



PUBLIC SECTOR FINANCIAL MANAGEMENT PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

PFM 2: LEGAL ASPECTS OF PUBLIC SECTOR FINANCE AND ADMINISTRATION

FRIDAY 13 DECEMBER 2024

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.
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8. Present legible and tidy work.
9. Graph paper (if required) is provided at the end of the answer booklet.

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SECTION A

This question is Compulsory and must be attempted.

QUESTION ONE–(COMPULSORY)

Democracy is defined as a government of the people, for the people and by the people. There are a number of characteristics of democracy such as the presence of an established system of laws; observance of the separation of powers; respect for the rule of law; carrying out activities such as judicial review; conducting free and fair elections and upholding human rights among other things.

Required:

With reference to the above scenario, answer the following questions:

- (a) Explain the significance of an established system of laws referred to above and explain its significance in Zambia's legal framework. (10 marks)
- (b) Explain the rationale behind the concept of separation of powers in a Government system. (10 marks)
- (c) A source of law is defined as a place where the law of a given place can be found. It symbolizes the origin of the law of a particular place. Every country has different documents that they may refer to as sources of law. Zambia equally has a number of sources of law which include the Constitution, Legislation, Judicial Precedent; Common Law and Equity.

Required:

Compare Legislation to the Constitution as sources of Law in Zambia.

(20 marks)

[Total: 40 Marks]

SECTION B

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

QUESTION TWO

- (a) Explain the sources of power for administrative agencies in Zambia. (10 marks)
- (b) The principle of separation of powers dictates that the powers of government must be divided amongst three organs namely the executive which is the nucleus of the government which formulate policy and consists of the President; Cabinet; the Civil Service and the Police service. The other organ is the Legislature which is in charge of formulating laws and consist of the members of Parliament. The Judiciary is the other organ of government. Of the three organs, the executive is the most powerful organs of government. Although according to the principles of separation of powers there is supposed to be a system of check and balance between the governmental powers.

Required:

Identify the organ that is the most appropriate in implementing the system of checks and balances and explain how this is done. (10 marks)

[Total: 20 Marks]

QUESTION THREE

- (a) Ululu country is situated in the North West of Africa. It recently gained independence in 2014. After that the President of Ululu formed Cabinet where he appointed Madam Power as one of his Cabinet Ministers. Madam Power excited with her new appointment, decided to pass a law that made it mandatory for all citizens to get Covid-19 vaccines. The people of Ululu state have expressed different feelings over this new pronouncements. They have approached you as an expert knowledgeable in administrative law, to find out if there is a way of dealing with this situation. (15 marks)
- (b) State two (2) advantages and two (2) disadvantages of using statutory instruments as a mechanism for law-making in Zambia. (4 marks)
- (c) Define a remedy in Judicial Review (1 mark)

[Total: 20 Marks]

QUESTION FOUR

- (a) Public administrative agencies being creations of statute are subject to judicial controls even though some statutes that establish them are subject to juridical control mechanisms. That still does not preclude judicial controls through the process of judicial review. The High court has powers in so far as controlling the manner in which administrative agencies make their decisions. There are also other alternative dispute resolutions mechanisms that are available in addressing some grievances that individuals may have arising from decisions of administrative agencies.

Required:

- (a) Describe an administrative agency. (10 marks)
- (b) Explain the differences between administrative law and constitutional law, in doing so, highlighting their respective scopes and focuses. (10 marks)

[Total: 20 Marks]

QUESTION FIVE

- (a) Explain the role of parliamentary question sessions in holding the Public Procurement Authority accountable and fostering transparency in procurement processes. (10 marks)
- (b) Describe the regulatory framework of the Zambia Revenue Authority in Zambia. (10 marks)

[Total: 20 Marks]

END OF PAPER

PFM 2 LEGAL ASPECTS OF PUBLIC SECTOR FINANCE AND ADMINISTRATION SOLUTIONS

SOLUTION ONE

- (a) The Constitution is the supreme law of a country, establishing the framework for its governance, rights, and duties of citizens, and the structure and powers of its institutions. In Zambia, the Constitution serves as the supreme law, providing the foundation for the organization and functioning of the state. It outlines the structure of government, including the executive, legislative, and judicial branches, and defines their respective powers and responsibilities.
- (b) The Constitution also guarantees fundamental rights and freedoms to all citizens, protecting them from governmental abuse and ensuring the rule of law. The constitution in Zambia establishes three organs that is the Judiciary, Executive and legislature. It is aimed at preventing arbitrary powers and ensuring political liberty. Its concept of checks and balances. This doctrine has been attributed to French Philosopher and aristocrat Baron Montesquieu. The reasoning for that was that because in the governance of a country there are these three functions that are performed that is administering the affairs of the state, discussing issues of national importance and making law and that of adjudication law. If the three are performed by different bodies and individuals, they would work as checks and balances. This concept operates on three limbs that seek to restrict absolute power. The rationale behind the separation of powers lies in the following principles:

