used for the proper procurement of services by the government which are meant to benefit the people and corruption in the process is curtailed to some extent. The two bodies are therefore important components of public sector finance and administration as they operate under administrative law which guides them in the collection of revenues for the government and on how the revenues collected are actually spent for the benefit of the tax payer. Because they are established under Acts of Parliament, their powers are limited by provisions of the

Acts establishing them so that any conduct outside the law establishing them, is adjudged *ultra vires* and therefore void.

(d) Judicial review is the mechanism by which public administrative bodies are brought before the courts of law to see whether their actions have been performed in accordance with the law and whether they actually have the legal authority to perform the functions they perform. It is a very useful tool for checking *intra* and *ultra vires* conduct on the part of public administrative bodies. Judicial review looks at the process leading to a decision made to ensure that the body making the decision in fact has the legal authority to make the decision made and to ensure the procedures as laid down by law are actually followed. If any one of the two does not exist, the body is said to have acted *ultra vires* and the body is either ordered to go back to the process of making the decision where the *ultra vires* is failure to follow the procedure or to completely quash the decision where the *ultra vires* is lack of legal authority to make the decision made. *Attorney General v Fulham Corporation and Kang'ombe v the Attorney General.* Judicial review therefore ensures arbitrariness in public sector finance and administration is curb thereby promoting accountability of public funds.

SOLUTION THREE

(a) Generally, like any other Administrative Institution, ZRA resolves its legal issues via Judicial Review which mainly looks at the powers conferred on a body and assessing whether the body has acted within the powers or where the power exists, assessing whether the procedure as laid down in a statute has been followed by the when performing its functions. Aside from judicial review, ZRA also has a tribunal. This is created under The Revenue Appeals Tribunal Act; By S 190 (1) of the Act, any person who is aggrieved by the decision or determination made by the Commissioner-General under the Act or under any regulation, or rules made under this Act, may in respect of the matter set out an appeal to the Tribunal in such a manner and within such time as the Minister may by regulation prescribe.

(b) As a public body, PPA is amenable to judicial review as means of regulating functions. Aside from that, the Public Procurement Authority Act 2008 and Public Procurement Authority Act 2008 and subsidiary legislation such as Statutory Instrument No. 63 of 2011 and the Public Procurement Regulations 2011 all contain regulatory frameworks under which the authority is to operate.

SOLUTION FOUR

(a) The **difference between Administrative law and Constitutional Law** is that administrative law is subordinate to Constitutional law.

- In contrast, Constitutional law is the highest law in Zambia and is considered supreme.
- Constitutional law is responsible for dealing with various state organs, and Administrative law is concerned with the organs of the state in motion.
- The reach of constitutional law is greater. For instance, it concerns people, governments, and human rights.
- However, administrative law is more specialized.
- While administrative law provisions are not as well recognized as constitutional law since they are not incorporated in a single text like the constitution, they are generally understood and explicitly stated in the constitution.

(b) Judicial review will not lie against a body or person performing private functions (Law v National Greyhound Racing Club Limited [1983] 3 All ER 300). In **Dr. Ludwig Sondashi v Brigadier General Godfrey Miyanda, MP (Sued as National Secretary of the Movement for Multi-Party Democracy) (1995- 1997) Z.R. 1** Judicial review would therefore not be the correct procedure when the decision challenged is not a public law decision. MMD party was held to be a club ad therefore to subject to judicial review.

SOLUTION FIVE

(a) The principle of judicial review as outlined in *Nyampala Safaris v Zambia Wildlife Authority* [2004] is that, "judicial review does not concern itself with the merits of the decision made by a body but by the process leading to the decision and having established that either the process was followed or the law existed giving the body authority to make the decision it made, it ends there and it is not the job of the court to substitute their decision for that made by a body". The statement clearly shows that judicial review does not look at the decision made but at the process leading to the decision to ensure the body acted according to the procedures laid down, and the body has the legal authority to make the decision made. If the body acted *intra vires*, the courts have no authority to interfere.

(b) Ordinarily a public body is one which is a creature of statute or established by or under an Act of Parliament. However since 1987, the court widened the interpretation of what a public bodies. *R v Panel on Mergers and Take-Over ex parte Datafin*. In the case the court ruled that the ordinary way to determine whether or not a body is a public body is to look at the source of its powers. It is usually the case that a public body will derive its powers from an Act of Parliament establishing it. However, a public was also qualified as a public body if the functions it performed were of a public nature or had public law consequences regardless of whether or not it is a creature of statute or, if, in the absence of that body which ordinarily is a private body, but because of the nature of functions its performs, the government would have seen it necessary to establish a body to perform the functions it performs then that body even though its source of power is not an Act of Parliament, will be brought within the ambit of a public body for judicial review purposes.

(c) The three grounds are: illegality, procedural impropriety and wednesbury unreasonableness. Illegality means a body does not in fact have the legal authority to make the decision it has made. In such instances, the decision of the body is quashed and would not have any effect. *William Harrington v Dora Siliya and the Attorney General* where the tribunal established to probe Hon. Siliya's alleged breaches of the Parliamentary and Ministerial Code of Conduct Act proceeded to venture into the constitution. The High Court held that the tribunal acted *ultra vires* as it did not have the legal authority to venture into the constitution as its jurisdiction was clearly matters relating to a breach of the Act of Parliament.

Procedural impropriety – in such instances, a body has acted procedurally wrong with regard to the procedure as laid down by the Act of Parliament establishing it and giving it the authority to perform public administrative functions. *Bedford Kango'mbe v The Attorney General*. The applicant a teacher was dismissed from the teaching service without proper procedures as laid down by law being followed. On an application for judicial review, the decision of the then President Kaunda was said to be *ultra vires* the law which required a person's dismissal to be recommended by the teaching service commission and the President was on to act on the recommendation of the commission and did not have the power to go contrary to the commission's findings.

Wednesbury unreasonableness – here the applicant is not contending that the body did not have the legal authority to make the decision it has made or that the procedure as laid down in the law was not followed but that, in making the decision, the body took into account certain trivialities it ought not to have taken into account that a reasonable person would not have taken into account or that the body failed to take into account certain factors it ought to have taken into account that a reasonable person would have taken into account and as a result of that, the bodies decision is so outrageous in its defiance of logic that a reasonable person would not have made the decision made by the body. Under this ground, if established that indeed the decision is unreasonable, the body would be ordered to go through the decision making process and either not take into account what would be considered trivialities or to ensure it takes into account what it failed to take into account whether or not the decision it makes after comes out the same. *Associated Provincial Picture Houses v Wednesbury Corporation*. The grounds of procedural impropriety and wednesbury unreasonableness have the same effect whereas illegality the effect is different.

(d) (i) Certiorari (quashing order) – this is one of the remedies in an application for judicial review. A quashing order has the effect of completely nullifying a decision made by a public body. This ground is available where a body exceeds the legal authority it has to make a decision made and therefore means the decision it has made has no backing of the law and therefore made arbitrarily. Therefore from the very beginning, the decision is wrong and, because the body has no legal authority to make the decision, it will not be asked to start from the beginning and make the decision notwithstanding the decision to be made. The body cannot at all be allowed to make that decision. *William Harrington v Dora Siliya and Attorney General; Attorney General v Fulham Corporation*.

(ii)Mandamus (mandatory order) this is a remedy available in judicial review where a body fails to follow procedure as outline in the law. A body that fails to follow the procedure stipulated by law is said to have acted arbitrarily and the decision it makes will not be valid although equally, will not be quashed. However, the courts will order the body to go back to the decision making process all over and follow the procedures as stipulated by law. Under this remedy which comes mainly due to want of procedure, it does not matter if the decision to be made by the body after having followed the correct procedure is the same as that made through want of procedure. What matters therefore is that the body is acting in accordance with the law and there is no arbitrariness in the manner the body makes decisions the law has given it authority to make. *Bedford Kango'mbe v Attorney General*

END OF SOLUTIOINS

Zambia Institute of Chartered Accountants

PUBLIC SECTOR FINANCIAL MANAGEMENT PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

PFM 3: GOVERNANCE AND MANAGEMENT IN PUBLIC SECTOR

TUESDAY 13 JUNE 2023

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 (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.

<u>QUESTION ONE</u> – (COMPULSORY)

WHOLE FOODS MARKET DILEMMA

Whole Foods Market has been declining in performance in the market for the last two (2) years. Due to this, the activist hedge fund that owns almost 9% of the common stock is pressuring the former. The activist hedge fund is eyeing the reform of the management style of the executive officers as it asserted that they are the ones responsible for the poor results achieved by the Whole Foods Market. In other words, the CEO of the Whole Foods Market is in trouble of losing his position and he must come up with the strategic direction for the company.

A few days ago, Amazon's CEO reached out to Whole Foods Market. It was expected as many news outlets reported that Amazon is interested in acquiring the latter for opportunities in the retail sector.

The reason why the Whole Foods Market is a good candidate for Amazon to acquire is its attractive value and strategic deal. Amazon expects that it can guarantee a substantial premium. The first signal of commitment by Amazon is the face-to-face meeting with the Whole Foods Market's CEO. Moreover, Amazon just launched a new service called Amazon-Fresh that fits perfectly with what Whole Foods Market has developed which is the local-based fresh-goods delivery system.

Most negotiators face challenges within themselves thinking about what to offer, what is the reasonable agreement to accept, and the real interest in the negotiation but it is important to compute the reservation price (RP). For this, you would need high-velocity decision-making because time is important in negotiations and the time you will need to decide is crucial.

Additionally, a profitable outcome depends on how negotiators deal and discuss during the negotiation process. Being an active listener and discussing issues is pivotal in the negotiation to be successful.

In the negotiation, Amazon has the upper hand as it has the capability to inflict damage on Whole Foods Market by not pursuing the negotiation. The threats looming the Whole Foods Market will cease if it collaborates with Amazon.

Additionally, Amazon demands secrecy. Any leakage will force Amazon to terminate the negotiation. In bidding situations, secrecy is important. Any leak of confidentiality will have disastrous outcomes regarding the agreements. A non-disclosure will allow Amazon to have steadiness, speed, and information symmetries in the negotiation.

Source: www.thecasecentre.org/products

Required:

(a) State any five (5) key skills for negotiations. (10 marks)

(b) What is a Reserve Price and why is it important in negotiations. (7 marks)

(c) In the scenario cited above, discuss how both Whole Foods and Amazon negotiating teams can manage to get the best deal. (15 marks)

(d) Discuss any four (4) areas of decision making that should be considered '**strategic**'. (8 marks)

[Total: 40 Marks]

SECTION B

There are FOUR (4) questions in this section.

Answer Any Three (3) Questions in this section.

QUESTION TWO

(a) Define management. (2 marks)

(b) Explain the four (4) key management functions. (8 marks)

(c) Conflicts are normally viewed as bad and /or negative, however, it should be noted that conflicts can sometimes be good in organizational settings as they may bring about better ideas of how to do things, resolve long standing problems, or bring clarifications of individual views.