Prevention of Tyranny: The separation of powers prevents the concentration of power in a single authority, reducing the risk of tyranny and abuse. By distributing powers among different branches, no single entity can dominate and oppress citizens.

Checks and Balances: It establishes a system of checks and balances where each branch has the authority to limit the actions of the other branches. This mutual oversight ensures that no branch exceeds its constitutional authority and helps maintain a balance of power.

Protection of Liberties: The separation of powers safeguards individual liberties by preventing any one branch from infringing upon the rights of citizens. The judiciary, for instance, acts as a check against legislative or executive actions that may violate constitutional rights.

Effective Governance: Dividing powers enhances the efficiency and effectiveness of governance. Each branch can focus on its specific functions without interference, leading to better decision-making and policy implementation.

Promotion of Accountability: The separation of powers fosters accountability as each branch is accountable for its own functions. This accountability is crucial in a democratic system, ensuring that officials are answerable for their actions to the public and other branches.

- (c) The Constitution of Zambia serves as the supreme law and plays a pivotal role in the legal framework;

Supremacy: The Constitution is supreme, meaning that any law inconsistent with its provisions is void to the extent of the inconsistency. It establishes the highest legal authority in Zambia.

Division of Powers: The Constitution outlines the distribution of powers among the executive, legislative, and judicial branches of government. It sets the foundation for the functioning of these institutions and their roles in law-making, law enforcement, and adjudication.

Protection of Rights: The Constitution guarantees fundamental rights and freedoms to individuals. It acts as a benchmark against which the validity of other laws is measured, ensuring that legislation aligns with constitutional principles.

Amendment Procedure: The Constitution provides a framework for its own amendment. Any changes to the Constitution must follow the specified procedures, emphasizing the significance of constitutional stability and adherence to established legal processes

Legislation plays a crucial role as a source of administrative law in Zambia for several reasons:

Granting and Limiting Powers: Statutory laws empower administrative agencies by conferring specific powers and duties upon them. These statutes define the scope of administrative authority, outlining what agencies can and cannot do in the execution of their functions.

Procedural Framework: Legislation establishes procedural frameworks for administrative decision-making. It prescribes the processes that administrative agencies must follow, including notice requirements, hearings, and the rights of affected parties, ensuring fair and transparent procedures.

Substantive Standards: Statutory laws set substantive standards that administrative agencies must adhere to when making decisions. These standards may include criteria for issuing permits, licenses, or regulatory decisions, ensuring that administrative actions are grounded in legal principles.

Enforcement Mechanisms: Legislative provisions often include enforcement mechanisms for administrative decisions. This may involve specifying penalties, fines, or other consequences for non-compliance with administrative orders, contributing to the effectiveness of administrative law.

Delegation of Powers: Legislation may delegate legislative authority to administrative agencies, allowing them to make rules and regulations within the scope defined by the statute. This delegation is subject to constitutional and legal limitations to prevent arbitrary exercises of power.

Amendment and Repeal: Legislative bodies have the authority to amend or repeal existing statutes, impacting the legal framework for administrative actions. Changes in statutory provisions may alter the powers, procedures, or standards applicable to administrative agencies.

In essence, legislation and statutes provide the statutory foundation for administrative law in Zambia, defining the legal parameters within which administrative bodies operate and ensuring accountability, transparency, and adherence to legal standards.

SOLUTION TWO

(a) Administrative agencies in Zambia derive their power from various sources, enabling them to fulfill their responsibilities effectively. The key sources of power for these agencies include:

Legislation:

Administrative agencies in Zambia derive power from statutes and laws passed by the legislature. These laws define the scope of the agency's authority, functions, and responsibilities.

Delegated Authority:

Administrative agencies often receive delegated authority from the government or specific statutes. The delegation of authority allows agencies to act on behalf of the government within a particular domain. The Zambia Revenue Authority, for example, is delegated authority to collect taxes and customs duties.

Rulemaking and Regulations: Agencies have the power to make rules and regulations that further specify how laws should be implemented. The Zambia Procurement Authority, through its regulatory powers, issues guidelines and regulations to govern procurement, and ensuring consumer protection.

Adjudicative Powers:

Some agencies have quasi-judicial powers, allowing them to resolve disputes and make decisions in legal matters.

(b) The Judiciary in Zambia performs various functions, including:

Interpretation of Laws: The judiciary is responsible for interpreting laws, including the constitution. Courts ensure that laws are applied consistently and in line with constitutional principles.

Dispute Resolution: The judiciary resolves legal disputes through fair and impartial hearings. This includes civil, criminal, and constitutional cases.

Protection of Rights: Courts protect the rights and liberties of individuals by ensuring that laws and government actions comply with constitutional guarantees.

Judicial Review: The judiciary has the power of judicial review, allowing it to review the constitutionality of laws and government actions. This ensures that they align with the constitution.

Adjudication of Criminal Cases: Courts hear criminal cases, ensuring that justice is served and individuals accused of crimes receive fair trials.

Independence: The judiciary must operate independently to uphold the rule of law. Judges are expected to make decisions based on legal principles, free from political influence.

SOLUTION THREE

(a) A statutory instrument (S.I) is delegated legislation passed by Ministers under powers conferred on them by an act of parliament. A Statutory Instrument is any delegated legislation. Statutory Instruments are very important sources of administrative law as they make the process of Public Administration Smooth and supplement provisions of the act of parliament. Statutory Instruments ensure there is no gap in the law at any one time to address issues as they may rise in society. The ease with which they are created ensures the continuation of public administration functions and provisions of services to the public. However, they are not stand alone laws but are passed pursuant to the mother act. If they are in conflict with enabling act they would be adjudged ultra vires. See. Attorney general v The Local Government Election Commission.

(b) Advantages and Disadvantages of SIs

Advantages:

Flexibility: SIs provide flexibility for quick and targeted legal changes without the need for lengthy parliamentary processes.

Efficiency: They allow for the detailed regulation of complex matters, ensuring laws can adapt promptly to evolving situations.

Technical Expertise: SIs permit experts in specific fields to draft detailed regulations, enhancing the technical quality of legislation.

Disadvantages:

Limited Scrutiny: The fast-track nature of SIs may result in limited parliamentary scrutiny, raising concerns about accountability.

Potential Abuse: There's a risk of misuse of powers granted by the parent Act, leading to regulations that go beyond the intended scope.

Democratic Deficit: Critics argue that SIs may bypass the democratic process, as they are not subjected to the same level of public and parliamentary debate as primary legislation.

(c) A remedy is any method available at law for the enforcement protection or recovery of rights or for obtaining redress for their infringement

SOLUTION FOUR

- (a) Administrative agencies in Zambia, like in many other countries, play a crucial role in governance and regulation. Here are some brief notes on administrative agencies in Zambia: Administrative agencies in Zambia are bodies established by the government to implement and enforce specific laws and regulations. They serve various functions such as regulation, adjudication, licensing, and oversight across different sectors of the economy. While administrative agencies operate under the authority of the government, they are often designed to function independently within their respective domains. This independence helps ensure impartiality and effectiveness in carrying out their mandates. These agencies are responsible for overseeing compliance with laws and regulations within their sectors. For example, agencies like the Zambia Revenue Authority (ZRA) oversee tax compliance. Administrative agencies issue licenses, permits, and certifications necessary for conducting business or practicing certain professions. Some administrative agencies in Zambia have quasi-judicial powers, allowing them to adjudicate disputes and enforce compliance through administrative proceedings. This helps in resolving conflicts and maintaining order within regulated industries. Administrative agencies are expected to operate transparently and be accountable for their actions. They often publish reports, hold public hearings, and engage stakeholders to ensure accountability and foster trust in their operations. Overall, administrative agencies in Zambia play a vital role in ensuring regulatory compliance, providing public services, and facilitating economic activities. However, addressing challenges and ensuring their effective functioning remains an ongoing concern for policymakers and stakeholders.
- (b) Constitutional law is concerned with the aspect of constituting a state. This involves establishing institutes of government and conferring on them the power they have. Constitution is said to be static law, because it does not make any specific provisions as to the manner the administrative functions of the state are to be conducted. Administrative law looks at the day to day administrative functions of administrative bodies. It establishes public administrative institutions and ensures there is a benchmark against which these administrative institutions will be assessed to ensure conformity with the law. Administrative law provides checks by way of Judicial review. This aspect is applied daily in administrative law there it is considered a law in motion. Although constitutional law may be considered more supreme in status Administrative Law is more important in the day to day running of a country. Administrative law governs the activities of administrative agencies and ensures they act within the scope of their authority and in accordance with legal principles.
- It regulates the relationship between citizens and government agencies, providing mechanisms for accountability and fairness in administrative decision-making. Administrative law encompasses principles of natural justice, procedural fairness, and judicial review, which ensure that administrative actions are lawful, reasonable, and justifiable.