Required:

Discus the five (5) conflict resolution strategies which can be used for minimizing and resolving conflicts**.** (10 marks)

[Total: 20 Marks]

QUESTION THREE

(a) List the functions of managements according to Henri Fayol. (5 marks)

(b) Draw a MATRIX organization structure and give three advantages for this form of structure in project implementation. (15 marks)

[Total: 20 Marks]

QUESTION FOUR

Discuss the activities associated with Contract life Cycle. (20 marks)

[Total: 20 Marks]

QUESTION FIVE

'An Act to revise the law relating to procurement so as to enhance transparency, efficiency, effectiveness, economy, value for money, competition and accountability in public procurement; regulate and control practices relating to public procurement in order to promote the integrity of, fairness and public confidence in, the procurement process; promote the participation of citizens in public procurement; continue the existence of the Zambia Public Procurement

Authority; repeal and replace the Public Procurement Act, 2008; and provide for matters connected with, or incidental to, the foregoing". *(Public procurement Act 2020)*

Required:

(a) What are the duties of a procurement Manager? (5 marks)

(b) Discuss Five (5) functions of a manager postulated by Henry Fayol (15 marks)

[Total: 20 Marks]

END OF PAPER

PFM 3: GOVERNANCE AND MANAGEMENT IN PUBLIC SECTOR SUGGESTED SOLUTIONS

SOLUTION ONE

(a) State any Five (5) key skills for negotiations

Key skills for negotiating requires:

(i) Preparation and planning skills
(ii) Knowledge of the subject matter
(iii) Ability to think clearly and rapidly and under pressure and uncertainty
(iv) Ability to express thoughts verbally
(v) Listening skill
(vi) Patience general problem solving and analytical skills

(b) What Is a Reserve Price and why is it important in negotiations

A reservation price is the minimum amount that a seller will accept as the winning bid. Alternatively, it is less commonly known as the highest price a buyer is willing to pay for a good or service.

It important knowing the reservation price in negotiation because:
Knowing your reservation price – the highest price you would pay in the negotiating scenario – can empower you to walk away from a bad deal and seek a better bargain. In any negotiation, your **B**est **A**lternative **T**o a **N**egotiated **A**greement (BATNA) is intimately tied to your reservation price.

(c) In the scenario cited above, discuss how both Whole Foods and Amazon negotiating teams can manage to get the best deal.

(i) Both parties must make an effort to retrieve data from both sides to quantify and evaluate the outcome of every possible solution

(ii) Good negotiator must anchor the positioning battle around the reservation price. It is important to consider the other party's perspective to take action in their situation rather than our own.

(iii) Building trust with information and interest with the other party creates a fruitful negotiation process.

(iv) Good deal is made when both parties meet on the same ground and terms.

(v) Professional ethics in the negotiations must be observed by both parties.

(d) Discuss any four (4) areas of decision making that should be considered '**strategic**'.

The four (4) areas of decision making that should be considered 'strategic' are:

(i) Decisions affecting the **long-term direction** that the business should take. Long-term in practice usually means planning and implementing strategies for up to the next five years or longer.

(ii) Decisions about the **scope of an organization's activities**. This includes decisions about the overall and purpose of the organization and the activities it should undertake.

(iii) For commercial business organizations, strategy should be about gaining some kind of **advantage in competition**. Business operates in a competitive environment.

(iv) Strategic management in some organizations takes the form of **adapting the activities of business to fit the environment** in which it operates. An example of this is making decisions to change products and services that the business produces to meet the changing requirements its customers.

(v) A different approach to strategy is to **exploit unique resources** and the **special competences** of its employees.

Strategic decisions are affected by the **values and expectations** of all the organization's **stakeholders** and should take into consideration the expectations of the major stakeholders.

SOLUTION TWO

(a) **Define 'Management**.'

Management is the coordination and administration of tasks to achieve a goal. Such administration activities include setting the organization's strategy and coordinating the efforts of staff to accomplish these objectives through the application of available resources. Management can also refer to the seniority structure of staff members within an organization.

Management is the process of planning and organizing the resources and activities of a business to achieve specific goals in the most effective and efficient manner possible. Efficiency in management refers to the completion of tasks correctly and at minimal costs. Effectiveness in management relates to the completion of tasks within specific timelines to yield tangible results.

(b) **Explain the four key management functions.**

(i) **Planning:** Effective planners employ strategies to help them accurately identify important tasks and their priority levels and determine appropriate timelines to complete them. This includes carefully assessing time frames and deadlines that are appropriate.

(ii) **Organizing:** Effective resource coordination is a foundational requirement for any business or team's future success. Disorganized managers result in employees being shuffled around and resource bottlenecks, which are both highly disruptive to any team's goals. Organizing includes defining and classifying activities. Before assigning a single employee, clearly define the goals and duties associated with each position.

(iii) **Leading:** Effective leadership isn't hard science, but there are key principles that most great leaders put into practice.

-Create a shared vision. Align the success of the team with that of the individual.
-Establish a positive team culture
-**Lead by example.** Exemplify the qualities that you want your team to have.

(iv) **Controlling:** Controlling is all about making sure that objectives are met and understanding how to make appropriate adjustments when issues arise. It includes setting concrete standards so that you can actually determine if a particular goal has been met. This is especially important to do for project milestones. You need to develop a strategy so that managers in each department can continually monitor workers' work quality and performance.

(c) Conflicts are often viewed as bad and/or negative, however, it should be noted that conflicts can sometimes be good in organizational settings as they may bring about better ideas of how to do things, resolve long standing problems, or bring clarification of individual views.

Discuss the Five (5) conflict resolution strategies which can be used for minimizing and resolving conflicts

(i) **Accommodating:** Accommodating refers to when one party gives in to the wishes of another. While this is a way of being cooperative in a team dynamic, it lacks assertiveness. Often professionals who prefer to avoid conflict use this strategy as a reflex reaction to keep the peace. They must work hard to train themselves to not over-rely on this conflict resolution strategy and be open to more constructive problem-solving methods.

Accommodating is useful when the benefits outweigh the consequences. However, it's important to implement this method sparingly. Too much accommodation can give rise to authoritarian leaders who hamper innovation.

(ii) **Avoiding:** Avoiding is when people ignore or withdraw from a conflict entirely. Like the accommodating method, professionals who fall back on avoiding a situation are uncomfortable with confrontation. They believe the consequences exceed the reward, so avoiding a conflict is the best option to facilitate harmony.

While sometimes avoiding conflicts can maintain business ties, the method prevents you from contributing anything of value. Avoiding stifles creativity and unconventional thinking. An organization that reinforces a culture of avoiding conflict harms itself because it discourages people from sounding the alarm on potentially dangerous issues.

(iii) **Compromising:** Another conflict resolution strategy is compromising. Professionals who use this method balance assertiveness and cooperation. They try to work in the best interests of both parties because everyone agrees to sacrifice something for the greater good. We often view compromise as the fairest action, even if no one leaves a negotiation particularly happy. It's also a useful temporary solution that allows you to consider a more suitable alternative.

While compromise can resolve conflicts effectively, it may force you to make tough decisions. As a general rule in business, qualities like ethics, integrity and trustworthiness are compromises you should avoid.

(iv) **Collaborating:** Collaborating means working with others towards a mutually agreeable resolution. In a team dynamic, leaders delegate tasks equally, giving each individual a chance to contribute their skills and experience.

Collaboration ensures everyone actively participates in the solution when dealing with a conflict. Unlike the compromise method, where both parties may feel they have to sacrifice something, collaboration encourages you to work out a solution that everyone can support. For example, a salesperson and a customer may collaborate on the terms of a contract until both sides find it acceptable.

(v) **Competing:** Competing is a conflict resolution method people use when they go into a conflict with a plan to win. Strong personalities in the workplace often rely on this method. You can't avoid them because they aren't afraid to express their opinions. Sometimes it can also be difficult to collaborate and compromise with them because their goal is to press for their agenda at any cost. Competing may work in sports, but it's rarely a good strategy for group problem-solving.

In the workplace, it's often a symptom of people feeling unheard. It doesn't allow for diverse perspectives to inform a total picture.

SOLUTION THREE

(a) List the functions of managements according to Henri Fayol

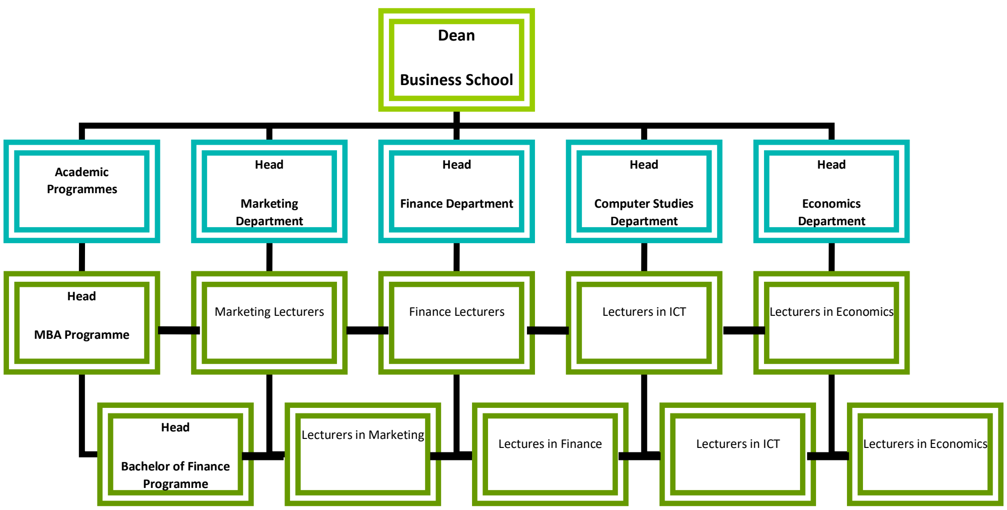
(i) Planning

(ii) Organizing

(iii) Leading (directing)

(iv). Controlling

(b) Draw a MATRIX organization structure and give three advantages for this form of structure in project implementation.



Advantages

(i) Decision making is decentralised to a level where information is processed properly and relevant knowledge applied.

(ii) Extensive communications networks help develop process large amounts of information.

(iii) With decisions delegated to appropriate levels (project level) higher management levels are not overloaded with operational decisions.

(iv) Resource utilisation is efficient because key resources are shared across several important programmes or products at the same time.

SOLUTION FOUR

Explain the activities associated with Contract life Cycle.

(i) Planning stage: includes strategic objectives made and converted into approved budgets and operational plans with sufficient details.

(ii) Creation stage: the stage involves preparing the first draft of the contract documentation

(iii) Collaboration stage involves drafting and negotiating the process which includes internal and external reviews to ensure legal effect and financial requirements are agreed with stakeholders.

(iv) Execution stage: this is the act of signing the contract, making it legally enforceable and formalizing the terms of the contract.

SOLUTION FIVE

(a) What are the duties of a procurement Manager?

A Procurement Manager, or Purchasing Manager, oversees a company's sourcing capabilities and supply chain. They are responsible for finding and evaluating suppliers, products and services, negotiating contracts and acquiring the most cost-efficient deals without compromising on quality.

(b) Discuss Five (5) functions of a manager postulated by Henry Fayol

1. Planning: Planning is the first and foremost function of the management process. It is the thinking process to determine the proposed course of action, what, how, when, where and who has to perform the work or things to be done.

2. Organization: Organization as a process institutes the harmonious adjustment between the different factors of production as land, labor, capital of the business enterprise, so that ultimate goal is achieved.

3. Commanding: Commanding is primarily concerned with supervision, regulation, inspiration, inspection and guidance of the activities of the employees in such a manner so as to achieve the pre-determined goals of the organization smoothly.

4. Coordination: Coordination is an understood agreement to achieve predetermined goal of business enterprise utilizing all the factors of production. This lubricates all the concerned activities towards facilitation of work and achieving the desired result. "All these elements will be dealt in with detail in the fore coming posts."

5. Control: Control is that process which keeps the whole system in check so that it moves as per the pre designated parameters or verifying the total movement of the business enterprise as per the plan and adopting corrective measures thereon for any deviation. Apart from the above mentioned five elements, other two elements which are adopted by several managers are as follows:

END OF SOLUTIONS

PUBLIC SECTOR FINANCIAL MANAGEMENT PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

PFM 4: PUBLIC SECTOR FINANCIAL MANAGEMENT

FRIDAY 16 JUNE 2023

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 (2) sections:
   Section A: One (1) Compulsory scenario question.
   Section B: Four (4) Optional scenario 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.