SOLUTION FIVE

(a) Role of Parliamentary Question Sessions:

Members of Parliament can use question sessions to seek information from the PPA regarding specific procurement activities, policies, or challenges. This promotes transparency by ensuring that relevant information is disclosed to the public through parliamentary proceedings. Question sessions serve as an accountability mechanism, allowing MPs to directly question PPA officials about their decisions, actions, and overall performance. This contributes to public scrutiny and trust in the procurement process. MPs may use question sessions to engage in discussions about procurement policies, seeking clarifications or proposing changes. This dialogue fosters a transparent and informed approach to procurement-related matters. Question sessions contribute to public awareness of the PPA's activities and decisions, ensuring that citizens are informed about the procurement processes and policies. Through questions and responses, the PPA can address concerns raised by MPs, demonstrating a responsive and accountable approach to governance in the procurement sector. The open questioning process acts as a deterrent to corrupt practices, as the PPA is accountable for its actions and decisions in a public forum.

- (b) As a public body the authority is amenable to judicial review as a means to regulating its functions. There are provisions in the Act that provide for the regulatory framework of the authority and the manner to address grievances that may arise. where an applicant is dissatisfied by the decision of the authority they have further recourse to Revenue Appeals Tribunal as provided in the Customs and Excise Act. The authority accounts to parliament through the minister of finance. at the end of each year a financial report is presented to the minister. Section 25 of the Zambia Revenue Authority Act requires the agency to present a financial report to the Minister of Finance.

END OF SOLUTIONS



PUBLIC SECTOR FINANCIAL MANAGEMENT PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

PFM 4: PUBLIC SECTOR FINANCIAL MANAGEMENT

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SECTION A

This question is Compulsory and must be attempted.

QUESTION ONE

A team of experts from Zambee, a country in East Africa, was sent to Morona, a country in the Northern Part of Africa. This team was comprised of experts in engineering, urban planning, financial and banking sectors. Also in the entourage were two (2) members of the main opposition party. This was to ensure inclusiveness. The leader of the delegation was from the ruling political party. There was an extensive stakeholder engagement process before the Government decided to constitute this team which travelled to Morona.

The nation of Morona in 2022, hoisted a senior world cup soccer tournament which was successful. This nation was able to attract private investors in the transport and hotel sectors, among others. Further, the country, as a host nation, used a Private Public (PPP) model in the road and rail rehabilitation. They started preparing to bid four (4) years earlier before they were awarded the bid to hoist this prestigious tournament.

The terms of reference of the team from Zambee sent to Morona involved the learning of the best practices on the strategies and techniques used by Morona to win the bid to hoist the senior world cup tournament. The reason being that Zambee has decided to bid to hoist the Senior African Cup Football tournament in the next five (5) years. They learnt from the visit that the host country must plan well in advance. The planning should include the building and rehabilitation of the existing infra-structure which includes stadia, road network and ensuring that cleanliness of municipalities is implemented well in advance.

The report, of the Zambee team included:

- (1) A section on two (2) monthly rolling prizes of K30,000 and K100,000 to be introduced by the councilors which will be given to the cleanest household and municipality respectively.
- (2) An independent team of assessors to be selected whose responsibility would be to ensure that they carry out the assessment based on the assessment tool developed by this team.

The source of funds for this exercise will be Non-Tax Revenue and will be provided for in the National Budget.

The Government of Zambee further appointed eminent nationals that constituted a Task Force to oversee the preparation and the actualization of the hoisting of the senior men's African Football tournament that they plan to hoist. Members of this team had representatives from different ministries with various professional backgrounds.