<u>QUESTION ONE</u> – (COMPULSORY)

Country Gutila had the following percentage (%) allocation of each sector for the 2022 budget. The budget was going to be financed by revenues from both tax and non-tax sources, borrowing from foreign and domestic sources (debt management is critical) and thirdly from withdrawals from available cash balances.

FUNCTION	SHARE OF THE BUDGET (%)
General Public Services	40.5
Defense	4.9
Public Order and Safety	3.1
Economic Affairs	20.9
Environmental Protection	0.6
Housing and Community Amenities	0.5
Health	8.4
Recreation, culture and religion	2.3
Education	13.9
Social Protection	4.9
Total	**100**

The preparation of the national budget followed the consolidation of the presentations by the various government spending agencies submission. Further, professional bodies made their written presentations indicating as to what they expected to be considered in the budget.

It was observed that the country had just recovered from the negative impact of the Covid 19 and hence the economy was gradually growing in all sectors, including tourism. The minister of tourism emphasized on the growth of local tourism as well as attracting international tourists.

The agricultural sector was also poised to grow exponentially. Parliament of Gutila country in its sitting unanimously approved, after extensive debate, the establishment of an agricultural bank to specifically address the agriculture sector challenges from working capital and fixed asset investment (e.g. combine harvesters, tractors, harrows and other agricultural equipment) funding to extreme climate changes negatively affecting the industry.

The establishment of an agricultural bank was to be established on Public Private Partnership (PPP) basis. It was reported in Parliament that the Government of Gutila was merely going to facilitate the process and political support in the establishment of this bank.

A supplementary budget was presented, debated and eventually agreed upon by the parliamentarians in April, 2022. This was as a result of the need to reallocate more resources to capital expenditure to address the rebuilding of bridges which were washed away by unanticipated heavy rains experienced in the month of January 2022.

It was further noted that during the fiscal year 2022 and beyond, banking services were going to be enhanced so as to ensure that the various services to the citizens of Cutila are delivered effectively, efficiently and transparently.

As per sector allocation, the defense spending was allocated 4.9% equal percentage with social protection also with 4.9%. During the mid-year review of the budget against actual, it was noted that social protection was over spent as the actual spending stood at 10% over the budgeted amount. On the other hand, the economic affairs was grossly underspent as there were very few activities being implemented under this allocation. These scenarios were noted when the budgetary control reports were prepared and submitted by the controlling officers. It was decided that a virement be implemented between these two expenditure budget items

Required:

(a) Explain clearly the various stages of the Budget Cycle the countries follow. (8 marks)

(b) Explain the term virement and justify its application. (5 marks)

(c) Describe what is meant by a supplementary budget and how does it arise? (6 marks)

(d) Explain how the banking services assist governments in strengthening public sector management of public finances. (10 marks)

(e) Explain clearly as to why debt management is critical and further, identify the various institutional framework within which debt management operates. (11 marks)

[Total: 40 Marks]

SECTION B

There are FOUR (4) questions in this section. Attempt any three (3) questions.

<u>QUESTION TWO</u>

Nitrogen Chemicals company is a government owned manufacturing company. It has a cash deficit of K80 Million at the beginning of July 2023. Assume you are the financial manager of Nitrogen Chemicals company. The Director of finance is concerned with the cash flow position of the company. He has provided you with the following data and estimates so that you could assist him to prepare a cash budget.

	Sales	**Salaries**	**Indirect Expenses**
	K000	K000	K000
July	85,000	15,000	10,500
August	60,000	16,000	11,000
September	70,000	16,500	10,000

The following information is available regarding direct material.

	Opening inventory	**Material usage**
	K000	K000
July	6,000	9,000
August	4,000	10,000
September	7,000	10,500
October	5,500	

NOTES:

1) 20% of sales are for cash, the balance is receivable the following month. The amount received in July for June's sales is K31,500,000.
2) Salaries are paid in the month they are incurred.
3) Indirect expenses include K2,000,000 per month for depreciation. Indirect expenses are settled the month following. K8,000,000 is to be paid in July for June's indirect expenses.
4) Purchases of direct materials are paid for in the month purchased.
5) Equipment of K30,000,000 is to be purchased in August.

Required:

(a) Prepare a cash budget for Nitrogen Chemicals company for July, August and September 2023. (13 marks)

(b) Advise the finance director of seven ways of improving the cash flow position of the company. (7 marks)

[Total: 20 Marks]

QUESTION THREE

A team of experts were identified to carry out a financial evaluation of the successful bidder, Denster Ltd who was selected to develop a business capital project in the south-east province of country Frietle. Denster Ltd was selected after satisfying the evaluating team largely on the technical submission. However, the final decision to award the contract to Denster ltd was going to be based on the outcomes of the financial evaluation. It was agreed by the financial experts that they were going to use the payback period to decide on whether the preferred bidder was going to finally be awarded the contract or not.

Denster Ltd proposed a total investment of K121,800.

The net cash flow projections over a six (6) year period for this investment was projected as follows:

Years	**1**	**2**	**3**	**4**	**5**	**6**
	K'000	K'000	K'000	K'000	K'000	K'000
Net Cash Flows	25,000	18,000	7,800	16,000	50,000	20,000

Required:

(a) Explain is the payback period and its implications? (5 marks)

(b) Distinguish between the Net Present Value (NPV) and the payback period of an investment. (2 marks)

(c) Calculate the payback period of this investment using the cumulative net cash flows. (3 marks)

(d) Advise whether the investment should be accepted or not in the event that financial experts require that the initial investment amount should be recovered in 4 (four) years or less. (3 marks)

(e) State clearly the advantages and disadvantages of the payback method. (7 marks)

[Total: 20 Marks]

QUESTION FOUR

Stakeholders are important in both private and public institutions. Their engagement is critical as their views are highly appreciated in the process of effectively enhancing positive relationships with the organizations, programmes and projects. The relationships with stakeholders should be managed and monitored due to their importance.

Required:

(a) Explain both the direct and indirect influence of stakeholders for a Government Institution. (6 marks)

(b) Discuss the seven (7) principles of stakeholder management. (14 marks)

[Total: 20 Marks]

QUESTION FIVE

Assume you are an accountant in a government hospital. The hospital is currently evaluating its performance for the last quarter against the targets. The purpose of the evaluation is aimed at improving service delivery in the health sector. It's performance is being measured against certain pre-determined criteria.

In addition, assume that you have been informed that as part of your continuing professional development you have been nominated to present a paper at a workshop next month. The workshop will be on performance management in the public sector where you will be discussing the ongoing public sector financial management reforms.

The workshop will be specifically focused on the assessment of public sector financial management performance and the indicators of performance management in the public sector.

Required:

Prepare a paper to be used at the presentation. Your paper should cover the following:

(a) An explanation of five (5) stages of the performance management cycle in the public sector. (10 marks)

(b) Discuss five (5) practical performance measures for the government hospital. (10 marks)

[Total: 20 Marks]

END OF PAPER

Formula Sheet

Economic order quantity

$$= \sqrt{\frac{2C_0D}{C_H}}$$

Miller – Orr Model

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

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

The Capital Asset Pricing Model

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

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

$$P_o=\frac{D_o(1+g)}{(r_e\text{-}g)}$$

Gordon's growth approximation

$$g=br_e$$

The weighted average cost of capital

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

The Fisher formula

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

Purchasing power parity and interest rate parity

$$s_1=S_0 x \frac{(1+h_c)}{(1+h_b)} \qquad f_0=s_0 x \frac{(1+i_c)}{(1+i_b)}$$

Present Value Table

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

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

Discount rate (r)

Periods (n)	1%	2%	3%	4%	5%	6%	7%	8%	9%	10%	
1	0·990	0·980	0·971	0·962	0·952	0·943	0·935	0·926	0·917	0·909	1
2	0·980	0·961	0·943	0·925	0·907	0·890	0·873	0·857	0·842	0·826	2
3	0·971	0·942	0·915	0·889	0·864	0·840	0·816	0·794	0·772	0·751	3
4	0·961	0·924	0·888	0·855	0·823	0·792	0·763	0·735	0·708	0·683	4
5	0·951	0·906	0·863	0·822	0·784	0·747	0·713	0·681	0·650	0·621	5
6	0·942	0·888	0·837	0·790	0·746	0·705	0·666	0·630	0·596	0·564	6
7	0·933	0·871	0·813	0·760	0·711	0·665	0·623	0·583	0·547	0·513	7
8	0·923	0·853	0·789	0·731	0·677	0·627	0·582	0·540	0·502	0·467	8
9	0·914	0·837	0·766	0·703	0·645	0·592	0·544	0·500	0·460	0·424	9
10	0·905	0·820	0·744	0·676	0·614	0·558	0·508	0·463	0·422	0·386	10
11	0·896	0·804	0·722	0·650	0·585	0·527	0·475	0·429	0·388	0·350	11
12	0·887	0·788	0·701	0·625	0·557	0·497	0·444	0·397	0·356	0·319	12
13	0·879	0·773	0·681	0·601	0·530	0·469	0·415	0·368	0·326	0·290	13
14	0·870	0·758	0·661	0·577	0·505	0·442	0·388	0·340	0·299	0·263	14
15	0·861	0·743	0·642	0·555	0·481	0·417	0·362	0·315	0·275	0·239	15

(n)	11%	12%	13%	14%	15%	16%	17%	18%	19%	20%	
1	0·901	0·893	0·885	0·877	0·870	0·862	0·855	0·847	0·840	0·833	1
2	0·812	0·797	0·783	0·769	0·756	0·743	0·731	0·718	0·706	0·694	2
3	0·731	0·712	0·693	0·675	0·658	0·641	0·624	0·609	0·593	0·579	3
4	0·659	0·636	0·613	0·592	0·572	0·552	0·534	0·516	0·499	0·482	4
5	0·593	0·567	0·543	0·519	0·497	0·476	0·456	0·437	0·419	0·402	5
6	0·535	0·507	0·480	0·456	0·432	0·410	0·390	0·370	0·352	0·335	6
7	0·482	0·452	0·425	0·400	0·376	0·354	0·333	0·314	0·296	0·279	7
8	0·434	0·404	0·376	0·351	0·327	0·305	0·285	0·266	0·249	0·233	8
9	0·391	0·361	0·333	0·308	0·284	0·263	0·243	0·225	0·209	0·194	9
10	0·352	0·322	0·295	0·270	0·247	0·227	0·208	0·191	0·176	0·162	10
11	0·317	0·287	0·261	0·237	0·215	0·195	0·178	0·162	0·148	0·135	11
12	0·286	0·257	0·231	0·208	0·187	0·168	0·152	0·137	0·124	0·112	12
13	0·258	0·229	0·204	0·182	0·163	0·145	0·130	0·116	0·104	0·093	13
14	0·232	0·205	0·181	0·160	0·141	0·125	0·111	0·099	0·088	0·078	14
15	0·209	0·183	0·160	0·140	0·123	0·108	0·095	0·084	0·074	0·065	15

Annuity Table

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

Where r = discount rate
n = number of periods

Discount rate (r)

Periods (n)	1%	2%	3%	4%	5%	6%	7%	8%	9%	10%	
1	0·990	0·980	0·971	0·962	0·952	0·943	0·935	0·926	0·917	0·909	1
2	1·970	1·942	1·913	1·886	1·859	1·833	1·808	1·783	1·759	1·736	2
3	2·941	2·884	2·829	2·775	2·723	2·673	2·624	2·577	2·531	2·487	3
4	3·902	3·808	3·717	3·630	3·546	3·465	3·387	3·312	3·240	3·170	4
5	4·853	4·713	4·580	4·452	4·329	4·212	4·100	3·993	3·890	3·791	5
6	5·795	5·601	5·417	5·242	5·076	4·917	4·767	4·623	4·486	4·355	6
7	6·728	6·472	6·230	6·002	5·786	5·582	5·389	5·206	5·033	4·868	7
8	7·652	7·325	7·020	6·733	6·463	6·210	5·971	5·747	5·535	5·335	8
9	8·566	8·162	7·786	7·435	7·108	6·802	6·515	6·247	5·995	5·759	9
10	9·471	8·983	8·530	8·111	7·722	7·360	7·024	6·710	6·418	6·145	10
11	10·37	9·787	9·253	8·760	8·306	7·887	7·499	7·139	6·805	6·495	11
12	11·26	10·58	9·954	9·385	8·863	8·384	7·943	7·536	7·161	6·814	12
13	12·13	11·35	10·63	9·986	9·394	8·853	8·358	7·904	7·487	7·103	13
14	13·00	12·11	11·30	10·56	9·899	9·295	8·745	8·244	7·786	7·367	14
15	13·87	12·85	11·94	11·12	10·38	9·712	9·108	8·559	8·061	7·606	15

(n)	11%	12%	13%	14%	15%	16%	17%	18%	19%	20%	
1	0·901	0·893	0·885	0·877	0·870	0·862	0·855	0·847	0·840	0·833	1
2	1·713	1·690	1·668	1·647	1·626	1·605	1·585	1·566	1·547	1·528	2
3	2·444	2·402	2·361	2·322	2·283	2·246	2·210	2·174	2·140	2·106	3
4	3·102	3·037	2·974	2·914	2·855	2·798	2·743	2·690	2·639	2·589	4
5	3·696	3·605	3·517	3·433	3·352	3·274	3·199	3·127	3·058	2·991	5
6	4·231	4·111	3·998	3·889	3·784	3·685	3·589	3·498	3·410	3·326	6
7	4·712	4·564	4·423	4·288	4·160	4·039	3·922	3·812	3·706	3·605	7
8	5·146	4·968	4·799	4·639	4·487	4·344	4·207	4·078	3·954	3·837	8
9	5·537	5·328	5·132	4·946	4·772	4·607	4·451	4·303	4·163	4·031	9
10	5·889	5·650	5·426	5·216	5·019	4·833	4·659	4·494	4·339	4·192	10
11	6·207	5·938	5·687	5·453	5·234	5·029	4·836	4·656	4·486	4·327	11
12	6·492	6·194	5·918	5·660	5·421	5·197	4·988	4·793	4·611	4·439	12
13	6·750	6·424	6·122	5·842	5·583	5·342	5·118	4·910	4·715	4·533	13
14	6·982	6·628	6·302	6·002	5·724	5·468	5·229	5·008	4·802	4·611	14
15	7·191	6·811	6·462	6·142	5·847	5·575	5·324	5·092	4·876	4·675	15

PFM4 PUBLIC SECTOR FINANCIAL MANAGEMENT SUGGESTED SOLUTIONS

SOLUTION ONE

(a) Stages of the Budget Cycle:

- **Budget Formulation**
  The budget is formulated based on a clear overall strategy and are prepared in order to support the implementation of policies to achieve public service goals. It facilitates strategic, operational or programmatic resources decisions.
  Annual budgets are aligned with medium term plans and there is effective participation by stakeholders in the process.

- **Budget Approval**
  The budget is approved by the legislative, which effectively scrutinizes the government plans. It appropriates funds for expenditure by Ministries, Provinces and spending agencies (MPSAs).

- **Budget Execution**
  Budget execution is the implementation of the approved budget largely devolved to individual Ministries, Provinces and spending agencies (MPSAs). Its implemented in accordance with the financial management policies and regulations, processes, procedures and systems set by the Ministry of Finance.

- **Budget Auditing and assessment**
  The annual financial reports are produced which are subjected to independent external audits and scrutiny. The budget assessment is used to assist in the formulation of future budgets, support scrutiny prior to approval and used to improve processes related to budget execution.

(b) Meaning of Virement and explanation

- This refers to the process of transferring an approved budgetary provision from one operating cost item to another. It means the transfer of monies from one budget line to another. It facilitates the budget to be adjusted to bring it back into line with the actual. It is the process of meeting overspending in one area with underspending in another area.
- It represents a mechanism to effect budgetary amendments within the financial year.

(c) Supplementary budget

- Supplementary budgets are made when the government needs to spend funds for which it has not received parliamentary approval. Such provisions are intended to be utilized for urgent and unforeseen expenditure.
  A revised Budget is usually prepared by the central government and submitted in June and September.

- This arises as a result of unanticipated needs that arises as a result of a spending agent requiring more funds or were the spending agent has:

(i) Unspent funds at the end of the financial year which it has retained and released upon approval of a supplementary budget.
(ii) Where it receives a donation or grant that was not anticipated during the financial year, a supplementary budget may be prepared for approval for such a donation or grant.

(d) Banking Services:

- Advisory,
- Financing,
- Risk management
- Transactional Solutions
- Helps Government
    - Transparency,
    - Accountability
    - Service Delivery
- Improve Governance environment
- Helps reduce the risk of corruption.
- Strengthening public sector management

(e) Importance of Debt Management

- This is to ensure that the government's financing requirements and its payment obligations are fulfilled at least cost.

Framework:

- Governance
- Management of Internal Operations
- Debt management strategy
- Risk Management Framework
- Scope for active management
- Contingent Liabilities
- Development and maintenance of an efficient and effective market for Government Securities
- Portfolio diversification and 1instruments
- Primary Market
- Security market

SOLUTION TWO

(a)

working 1 Purchases

	JULY	AUGUST	SEPT
	K000	K000	K000
Material usage	9,000	10,000	10,500
Closing inventory	4,000	7,000	5,500
	13,000	17,000	16,000
Less opening inventory	6,000	4,000	7,000
Purchases	7,000	13,000	9,000
Total			
Working 2 indirect exp			
	JULY	AUGUST	SEPT
	10,500	11,000	10,000
Depreciation	(2,000)	(2,000)	(2,000)
	8,000	8,500	9,000
Total			
CASH BUDGET JULY-SEPT	2023		
	JULY	AUGUST	SEPTEMBER
	K000	K000	K000
RECEIPTS OF CASH			
Cash Sales	17,000	12,000	14,000
Credit Sales	31,500	68,000	48,000
TOTAL	48,500	80,000	62,000
CASH PAYMENTS			
Salaries	15,000	16,000	16,500
Indirect expenses	8,000	8,500	9,000
Direct Materials	7,000	13,000	9,000
Equipment	-	30,000	-
TOTAL	30,000	67,500	34,500

Surplus/(deficit) per month	18,500	12,500	27,500
Opening balance	(80,000)	(61,500)	(49,000)
Closing balance	(61,500)	(49,000)	(21,500)
TOTAL			

(b) Seven ways of improving the cash flow position of Nitrogen Chemicals.

1. Delay payment to suppliers. – this can be done by negotiating better credit terms with the suppliers.
2. Speeding up payments from customers- this can be done by giving them cash discounts for prompt payment.
3. Keeping low inventory levels. This can be achieved by stocking only what is needed in the short term.
4. Delay hiring employees.
   This can be done by improving the productivity of current employees (without burning them out), use independent contractors and consider outsourcing certain non-essential functions.
5. Leasing assets and not buying- instead of buying the equipment for K30,000,000 in August a leasing arrangement can be entered into.
6. Create contingency plans. Have several budget projections including worst case and best case scenario and think about how you might respond.
7. Avoid wasteful expenditure – Recycle and re-use what you can – for example boxes and file folders can be recycled.

SOLUTION THREE

(a) Payback period and its implication:
- The payback period is the length of time it takes to recover the cost of an investment or the length of time an investor needs to reach a breakeven point.
- It provides information about a project liquidity and risks
- The shorter paybacks indicate more attractive investment, while longer payback period are less desirable.
- The payback period is calculated by dividing the amount of the investment by the annual cash flow.
- Account and fund managers use the payback period to determine whether to go through with an investment.

(b) Distinguish between the (NPV) and the payback period:
The difference between Net Present Value (NPV) and the payback period is that the payback period is used to analyse the number of years the investment amount will be recovered while the Net Present Value (NPV) determines the present value of the subsequent cash flow resulting from the project investment.

(c) Payback Period:

Year	Net Cash Flow K'000	Cumulative net cash inflow(K'000)
1	25,000	(96,800)
2	18,000	(78,800)
3	7,800	(71,000)
4	16,000	(55,000)
5	50,000	(5,000)
6	20,000	

The payback period is 5.25 years.

(d) Advise:
- The payback period is longer than the maximum desired payback period of the management (4) years. The investment based on this method should not be undertaken.

(e) Payback period method:

Advantages of the payback method
- Easy to compute
- The shorter the payback, the better since funds are released for another investment strategy
- A useful capital budgeting method for cash poor companies
- This is essential for the liquidity of a company for a shorter payback period
- Risk reduction associated with changing economic conditions.

Disadvantages of the payback

- Does not consider the useful life of the assets and inflow of cash after payback period
- The method does not take into account the time value of money.

SOLUTION FOUR

(a) Stakeholders for Government institutions:

Direct Influence

- Legal Hierarchy
- Leadership authority
- Control of strategic resources
- Ability to negotiate

Indirect Influence

- Social, economic or political position
- Strategic control with regards to those resources specifically for the project.
- Informal influence

(b) Principles of Stakeholder management

- In decision making and operations, managers should actively monitor the concerns of all the legitimate stakeholders
- Managers should listen to and openly communicate with stakeholders.
- Managers should adopt processes and modes of behavior that take into account concerns of each stakeholder
- Recognition by the managers of the interdependence.
- Team work is critical and recognition of the other entities both public and private.
- Activities that might jeopardise inalienable human rights should be avoided.
- Managers must accept the potential conflicts between their own roles and corporate stakeholders and their legal and moral responsibilities.

SOLUTION FIVE

(a) Five stages of the performance management cycle.

(i) Setting objectives – what you want to achieve e.g 25% increase in production next year. Setting objectives is the first act a public sector organization will have to undertake. The organisation must first strategise on the goals the organization wants to meet in the first place.

It also includes the measures that will be used to determine whether expectations and goals are being met.

(ii) Measuring the performance – consistently measuring performance and providing ongoing feedback to actual performance toward reaching the set objectives. Ongoing measuring of performance provides the opportunity to check the performance to identify and resolve any problems early.

Measuring performance involves collecting, analyzing and reporting information regarding the performance of employees and the public sector organisation.

(iii) Feedback of performance results – this is an evaluation of actual performance against targets.

It evolves evaluating employee or group performance against the elements and standards in an employee's performance plan, summarizing that performance, and assigning a rating of record and organisation actual performance against the set targets.

(iv) Reward systems based on performance outcomes. – Providing incentives to and recognition of employees, individually and as members of groups, for their performance and acknowledging their contributions to the organisation.

(v) Amendments to objectives and activities. A review of the objectives and activities can be done for the purpose of making improvements.

(b) Essential healthcare practical performance measures:

(i) **Length of stay**

Measures the length of time between a patient's admittance and discharge. This metric gives an institution hard data over time on care efficiency.

(ii) **Readmission rates**

Tracks the percentage of patients that are re-admitted within 30 days of their discharge. Hospitals are able to quantify the quality of care patients received. A large percentage of readmissions may mean that patients are receiving substandard care and providers are overlooking complications or relevant patient data.

(iii) **Mortality rates**

How many patients die during a hospital stay before being discharged? This measurement indicates how well an institution can stabilize a patient's condition following surgery or another procedure.

(iv) **Bed utilization rate (or bed occupation rate)**

Measures how many hospital beds are being used at any given time. If there are too many hospital beds available, a hospital many lose money because staffing and maintenance costs remain relatively constant — no matter the number of patients.