As part of the preparation, three (3) cities were identified to have new stadiums built. Apart from the stadiums, it was agreed that some space be made available in these cities for modern shopping complexes to be built. These shopping complexes were to be of high standard and the private sector was invited to bid in the building of these shopping complexes under the Public Private Partnerships.

In evaluating the received bids as a response to the advertisement, a total of three (3) companies were selected. Both technical and financial bids were submitted by these firms. The financial

evaluation was done. This involved the use of Net Present Value (NPV). All the three companies presented very strong arguments regarding corporate social responsibility in the towns they will build modern shopping complexes. These are the towns where some games will be played.

Gouila Plc is considering to invest an initial cash outlay of K3,000,000 in the project known as Project A to construct a facility at the shopping mall, Kilotia Investments intends to have an initial investment of K1,000,000 in Project B to construct another facility at the shopping Mall and Hehi Ltd anticipates to construct another facility with a net initial outlay of K2,500,000. All of these projects facilities will have an estimated life span of four (4) years.

The Net cash inflows with related probabilities by each company for their project facilities have been estimated as follows:

GOUILA PLC

YEAR	PROBABILITY	K
0		(3,000,000)
1	0.40	2,000,000
2	0.30	4,000,000
3	0.50	3,000,000
4	0.45	4,600,000

KILOTIA INVESTMENT LTD

YEAR	PROBABILITY	K
0		(1,000,000)
1	0.30	2,000,000
2	0.20	3,000,000
3	0.40	2,000,000
4	0.35	4,000,000

HEHI LTD

YEAR	PROBABILITY	K
0		(2,500,000)
1	0.20	3,000,000
2	0.40	1,700,000
3	0.10	2,500,000
4	0.15	3,500,000

It has been indicated in the bid document that the first project facility with the highest NPV will be implemented first, followed by the one with second highest, and lastly to be considered will be the one with the lowest. Further, if the NPV is negative, then that project will be automatically rejected.

Assume a risk free discount rate of 15%

Required:

- Calculate the Net Present Value (NPV) for each project proposal and discuss the findings. (18 marks)
- Explain the other methods you can use for project appraisal. (5 marks)
- Explain the various types of Non-Tax Revenue as a source of government revenue

(12 marks)

- (d) Discuss any three (3) groups who are key stakeholders, with regards to public sector financial management and give specific examples of internal and external stakeholders for a government institution. (5 marks)

[Total: 40 Marks]

SECTION B

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

QUESTION TWO

You are appointed as the Internal Controls Manager for a Government printing department tasked with producing secure and sensitive documents such as official Government publications. The department is also responsible for production of National Identity Cards and Passports.

It is responsible for ensuring the integrity, confidentiality, and accuracy of these documents to maintain public trust and national security. Given the critical nature of the documents produced, the Government has expressed concern about potential security breaches, unauthorized access and the need for enhanced internal controls.

The government recently suspended the production of National Identity Cards and Passports because of weaknesses in internal controls identified by government auditors from the Auditor General's office during a recent audit.

Required:

- (a) As the newly appointed Internal Controls Manager outline a comprehensive plan for strengthening internal controls within the government printing department. Your plan should address at least five (5) challenges associated with the production of secure and sensitive documents. (15 marks)
- (b) Explain five (5) benefits of an internal control system to an organization. (5 marks)

[Total: 20 Marks]

QUESTION THREE

You have recently been appointed as the Budget Manager for Mala local authority which is experiencing complex financial challenges. The Local Authority serves a diverse community, managing public services such as education, public safety, waste management, and community development. Due to changing demographics, economic conditions, and increasing demands for improved services, effective budget preparation is crucial to address community needs while ensuring financial sustainability and regulatory compliance.

As the newly appointed Budget Manager for the Local Authority, you are tasked with overseeing the budget preparation process for the upcoming fiscal year for Mala local authority.

Mala Local authority has been running a budget deficit for many years. During a recent full council meeting, the councilors wanted to know the reasons why the council has been running a budget deficit for many years.