(v) **Hospital incidents**

Measures the consequences from unexpected side effects of hospital procedures. The metric is an important indicator of whether a hospital has the procedures in place to give high-quality care without triggering an incident

END OF SOLUTIONS

PUBLIC SECTOR FINANCIAL MANAGEMENT PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

PFM 5: PUBLIC SECTOR AUDITS

THURSDAY 15 JUNE 2023

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 (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.

<u>QUESTION ONE</u> – (COMPULSORY)

In 2016, the Road Development Agency (RDA) decentralized the awarding and supervision of contracts for township roads to the Provincial Road Development Engineering Divisions headed by Provincial Road Engineers (PREs) based at each of the ten provinces.

The aim of decentralizing was to speed up the award of contracts and have closer supervision of the road works in progress. The Provincial Road Engineers were given authority to award contracts of up to a maximum of K50 million without tender. Above this amount tenders are invited from eligible contractors who are required to submit their tenders to the Provincial Road Engineer. The Provincial Engineer is required to analyze the tenders and to submit a summary of the analysis to the tender committee for consideration and award.

The Southern Provincial Road Development Engineering Division has a workforce of twenty-five employees. Due to irregular funding by the Central Government, the employees are not paid on time and currently they are three months in salary arrears. The accounts office is manned by three members of staff and there is limited segregation of duties. The Senior Accountant who is responsible for the preparation of bank reconciliation took vocational leave and no bank reconciliations have been prepared for four months.

In 2018, tenders for the tarring of township roads in the provincial headquarters of Southern Province were invited from eligible contractors. The road works were all above the threshold of K50 million. The Provincial Permanent Secretary exerted influence on the Provincial Road Engineer to include, among the bidders, a company that was not on the list of approved contractors. He verbally told the Provincial Road Engineer that the named contractor was referred to him by higher authorities. The Provincial Engineer agreed to the request and he asked the Provincial Permanent Secretary, who is a member of the Tender Committee, to support the bid of a company in which the Road Engineer has shares.

Payments to contractors who carried out road works in 2017 have not been made to-date due to lack of funds. The Provincial Engineer submits a schedule of all outstanding payments and makes recommendations to Headquarters on which contractors should be paid.

You work for the Office of the Auditor-General (OAG) as principal auditor. You have been assigned to lead a team of auditors to carry out an audit of the operations of the Southern Provincial Road Development Engineering Division for 2018. This is going to be the first audit of the regional office of the Provincial Road Engineer.

Except for you, the rest of the audit team members have no experience in public sector audits. One of the Audit Assistants has come to you and suggested that you should use the services of an audit expert in performing some of the audit work. The Audit Assistant is concerned that audit risk in this audit may be high because the institution has not been subject to an audit in the past.

There is a need to establish the level of audit risk and to consider the effectiveness of internal controls that may exist.

In the pre-audit meeting with the Management of the Provincial Road Development Engineering Division you discover that your wife is a cousin to the wife of the Provincial Road Engineer. The couple has invited you to stay at their house during the period of the audit. The rest of the audit team will find their own accommodation because they obtained subsistence allowances meant for accommodation and food. The Southern Provincial Road Engineer has informed you that the office has a staff canteen and he has suggested that the audit team can have free lunch at the staff canteen during their stay.

During the course of the audit, one of the Audit Assistants informed you that he came across a fraud that occurred in 2017 involving overpayments to suppliers. When he questioned the Provincial Road Engineer he was told that the person who was involved in the fraud has since been transferred to another province on his recommendation. Other members of staff are aware of the fraud and the action that was taken against the person involved. You advised the Audit Assistant not to document the fraud because action against the person involved has already been taken and in line with the principle of confidentiality, this matter should be kept confidential.

Required:

(a) Identify and explain five (5) fraud risk factors that exist in the Southern Provincial Road Development Engineering Division. (10 marks)

(b) Explain the meaning of audit risk and its components in public sector auditing. (6 marks)

(c) Explain the five (5) elements of internal control in accordance with ISSAI 1315 *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment.* (10 marks)

(d) Identify and explain five (5) ethical issues in the audit of the Southern Provincial Road Development Engineering Division by the Office of the Auditor-General (OAG). (5 marks)

(e) Suggest suitable responses to the ethical issues identified in (d) above. (5 marks)

(f) Suggest four (4) matters that the audit team should consider before placing reliance on the work of an expert. (4 marks)

[Total: 40 Marks]

SECTION B

There are FOUR (4) questions in this section.

Attempt any THREE (3) questions in this section.

QUESTION TWO

(a) The Supreme Audit Institution (SAI) in Zambia is the Office of the Auditor General (OAG) which is a member of the International Organisation of Supreme Audit Institutions (INTOSAI). The Office of the Auditor-General operates independently and does not report to any Government Ministry.

Required:

(i) Distinguish the roles of the International Organization of Supreme Audit Institutions (INTOSAI) and the Supreme Audit Institutions (SAIs). (4 marks)

(ii) Explain the role of the Office of the Auditor-General (OAG) in providing oversight on the use of public funds. (4 marks)

(iii) Explain why the Auditor-General (AG) does not report to any Government Ministry and why the appointment of the AG is enshrined in the Constitution of Zambia. (4 marks)

(b) You have been assigned to lead a team of public sector auditors to carry out a performance audit in the operations of the farmer extension services in the Eastern Province of the Republic of Zambia.

The objective of the extension service is to offer technical advice to farmers in the region with a view to improving productivity. The Provincial Extension Office is funded by the Ministry of Agriculture and in the year under review there is a total budget of K12 million.

The budget provides for the procurement of five motor bikes for the Extension Officers. The provincial office is responsible for the acquisition of the motor bikes. Each Extension Officer is given targets in terms of the number of farmers that should be visited per quarter. It is expected that with the introduction of farmer extension services, there will be an increase in the hectares of crop grown and also the yield which will help reduce the current food shortage in the country.

Required:

(i) Explain the objective of the performance audit of the extension services in the Eastern Province. (2 marks)

(ii) Briefly explain value for money audit and how it will be undertaken in the audit of the performance of the extension services in the Eastern Province. (6 marks)

[Total: 20 Marks]

QUESTION THREE

(a) At the planning stage of audits, the audit team is required to set materiality levels which will be applied during the audit.

ISSAI 1320 *Materiality in planning and performing an audit* gives guidance in the area of materiality.

Required:

Define materiality and explain how materiality is determined in financial statement audits. (5 marks)

(b) You are an Audit Supervisor in the Office of the Auditor-General's Directorate of Public Department and Investment. You are part of the engagement team assigned to the financial audit of China Zambezi Textiles, a public sector business organization.

You are specifically responsible for supervising and reviewing the work of Audit Assistants in your team.

Required:

(i) Describe the three (3) stages of the financial audit which will be performed at China Zambezi Textiles. (6 marks)

(ii) Explain the benefits of audit planning in accordance with ISSAI 1300. (5 marks)

(iii) Describe the Audit Supervisor's responsibilities in relation to supervising and reviewing the Audit Assistants' work during the audit of China Zambezi Textiles. (4 marks)

[Total: 20 Marks]

QUESTION FOUR

You are a Principal Auditor in the Office of the Auditor-General (OAG). You have been assigned to lead a team of auditors to carry out a financial audit of a Government owned institution of higher learning.

At the commencement of the audit, you informed the audit team members of the need to obtain sufficient appropriate audit evidence using the various methods available for gathering evidence.

Towards the end of the audit, the Senior Audit Assistant presented to you the working paper file for review. You realize that all the work that has been done related to the current year and there is no evidence of work carried out regarding subsequent events. When you questioned the Senior Audit Assistant, he responded by stating that he does not see the need for the team to perform audit procedures for transactions in the subsequent period which will be subject to the following year's annual audit.

The working papers also contain a draft management letter for your review.

Required:

(a) Explain the difference between a management letter and the audit report. (3 marks)

(b) Explain the meaning of subsequent events in an audit of financial statements. (2 marks)

(c) Explain the duties of the auditor between the year end and the date of signing the auditor's report and between the date of signing the auditor's report and the issue of the financial statements. (5 marks)

(d) Explain five (5) methods of obtaining audit evidence that may be used in the audit of the financial statements of the higher learning institution. (10 marks)

[Total: 20 Marks]

QUESTION FIVE

(a) Public sector auditors perform audit procedures at the planning stage, the substantive audit stage and the final review stage. During the substantive audit stage, the public sector auditors perform tests of control and substantive tests.

Required:

Explain the meaning and objectives of tests of control and substantive tests performed by public sector auditors. (4 marks)

(b) The audits performed by the public sector auditors go beyond the traditional audits of financial statements. In the Republic of Zambia, the Office of the Auditor-General (OAG) is responsible for performing various types of public sector audit in a number of institutions and organisations.

You are a Principal Auditor in the OAG. The Auditor-General has requested you to prepare notes on the following topics which will be used in the induction programme for newly recruited Audit Trainees:

(1) Organisations subject to audits by the OAG.

(2) Appointment and removal of the Auditor-General

(3) Main characteristics of forensic audits

(4) Benefits of Audit Committees.

Required:

(i) List four (4) examples of institutions or organizations that are subject to audits by the Office of the Auditor-General (OAG). (2 marks)

(ii) Explain how the appointment and removal of the Auditor-General (AG) is done in Zambia. (4 marks)

(iii) Explain four (4) main characteristics of forensic audits carried out by the Office of the Auditor-General. (6 marks)

(iv) Discuss four (4) benefits of Audit Committees. (4 marks)

[Total: 20 Marks]

END OF PAPER

PFM 5: PUBLIC SECTOR AUDITS SUGGESTED SOLUTIONS

SOLUTION ONE

(a) **Fraud risk factors in the Southern Provincial Road Development Engineering Division:**

1. **Decentralization of award of contracts:**
   Procurement is one of the risk areas in organizations. The transfer of responsibilities to the Provincial Road Engineer is a fraud risk factor in that this responsibility has been put in the hands of an individual who is not answerable to anyone else with regards to the award of tenders.
2. **Award of contracts without tender:**
   The limit of K50 million that can be awarded without following tender procedure is a material amount and this can be tempting to the Provincial Road Engineers to be involved in fraudulent activities with regards to the award of tenders. Preferential awards can be given for gratification without breaching any regulations.
3. **Delayed payments of salaries:**
   The delays in payment of salaries to staff is a fraud risk factor in that staff may justify fraud in view of the fact that they are paid their salaries late. Employees who handle cash will be pressured to misappropriate organizational funds in order to meet their financial requirements.
4. **Lack of segregation of duties:**
   The lack of segregation of duties implies that there are poor internal controls. This can tempt an individual to commit fraud knowing that it may not be detected or it will take some time before the fraud is detected.
5. **Non preparation of bank reconciliations:**
   The preparation of bank reconciliation is an essential control to enable prompt detection of fraud and error. The fact that bank reconciliations are not prepared on a regular basis and also that they are four months behind can motivate an individual handling funds to commit fraud hoping that this will not be detected promptly.
6. **Pressure from the Provincial Permanent Secretary:**
   Interference with the award of tenders by the Provincial Permanent Secretary is a fraud risk factor in that the Provincial Road Engineer may also decide to award tenders to contractors not on the list of approved contractors knowing that the Provincial Permanent Secretary is unlikely to question him on a matter that he is involved in. The fact that the Provincial Permanent Secretary seems also to have been pressured from above suggests that any political influence can be a fraud risk factor.
7. **Irregular payments to contractors:**
   Contractors want to be paid promptly for work done. The delays in paying the contractors and the fact that the Provincial Road Engineer recommends who should be paid is a fraud risk factor. The contractors are likely to pay gratification

for inclusion on the list of contractors to be paid. The pressure on the part of the Provincial Road Engineer increases in view of delays in receiving salaries.

8. **Transfer of staff involved in fraud:**
   The fact that no displinary action was taken against the staff member who was involved in fraud may motivate other members of staff to commit fraud knowing that no action will be taken.