Required:

- (a) Explain the stages in the budget preparation process for Mala local authority. (15 marks)

- (b) Explain the difference between a supplementary budget and a deficit budget. (5 marks)

[Total: 20 Marks]

QUESTION FOUR

An extract of the 2022 - 2024 National budget is presented below:

Source	2024 Budget		2023 Budget		2022 Budget	
	<i>Amount (‘K’ Billion)</i>	<i>Share of Budget (%)</i>	<i>Amount (‘K’ Billion)</i>	<i>Share of Budget (%)</i>	<i>Amount (‘K’ Billion)</i>	<i>Share of Budget (%)</i>
Domestic Revenue	141.11	79	111.64	66.7	98.86	57
Domestic Financing	16.33	9.3	15.58	9.3	24.46	14
Foreign Financing	17.01	9.7	38.4	23	47.85	28.22
Grants	3.44	2	1.71	1	1.82	0.78
Total Budget	177.89	100	167.33	100	172.99	100

The 2024 budget reveals an increase in domestic revenue from K98.8 billion in 2022 to K141.11 billion in 2024. In addition, domestic revenue accounted for 57% share of the budget in 2022 compared to 79% in 2024.

The 2024 budget reveals a decrease in domestic financing from K24.46 billion in 2022 to K16.33 billion in 2024. In addition, domestic financing accounted for 14% share of the budget in 2022 compared to 9.3% in 2024.

Required:

- (a) Explain the following terms and give three (3) examples of each.
- (i) Domestic revenue. (5 marks)
 - (ii) Domestic financing. (5 marks)
- (b) Explain the difference between foreign financing and grants. (4 marks)
- (c) Explain three (3) functions of the national budget in the Zambian economy. (6 marks)

[Total: 20 Marks]

QUESTION FIVE

Public sector institutions are embracing efforts to implement risk management policies. They are encouraging institutions and departments to catalogue risks. At a recent meeting of Permanent Secretaries, institutions were implored to develop measures to prioritize risks so that organizations are prepared to respond to them in an appropriate manner. The Secretary to the Cabinet indicated that the reason risk management is being emphasized is because "the environment in which we are operating is constantly evolving at a quick pace and it is therefore important that the public sector focuses at the right risks, at the right time and in the right ways".

Required:

You are the Director of Finance in the Ministry of Works and the Permanent Secretary has requested your office to prepare a presentation. Your presentation should cover the following parts (a) and (b) on risk management including:

- | | | |
|-----|--|------------|
| (a) | (i) Definition of risk Assessment. | (3 marks) |
| | (ii) challenges of risk assessment and | (3 marks) |
| | (iii) Conclusion and recommendations. | (4 marks) |
| (b) | Explaining the three (3) types of risk Assessment. | (10 marks) |

[Total: 20 Marks]

END OF PAPER

Formulae

Modigliani and Miller Proposition 2 (with tax)

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

Two asset portfolio

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

The Capital Asset Pricing Model

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

The asset beta formula

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

The Growth Model

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

Gordon's growth approximation

$$g = br_e$$

The weighted average cost of capital

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

The Fisher formula

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

Purchasing power parity and interest rate parity

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

Modified Internal Rate of Return

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

The Black-Scholes option pricing model

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

Where:

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

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

The Put Call Parity relationship

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

Present Value Table

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

Where r = discount rate

n = number of periods until payment

		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	0.941	0.837	0.766	0.703	0.645	0.592	0.544	0.500	0.460	0.424	9
10	0.905	0.820	0.744	0.676	0.614	0.558	0.508	0.463	0.422	0.386	10
11	0.896	0.804	0.722	0.650	0.585	0.527	0.475	0.429	0.388	0.305	11
12	0.887	0.788	0.701	0.625	0.557	0.497	0.444	0.397	0.356	0.319	12
13	0.879	0.773	0.681	0.601	0.530	0.469	0.415	0.368	0.326	0.290	13
14	0.870	0.758	0.661	0.577	0.505	0.442	0.388	0.340	0.299	0.263	14
15	0.861	0.743	0.642	0.555	0.481	0.417	0.362	0.315	0.275	0.239	15
(n)	11%	12%	13%	14%	15%	16%	17%	18%	19%	20%	
1	0.901	0.893	0.885	0.877	0.870	0.862	0.855	0.847	0.840	0.833	1
2	0.812	0.797	0.783	0.769	0.756	0.743	0.731	0.718	0.706	0.694	2
3	0.731	0.712	0.693	0.675	0.658	0.641	0.624	0.609	0.593	0.579	3
4	0.659	0.636	0.613	0.592	0.572	0.552	0.534	0.516	0.499	0.482	4
5	0.593	0.567	0.543	0.519	0.497	0.476	0.456	0.437	0.419	0.402	5
6	0.535	0.507	0.480	0.456	0.432	0.410	0.390	0.370	0.352	0.335	6
7	0.482	0.452	0.425	0.400	0.376	0.354	0.333	0.314	0.296	0.279	7
8	0.434	0.404	0.376	0.351	0.327	0.305	0.285	0.266	0.249	0.233	8
9	0.391	0.361	0.333	0.308	0.284	0.263	0.243	0.225	0.209	0.194	9
10	0.352	0.322	0.295	0.270	0.247	0.227	0.208	0.191	0.176	0.162	10
11	0.317	0.287	0.261	0.237	0.215	0.195	0.178	0.162	0.148	0.135	11
12	0.286	0.257	0.231	0.208	0.187	0.168	0.152	0.137	0.124	0.112	12
13	0.258	0.229	0.204	0.182	0.163	0.145	0.130	0.116	0.104	0.093	13
14	0.232	0.205	0.181	0.160	0.141	0.125	0.111	0.099	0.088	0.078	14
15	0.209	0.183	0.160	0.140	0.123	0.108	0.095	0.084	0.074	0.065	15