(b) **The meaning of audit risk in public sector auditing:**

Audit risk in public sector auditing is the risk that the auditor may issue an inappropriate opinion or conclusion.

The auditors aim at reducing audit risk to acceptable levels. Audit risk comprises three components as follows:

Inherent risk – this is the risk that exists because of the nature of the business or industry or the item. There is nothing that the public sector auditor can do to reduce inherent risk.

Control risk – this is the risk that the internal controls put in place by management may fail to prevent or detect material misstatement. Control risk is not under the control of the auditor. It is the responsibility of management to put in place suitable controls.

Detection risk- this is the risk that the auditor having performed the audit in line with the auditing standards may fail to prevent or detect material misstatements
Any of the above three elements of audit risk can cause the auditor to issue an inappropriate audit opinion.

(c) **Elements of internal control:**

1. **Internal control environment:**
   This is the environment within which the internal controls operate. It could be a weak or strong and this determination will enable the auditor to respond appropriately.
2. **Risk assessment processes of the client:**
   This is an evaluation of the systems that the organization being audited follows in identifying risks that face the organization. Internal controls are put in place to mitigate the risks that exist.
3. **IT systems relevant to the preparation of the financial statements:**
   This is the information system that the client organization uses to determine the figures in the financial statements.
   The public sector auditor needs to understand the system that the client uses.
4. **Control activities:**
   These are the actual controls that exist in a client company. The public sector auditor need to know the controls that are in the client company in assessing the risk of material misstatements.

5. **Monitoring of controls:**
   These are the systems that the client organization uses in order to monitor the existing controls. The most common method of monitoring controls is the use of internal audit.

(d) **Ethical issues in the Southern Provincial Road Development Engineering Division:**

1. **Competence of the audit team members:**
   One of the ethical values of public sector auditors is that they should have the necessary skills and competences to perform the audit.
   In the case at hand, except for the Principal Auditor the rest of the audit team members have no experience in public sector auditing.
2. **Principal auditor's wife related to wife of PRE:**
   One of the ethical requirement of the public sector auditors is that of objectivity. Lack of independence of the audit team members could lead to objectivity being compromised.
   The wife of the Principal Auditor is a close relative to the wife of the PRE who is being audited. This is likely to give rise to a self-interest threat and may affect the objectivity of the Principal Auditor.
3. **Principal Auditor lodging with PRE:**
   The offer that the principal auditor should lodge at the house of the PRE is an ethical issue which can give rise to a self-interest and familiarity threat. The PRE is a senior person being audited and is involved in the operations of the institution.
4. **Offer of free lunch to the audit team members:**
   The offer of free lunch to the audit team members at the staff canteen is an ethical matter which can give rise to a self-interest threat.
   This appears not to be one-day issue but rather for the duration of the audit and this may impact on the objectivity of the audit team members who will be motivated to saving the allowance that they were given for lunch.
5. **Non-disclosure of fraud:**
   Confidentiality is one of the ethical principles of public sector auditors. It requires that the public sector auditors should not disclose to third parties information that comes to their attention during the course of the audit without the permission of the client.
   There are, however, exceptions to this rule particularly where there is an illegality. Fraud in many organizations is a significant risk and the auditors should look out for any fraud that may cause the material misstatement of financial statements.
   The suggestion by the Principal Auditor that the fraud should not be documented because that would be in breach of confidentiality principle is incorrect.

(e) **Responses to ethical matters:**

1. The composition of the audit team assigned to this audit should be reviewed so that it should include staff who have some experience in public sector auditing. This is compounded by the fact that the Principal Auditor may not spend a lot of time at the client's premises.
   In the absence of other staff with the necessary skills, there should be strict supervision by the Principal Auditor of the rest of the audit team who will be involved in the audit.
2. The Principal Auditor should be replaced by someone who has not relationship with the client. In the case that this may not be possible, the work performed by the Principal Auditor should be reviewed by someone who was not involved in the audit as part of quality review.
3. The Principal Auditor should decline the offer to lodge with the PRE. He has been paid subsistence allowance and he should use this to find accommodation during the period of the audit.
4. Unless the cost of providing the lunch is clearly insignificant, the audit team should decline the offer.
5. The fraud should be documented and the auditor should find out from management of any fraud that they know or suspect.

(f) **Matters to consider in placing reliance of an expert:**

1. The objectivity of the expert by considering their independence from the client organization.
2. The qualifications and skills of the expert to carry out the work.
3. Previous work that has been done by the expert. This may be done by obtaining references from those that the expert did work in the past.
4. Membership to the professional body to which expert is a member.

SOLUTION TWO

(a) (i) **Roles of the INTOSAI and the SAI:**

The International Organization for Supreme Audit Institution (INTOSAI) is a world body whose main objective is to ensure that those responsible for the use of public funds do so for the benefit of the citizens.

This is achieved by the INTOSAI issuing standards that should be followed by member countries in their performance of public sector audits.
The INTOSAI also facilitates sharing of experiences amongst member countries.

Supreme Audit Institutions (SAI) on the other hand are those organizations of individual countries whose role is to carry out audits of the custodians and spenders of public funds.

The SAI carries out audits meant to hold those who spend public funds to be accountable and do so in the best interest of the general citizenry.

(ii) **Role of Auditor General in providing oversight:**

The Public Accounts Committee provides oversight on behalf of parliament on how those responsible for use of public funds perform their role as stewards.

Parliament confers responsibility on the executive and others charged with the use of public funds to apply them in the best interest of the citizens.

Parliament confers on the Auditor General the responsibility to carry out audits on how those charged with the use of public funds have performed their stewardship role.

The auditor performs audit procedures and report to the President and Parliament. Parliament through the Public Accounts Committee follow up the matters in the report with the responsible parties.

In this way the Auditor General plays a critical role in aiding those responsible for oversight perform their duty.

(iii) **Reporting of the Auditor General:**

The Auditor-General is autonomous and does not report to any Government Ministry.

The work of the Auditor-General involves carrying out audits and investigations on all Government Ministries and to report on the findings. For the Auditor General to carry these tasks effectively it is necessary that the Auditor-General remains independent of the auditees.

By not reporting to any Government Ministry, the Auditor-General maintains his independence and hence objectivity. The Auditor-General will not be intimidated by anyone which would not have been the case were he to report to any Government Ministry.

Appointment enshrined in the constitution:

The appointment and tenure of the Auditor-General is enshrined in the Constitution in order to give the Auditor General security of tenure of office.

The removal of the Auditor General is also contained in the constitution. This means that the Auditor General will not be scared of losing his job because he can only be removed under specific conditions spelled out in the Constitution.

(b) (i) **Objective of the performance audit of Eastern Province Extension services:**

The objective of carrying out a performance audit of the extension services in Eastern Province is to establish whether there is value for money in the activities that have been carried out under the program.

This will be achieved by evaluating the economy, efficiency and effectiveness of the program that has been undertaken.

(ii) **Value for money audit:**

The value for money audit in the extension service in the Eastern Province can be carried out by considering the three elements of value for money namely economy, efficiency and effectiveness.

This can be done as follows:

Economy:

This relates to consideration whether the activity has been carried out in the most economical way considering the relevant costs.

In the case at hand, the budget provides for the procurement of motor bikes for the Extension Officers. The question is whether the best price has been paid for the motor bikes without compromising on quality. There is a risk of misuse of public funds by way of paying more than is necessary for the bikes.

For example, if there was single sourcing of the motor bikes it is more likely that a higher price will have been paid than if the procurement was subject to tender.

Efficiency:

This involves comparing the input resources with the output. This suggests getting higher output for the same input resources.

In the case at hand, the input could be the cost of each Extension Officer compared with the expected output in terms of visits made. The higher the number of visits carried out using the same resources the better the efficiency in the use of resources.

Effectiveness:

This is related to the achievement of the intended objectives.

In this case, the extension services have been introduced with an objective of improving farmer productivity. This will be evidenced by an increase in the yield compared to the past levels.

In this case, this can be measured by comparing the productivity after introducing extension services and the productivity before the introduction of extension services.

SOLUTION THREE

(a) **Meaning of materiality:**

Materiality is defined as follows: 'Misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.'

In assessing the level of materiality there are a number of areas that should be considered. Firstly, the auditor must consider both the amount (quantity) and the nature (quality) of any misstatements, or a combination of both.

The quantity of the misstatement refers to the relative size of it and the quality refers to an amount that might be low in value but due to its nature could influence the user's decision.

In assessing materiality, the auditor must consider that a number of errors each with a low value may when aggregated amount to a material misstatement.

The assessment of what is material is ultimately a matter of the auditors' professional judgement, and it is affected by the auditor's perception of the financial information needs of users of the financial statements.

In calculating materiality, the auditor should also consider setting the performance materiality level.

This is the amount set by the auditor, it is below materiality, and is used for particular transactions, account balances and disclosures.

As per ISSAI 1320, materiality is often calculated using benchmarks such as 5% of profit before tax or 1% of gross revenue. These values are useful as a starting point for assessing materiality.

(b) **China Zambezi Textiles:**

(i) **Three stages of an audit**

- **Planning** – It is important to understand the audited entity and its environment as part of the risk assessment procedure. This includes the risk of material misstatement due to fraud and error at the financial statement and assertion level
- **Testing –** Auditors must undertake substantive tests to identify material misstatements at the assertion level. Tests of control are performed to assess the operating effectiveness of controls at the financial statement and assertion level. These are essential to validate the auditor's expectation of the operating effectiveness of controls
- **Completion –** Auditors shall make a conclusion as to whether sufficient and appropriate evidence has been obtained for all material financial statement assertions. In case an auditor is unable to obtain sufficient and appropriate

evidence in respect a material financial statement assertion, he is required to modify the audit report accordingly.

(ii) **Benefits of Planning**

- Helping the auditor to devote appropriate attention to important areas of the audit.

- Helping the auditor to identify and resolve potential problems on a timely basis.

- Helping the auditor to properly organize and manage the audit engagement so that it is performed in an effective and efficient manner.

- Assisting in the selection of engagement team members with appropriate levels of capabilities and competence to respond to anticipated risks and the proper assignment of work to them.

- Facilitating the direction and supervision of engagement team members and the review of their work.

- Assisting, where applicable, in coordination of work done by experts.

(iii) **Supervision**

- During the audit of China Zambezi Textiles, the Audit Supervisor should check the progress of the audit engagement to ensure that the audit timelines are met. Additionally, an Audit Supervisor should ensure that the Director of the department are kept updated on audit progress.
- The competence and capabilities of individual members of the engagement team should be considered, including whether they have sufficient time to carry out their work, whether they understand their instructions and whether the work is being carried out in accordance with the planned approach to the audit.
- Additionally, the supervision process should involve addressing any significant matters that may arise during the audit of China Zambezi Textiles, considering their significance and modifying the planned approach appropriately.

Review

- It is the duty of the Audit Supervisor to review the work completed by Audit Assistants and consider whether this work has been performed in accordance with professional standards and other regulatory requirements, and if the work performed supports the conclusions reached and has been properly documented.
- The Audit Supervisor should also consider whether all significant matters have been raised for Director's attention or for further

consideration and where appropriate consultations have taken place, whether appropriate conclusions have been documented.

SOLUTION FOUR

(a) **Difference between a management letter and an audit report:**

A management letter is one that is written by the auditor to the management of the responsible party. It is a by-product of the audit in that during the course of the audit, internal control weaknesses may be discovered. These are communicated to management by the auditor using a management letter.

The audit report is the outcome of the audit and is usually addressed to the interested parties such as the President and Parliament in the case of public service audits. The auditor communicates his opinion or conclusion in the audit report.

(b) **Meaning of subsequent events:**

Subsequent events are events that occur after the date that the financial statements period end.

Subsequent events can have audit significance in that they could give evidence of conditions that existed at the period end. These are events that take place between the end of the financial period and the date the audit report is signed.

(c) **Duty of auditor between year-end and date of audit report:**

The auditors have an active duty between the year end and the date of signing the audit report. The duty of the auditor is to look out for any subsequent events that take place during this period.

Once a subsequent event has been established, the auditor will enquire from Management on how the event has been accounted for. If accounted for correctly, then that marks the end. If not, the auditor will request Management to account for the event correctly as the case may be.

Duty of auditor between date of report and issue of accounts:

After the date the report is signed to the date of issue of the financial statements, the auditor has a passive duty.

It is the duty of management to bring to the attention of the auditor any matters that would have caused the auditor to issue a different opinion.

If any such matter comes to the attention of the auditor during this period, the auditor shall discuss the matter with management and find out how management hopes to deal with it.

If it requires amendment of financial statements and the financial statements are adjusted, the auditor shall perform audit procedures on the amendments and issue a new audit report.

The auditor will then extend the period of looking out for subsequent events to the date of the new audit report.

(d) **Methods of obtaining audit evidence:**

Observation – This consists of the public sector auditor looking at a process or procedure being done by others to confirm whether it is being done correctly. For example, the auditor observing staff doing carrying out an inventory count.

External confirmation – This is where the public sector auditor obtains evidence directly from third parties in paper or electronic form. For example, direct confirmation of receivables or bank balances.

Recalculation – This involves the auditor checking the arithmetical accuracy of documents or records. For example, redoing the arithmetic on an invoice raised.

Re-performance – This is an independent execution by the public sector auditor of procedures or controls for example the bank reconciliation being redone by the auditor.

Analytical procedures – This consists of an evaluation of financial or other information through analysis of plausible relationships and investigating unexpected fluctuations or relationships.

Inquiry – This consists of the public sector auditor seeking information from management and others within the organization.

SOLUTION FIVE

(a) **Meaning and objective of tests of control:**

Tests of control are procedures carried out by the public sector auditor to confirm the effectiveness or lack of effectiveness of the internal controls of a client organization.
During the planning stage of the audit, the auditors will gain an understanding of the applicable controls.

Objective of tests of control:

The main objective of performing tests of control is to assess the effectiveness of the internal controls. If the auditor concludes that the controls are operating effectively during the period under review, the auditor may decide to place reliance on the effectiveness of the controls and do less substantive tests.

Meaning and objective of substantive tests:

Substantive tests are the work that the auditor performs on the transactions and balances contained in the financial statements. Management make financial statement assertions concerning the figures in the financial statements. Auditors design suitable audit procedures to test the assertions contained in the figures in the financial statements.

Objective of substantive procedures:

The purpose of performing substantive procedures in public sector auditing is to establish whether or not the figures contained in the financial statements are materially misstated. The results of the substantive tests form the basis for the auditor's opinion.

(b) (i) **Institutions and organisations subject to audit by the Office of the Auditor-General:**

1. Government Ministries.
2. Local councils.
3. Publicly owned entities.
4. Any institution receiving government grants.

(ii) **Appointment of the Auditor-General:**

The appointment of the Auditor-General is provided for under the Constitution of Zambia.

The President of Zambia nominates an individual to take up the position of Auditor-General.

The name is subject to Parliament who decides whether or not the nominated person should take up the position. If Parliament is agreeable to the nomination they ratify the appointment and the individual takes up the appointment.

Removal of the Auditor-General:

The procedure and reasons for the removal of the Auditor-General is contained in the constitution.

The constitution sets out the reasons why the Auditor General may be removed including insanity and bankruptcy.

(iii) **Characteristics of forensic auditing:**

1. **Ad hoc rather than routine –** They do not happen as a matter of routine like financial statement audits. This is because they usually involve investigations and these are unpredictable.
2. **High probability of dishonest –** Usually forensic audits involve deception or dishonest by staff or management.
3. **Source of information –** This extends beyond the organization's records and usually will include interviews of those involved.
4. **May result in legal action –** The work may lead to court action against those involved or may require the forensic auditor to be an expert witness in a legal case.
5. **Different skills and mindset –** Because of differences in the features of a forensic audit, it requires different skills to suite the investigative role involved.
6. **Non-standard report –** In many cases of audit work there are standard forms of reporting. This is not the case with forensic audits which is not concerned with giving assurance but rather gathering evidence which is accurate and can stand in court and the report will depend on the terms of the assignment and is usually agreed at the time of engagement.

(iv) **Benefits of audit committees:**

1. The committee offers oversight on the work carried out in the Ministry.
2. The public institutions benefit from the skills that committee members possess.
3. Its very existence acts as a deterrent to fraud. Employees know that there is a group of people who will check what is being done.
4. Because internal audit department usually reports to the audit committee, it gives the department some independence of those in charge and so internal audit will be more objective in carrying out its work.
5. The committee has a role in monitoring internal controls of the institutions.

END OF SOLUTIONS

PUBLIC SECTOR FINANCIAL MANAGEMENT PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

PFM 6: FINANCIAL REPORTING FRAMEWORK FOR PUBLICSECTOR ENTITIES

MONDAY 12 JUNE 2023

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.

<u>QUESTION ONE</u> – (COMPULSORY)

The following has been extracted from the draft financial information of Mukosa Ltd, a public utility company which was formed in 2021 by the Government of the republic of Zambia. It is run by the community as a Government Business Enterprise (GBE):

Statement of profit or loss for the year ended 31 December 2022

Income	**K'000**
Revenue from contracts with customers	20,000
Other income	5,000
Finance income	15,000
Capital grant amortized	3,250
Total income	**43,250**
Expenditure	
Finance cost	8,500
Operating expenses	12,375
Depreciation	6,125
Employee benefit expenses	4,675
Total expenditure	**31,675**
Surplus before taxation	**11,575**
Income tax expense	**-**
Surplus for the year	**11,575**

Statements of financial position as at 31 December

	2022	**2021**
Descriptions	**K'000**	**K'000**
Assets:		
Non-current assets	**25,200**	**14,750**
Current assets:		
Inventory	1,000	2,250
Trade receivables	5,800	4,725
Cash and bank	750	300
Current assets	**7,550**	**7,275**

Total assets	**32,750**	**22,025**
Members' funds and liabilities:		
Members' funds:		
Accumulated funds	20,575	9,000
Other reserves	500	500
Total Members' funds	**21,075**	**9,500**
Non-current liabilities		
10% Loan notes	7,500	10,000
Bank Loan	1,750	0
Total Non-current liabilities	**9,250**	**10,000**
Current liabilities:		
Trade payables	2,150	2,250
Accruals	275	275
Total current liabilities	**2,425**	**2,525**
Total Members' funds and liabilities	**32,750**	**22,025**

Some stakeholders are concerned that Mukosa Ltd.'s going concern status could be questionable as it appears to have low level surplus and cash inflows. However, several stakeholders are of the view that this is almost impossible since Mukosa Ltd is a public sector entity.

Required:

(a) Prepare a statement of cash flows for the year ended 31 December 2022, using the indirect method. (12 marks)

(b) Outline any six (6) benefits of cash flow information to the Public Sector entities. (6 marks)

(c) State any four (4) characteristics of a Government Business Enterprise in line with IPSAS. (6 marks)

(d) Explain any five (5) qualitative characteristics of information included in the GPFRs of public sector entities. (10 marks)

(e) Explain any two (2) ways in which each of the following assist in performance management in the public sector in Zambia:

(i) The Auditor General. (2 marks)
(ii) The Accountant General. (2 marks)
(iii) The Secretary to the Treasury. (2 marks)

[Total: 40 Marks]

SECTION B

There are FOUR (4) questions in this section.

Attempt THREE (3) questions.

QUESTION TWO

The Ministry of Health has issued a tender for the procurement of IT equipment in clinics and hospitals. The Permanent Secretary has written to your office to participate in the evaluation of the procurement of IT equipment in your capacity as Director of Finance. You have discovered that the files submitted to your office with the analysis and quotations have been inflated with a potential to result in budget overruns. In addition, you have observed that the specifications of the computers are not aligned to what the clinics and hospitals had requested.

The Head of Procurement has approached your office suggesting that you support the quotations that have been submitted and that issues of Budget overruns should not be raised in the evaluation and procurement committee.

Required:

(a) Explain to the Head of Procurement, the IFAC's fundamental ethical principles that you would be violating if you support the inflated prices by not disclosing to senior management that the costs will result in budget over-runs. (8 marks)

(b) Explain how the code of ethics can be internalized and enforced in the public sector. (12 marks)

[Total: 20 Marks]

QUESTION THREE

Performance and financial management in the public sector cover the management, process, and behavioural aspects of strategy, execution, and managing and monitoring performance. This is important to public sector professional accountants, both as employees or advisors. Many of them are focused on helping Ministries, Provinces, and other Spending Agencies (MPSAs) deliver on objectives and strategies using a range of approaches.

You have been engaged as a Financial Consultant by the Government of the Republic of Zambia to assist newly recruited civil servants understand the balanced scorecard and ratio analysis as they relate to the public sector. Most of the new recruits are from the private sector.

The Accountant General wants you to also use the following details for one of the MPSA which produces essential drugs:

	Years ended 31 December	
	2022	2021
	K'000	K'000
Revenue	6,500	4,980
Operating profit	325	249
Non-current assets	7,000	5,000
Current assets	3,000	2,000
Current liabilities	4,000	1,500
Number of employees	1,200	600

The country is experiencing massive load shedding and the high unemployment rate is of great concern to Central Government.

Required:

(a) Calculate and comment on any four (4) suitable ratios which can be used to measure the performance of the MPSA. (12 marks)

(b) Discuss the use of the ratio analysis in performance evaluation in the public sector. (4 marks)

(c) Discuss the use of the balanced scorecard in performance evaluation in the public sector. (4 marks)

[Total: 20 Marks]

QUESTION FOUR

The Ministry of Local Government and Rural Development operates Rest Houses across the country. During the outbreak of covid 19, profitability in most of the rest houses declined. The Directors at the Ministry of Local Government and Rural Development made the following decisions for two (2) local authorities where recovery was not possible in the medium term:

1. To dispose of Ngabwe District council rest house.
2. To refurbish the rest house at Kazungula border in order to target the Tourism Market. The target was tourist visiting the tourist capital.

Required:

In line with IPSAS 40 Public Sector Combinations, explain how the following items of an acquired property should be dealt with at the date of acquisition.

(a) Liabilities related to restructuring or exit activities. (10 marks)

(b) Contingencies. (10 marks)

[Total: 20 Marks]

QUESTION FIVE

The government of the republic of Zambia engaged AFCON Construction to implement a road project in Lusaka District. Below is an extract of information from the books of AFCON for a newly constructed road in Lusaka.

	K
Total contract price	5,000,000
Cost incurred to date including K 500,000 relating to this year	1,500,000
Estimated costs to complete	800,000
Amounts Invoiced	1,000,000
Amounts received	900,000
Percentage Complete	60%

Required:

(a) Explain the two (2) bases on which profit on a construction contract may be recognized for an accounting period. (8 marks)

(b) Explain the accounting treatment of the above contract (8 marks)

(c) Prepare relevant extracts from the statement of financial performance and statement of financial position. (4 marks)

[Total: 20 Marks]

END OF PAPER

PFM 6: FINANCIAL REPORTING FRAMEWORK FOR PUBLICSECTOR ENTITIES SUGGESTED SOLUTIONS

SOLUTION ONE

(a)

Mukosa Ltd

Statement of cash flow for the year ended 31 December 2022	**K'000**	**K'000**
Cash flows from operating activities :		
Surplus for the year		11,575
Depreciation		6,125
Loss on disposal of non-current assets		0
Capital grant amortised		(3,250)
Finance income		(15,000)
Finance cost		8,500
Cash flow from operating activities		**7,950**
Decrease in inventory (2,250 – 1,000)		1,250
Increase in trade receivables (5,800 – 4,725)		(1,075)
Decrease in trade payables (2,250 – 2,150)		(100)
Net cash flow from operating activities		**8,025**
Cash flows from investing activities		
Purchase of non-current assets (W1)		(16,575)
Grant received		3,250
Interest received		15,000
Net cash flows utilised in investing activities		**1,675**
Cash flows from financing activities		
Repayment of long term loans		(2,500)
Interest paid		(8,500)
Proceeds from borrowing		1,750
Net cash flow from financing activities		**(9,250)**
Increase/(Decrease) in cash and cash equivalents		450
Cash and cash equivalents at the beginning of the year		300
Cash and cash equivalents at the end of the year		**750**

Purchase of non-current assets:

W1

	K'000
Opening carrying amount	(14,750)
Depreciation	6,125
Closing carrying amount	25,200
Purchase of non-current assets	16,575

(b) **Benefits of cash flow information include:**

- It helps entity to predict the future cash requirements.
- It helps an entity predict its ability to generate cash flows in the future.
- It provides an entity with the means by which it can discharge its accountability for cash inflows and cash outflows during the reporting period.
- When used with information from other financial statements, cash flow information enables an entity to evaluate the changes in net assets/equity of an entity, its financial structure and its ability to affect the amounts and timing of cash flows in order to adapt to changing circumstances and opportunities.
- It enhances the comparability of the reporting of operating performance by different entities, because it eliminates the effects of using different accounting treatments for the same transactions and other events.
- It helps in checking the accuracy of past assessments of future cash flows.
- The survival of the business depends on the ability to generate cash. Cash flow accounting directs attention towards the critical areas.
- Cash flow is more comprehensive than net profit which depends on accounting conventions and concepts.
- Creditors and other funders are more interested in an entity's ability to repay them than in its profitability.
- It Helps the Government to evaluate liquidity and future cash flow requirement and accountability for its use of cash resources.
- It can be a measure of the extent to which a government has generated sufficient cash flows to maintain programs and services.
- Cash flow reporting satisfies needs of all users better than profit and loss account.

(c) **Government Business Enterprise (GBE) in line with IPSAS**

Government Business Enterprise (GBE) means an entity that has all the following characteristics:

- Is an entity with the power to contract in its own name.
- Has been assigned the financial and operational authority to carry on a business.
- Sells goods and/or services, in the normal course of its business, to other entities at a profit or full cost recovery.
- Is not reliant on continuing government funding to be a going concern (other than purchases of outputs at arm's length; and
- Is controlled by a public sector entity.

- GBEs apply IFRSs issued by IASB.

(d) **Public sector financial statements should meet the following qualitative characteristics:**

(i) **Relevance** –public sector information should be capable of changing previous views held by users of financial information for public sector entities. This is known as having a confirmatory value. In this way it must influence economic decisions of user of such information.

(ii) **Faithful representation**-in order for the users of public information to rely on it should not be biased and should not contain errors and must be complete.

(iii) **Understandability** –the users of public sector information should be able to clearly understand the contents and explanations that relate to contents of public sector financial statements. The language and terms used in the financial statements should be clear for user to make informed economic decisions and prepared at the appropriate knowledge level of the users.

(iv) **Timelines**-for the users of public sector information to make appropriate use and take actions, information whether non-financial and financial should be prepared on time. Information that is prepared and presented late will be rendered of no use. For instance, statistics of census collected by the central statistics office about the population of the country should not be delayed. Otherwise Government will not be able to plan efficiently for the country.

(v) **Comparability** –the users of information need information that is presented in a way that makes it possible for them to compare performance of one public sector entity to another on a yearly basis**.**

(e) (i) **The auditor general**

Auditing of financial statements helps make people accountable for their performance.

Strengthens accountability and transparency in the public sector.

(ii) **The accountant general**

Financial policies development for improved financial performance.

Helps with timely coordination and production of government accounts;

(iii) **The secretary to the treasury**

Ensuring implementation of recommendations of Parliamentary Committee on Public Accounts.

Releasing of funds from the consolidated Fund for appropriation by controlling officers.

SOLUTION TWO

(a) **Objectivity**

As the files have been generated by Head – procurement and the individual involved approached you about need not to alert management of the shortcomings, by listening to their call, you will be operating under undue influence with no independence of making own decision. This is unacceptable and matter needs to be reporting to those in supervisory role for head – procurement.

Integrity

By agreeing with the head – procurement, there will be violation of integrity on my part as finance Director. Failure to be truthful.

Professional competency and due care

An accountant is expected to have reasonable knowledge of every other departmental operation in the organization as each activity has an impact on finance department hence the wrong doings by procurement team need to reach management via finance team.

Confidentiality

While confidentiality is important to abide by in every section of operation so as not to take advantage of information you come in contact with for personal expedience, if disclosure saves organization from loss of resources, it must be done. Like in the procurement case, disclosure needs to be made.

Professional behavior

Any professional that fails to adhere to above issues will be bringing discredit to their profession and are expected to be punished to deter others from committing similar offence.

(b)

-workshops
-organized training
-routine meetings
-through mission and value statements
-policy manual
-staff orientation at start of their employment
-disciplinary action against offenders
-existence of integrity and ethics committee

SOLUTION THREE

(a) **Calculation and commenting on any four (4) suitable ratios which can be used to measure the performance of the MPSA**

Suitable ratios	**2022**	**2021**
Calculations		
Operating margin = Operating profit X 100% / Revenue	325 X 100% / 6,500	249 X 100% / 4,980
	= 5%	**= 5%**

Comments

The operating profit margin is the same. This could indicate that pricing in the industry is regulated in order to protect the public.

Asset turnover = Revenue / Assets	6,500 / (7,000 + 3,000)	4,980 / (5,000 + 2,000)
	= 0.65 times	=0.71 times

Comments

The asset turnover has decreased. This could be due to the presence of non-performing assets and/or assets bought during the year due to political pressure but there was no need for them.

Calculation	**2022**	**2021**
Current ratio = Current assets / Current liabilities	3,000 / 4,000	2,000 / 1,500
	= 0.75:1	=1.33:1

Comments

The current ratio has decreased. This could be due to reduced inventory due to load shedding.

Revenue per employee = Revenue / No, of employees	K6,500,000 / 1,200	K4,980,000 / 600
	= K5,416.67	=K8,300

Comments

The revenue per employee has decreased. This could be due to a directive by Central Government to recruit more people and assist in reducing the unemployment rates.

(b) **Use of the ratio analysis in performance evaluation in the public sector**

- Ratio analysis is not as widespread in government as in the private sector.
- The primary problems are weaknesses in how key information needed for assessing financial condition is reported.

- Generally, ratios in government are effective only for certain units and generalized ratios are hard to compare from state to state since the unit of government is so large and complex.
- However, some notable success has been achieved in developing applicable ratios for interpreting the financial condition of local government and institutions of higher education.

(c) **Use of the balanced scorecard in performance evaluation in the public sector**

- The balanced scorecard is a widely recognized strategy-management framework that, since its inception by Kaplan and Norton in the early 1990s, has been adopted, modified, and applied by many entities, both public and private, worldwide.
- First developed as an enhanced performance measurement system, the balanced scorecard evolved into a holistic system for strategic execution.
- The balanced scorecard incorporates both financial (financial perspective) and non-financial (Customer, internal processes, and innovative and learning perspectives) indicators of performance.

SOLUTION FOUR

In line with IPSAS 40 Public Sector Combinations, explanation on how the following items of an acquired property should be dealt with at the date of acquisition.

i) Liabilities related to restructuring or exit activities

ii) Contingencies

(a) **Liabilities related to restructuring or exit activities**

For amalgamations, the standard requires use of the "modified pooling of interests" method of accounting, which is a variation of the pooling of interests method of accounting (also referred to as "merger accounting"), in which the amalgamation is recognized on the date it takes place.

For acquisitions, IPSAS 40 requires use of the "acquisition" method of accounting, applying the same approach as in IFRS 3, Business Combinations. This is supplemented with additional guidance for public sector specific situations.

IPSAS 40 also excludes from its scope the accounting for the formation of a joint arrangement in the financial statements of the joint arrangement itself

Applying the acquisition method of accounting requires:

• Identifying the acquirer;

• Determining the acquisition date;

• Recognizing and measuring the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquired operation; and

• Recognizing and measuring goodwill, a gain or loss from an acquisition.

The acquirer recognizes, separately from any goodwill recognized, the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquired operation. This may include items not previously recognized by the acquired operation.

The acquirer measures the identifiable assets acquired and the liabilities assumed at their acquisition-date fair values. IPSAS 40 provides limited exceptions to these

recognition and measurement principles. For example, contrary to IPSAS 19, Provisions, Contingent Liabilities and Contingent Assets, the acquirer recognizes a contingent liability assumed in an acquisition where consideration is transferred.

(b) **Contingencies**

Contingent consideration is usually an obligation of the acquirer to transfer additional assets or equity interests to the former owners of an acquired operation as part of the exchange for control of the acquired operation if specified future events occur or conditions are met. However, contingent consideration also may give the acquirer the right to their turn of previously transferred consideration if specified conditions are met.

IPSAS 19, Provisions, Contingent Liabilities and Contingent Assets, defines a contingent liability as:

(a) A possible obligation that arises from past events, and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or

(b) A present obligation that arises from past events, but is not recognized because:

(i) It is not probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation; or

(ii) The amount of the obligation cannot be measured with sufficient reliability.

Measurement

The requirements in IPSAS 19 do not apply in determining which contingent

liabilities to recognize as of the acquisition date. Instead, the acquirer shall

recognize as of the acquisition date a contingent liability assumed in an

acquisition where consideration is transferred if it is a present obligation that

arises from past events and its fair value can be measured reliably

Therefore, contrary to IPSAS 19, the acquirer recognizes a contingent liability assumed in an acquisition where consideration is transferred at the acquisition date even if it is not probable that an outflow of resources embodying economic

benefits or service potential will be required to settle the obligation.

Subsequent Accounting

After initial recognition and until the liability is settled, cancelled or expires, the acquirer shall measure a contingent liability recognized in an acquisition at the higher of:

(a) The amount that would be recognized in accordance with IPSAS 19; and

(b) The amount initially recognized less, if appropriate, cumulative amortization recognized in accordance with IPSAS 9, Revenue from Exchange Transactions.

This requirement does not apply to contracts accounted for in accordance with IPSAS 29

SOLUTION FIVE

(a) Input method – it uses total costs todate expressed as a % of total expected contract costs to completion to calculate degree of completion of contract upon which if overall contract outcome is known, the % is used to ascertain profit calculated. If overall outcome is not known, then no profit or loss is recognized.

Output method - it uses value of work certified todate expressed as a % of total contract price to completion to calculate degree of completion of contract upon which if overall contract outcome is known, the % is used to ascertain profit calculated. If overall outcome is not known, then no profit or loss is recognized.

(b) As the overall outcome of the contract is known, and it is expected to make a profit, the degree of completion of 60% would be applied to total expected cost to ascertain cost of sales and to contract price to ascertain recognizable sales by AFCON Construction.

(c) Relevant extracts will be as follows:

Overall profitability	
Revenue	5,000
Total costs(1500+800)	(2,300)
Total profitability	2,700

Profit and loss extract	K'000
Revenue (60%x5,000)	3,000
Cost of sales (60%*2,300)	<u>(1,380)</u>
Profit	<u>1,620</u>

Statement of Financial Position	
Costs todate	1,500
Profit	1,620
Invoiceable	3,120
Less invoiced	(1,000)
Contract assets	2,120
Receivable	100

END OF SOLUTIONS