Annuity Table

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

Where r = discount rate
 n = number of periods

		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

Standard normal distribution table

	0.00	0.01	0.02	0.03	0.04	0.05	0.06	0.07	0.08	0.09
0.0	0.0000	0.0040	0.0080	0.0120	0.0160	0.0199	0.0239	0.0279	0.0319	0.0359
0.1	0.0398	0.0438	0.0478	0.0517	0.0557	0.0596	0.0636	0.0675	0.0714	0.0753
0.2	0.0793	0.0832	0.0871	0.0910	0.0948	0.0987	0.1026	0.1064	0.1103	0.1141
0.3	0.1179	0.1217	0.1255	0.1293	0.1331	0.1368	0.1406	0.1443	0.1480	0.1517
0.4	0.1554	0.1591	0.1628	0.1664	0.1700	0.1736	0.1772	0.1808	0.1844	0.1879
0.5	0.1915	0.1950	0.1985	0.2019	0.2054	0.2088	0.2123	0.2157	0.2190	0.2224
0.6	0.2257	0.2291	0.2324	0.2357	0.2389	0.2422	0.2454	0.2486	0.2517	0.2549
0.7	0.2580	0.2611	0.2642	0.2673	0.2704	0.2734	0.2764	0.2794	0.2823	0.2852
0.8	0.2881	0.2910	0.2939	0.2967	0.2995	0.3023	0.3051	0.3078	0.3106	0.3133
0.9	0.3159	0.3186	0.3212	0.3238	0.3264	0.3289	0.3315	0.3340	0.3365	0.3389
1.0	0.3413	0.3438	0.3461	0.3485	0.3508	0.3531	0.3554	0.3577	0.3599	0.3621
1.1	0.3643	0.3665	0.3686	0.3708	0.3729	0.3749	0.3770	0.3790	0.3810	0.3830
1.2	0.3849	0.3869	0.3888	0.3907	0.3925	0.3944	0.3962	0.3980	0.3997	0.4015
1.3	0.4032	0.4049	0.4066	0.4082	0.4099	0.4115	0.4131	0.4147	0.4162	0.4177
1.4	0.4192	0.4207	0.4222	0.4236	0.4251	0.4265	0.4279	0.4292	0.4306	0.4319
1.5	0.4332	0.4345	0.4357	0.4370	0.4382	0.4394	0.4406	0.4418	0.4429	0.4441
1.6	0.4452	0.4463	0.4474	0.4484	0.4495	0.4505	0.4515	0.4525	0.4535	0.4545
1.7	0.4554	0.4564	0.4573	0.4582	0.4591	0.4599	0.4608	0.4616	0.4625	0.4633
1.8	0.4641	0.4649	0.4656	0.4664	0.4671	0.4678	0.4686	0.4693	0.4699	0.4706
1.9	0.4713	0.4719	0.4726	0.4732	0.4738	0.4744	0.4750	0.4756	0.4761	0.4767
2.0	0.4772	0.4778	0.4783	0.4788	0.4793	0.4798	0.4803	0.4808	0.4812	0.4817
2.1	0.4821	0.4826	0.4830	0.4834	0.4838	0.4842	0.4846	0.4850	0.4854	0.4857
2.2	0.4861	0.4864	0.4868	0.4871	0.4875	0.4878	0.4881	0.4884	0.4887	0.4890
2.3	0.4893	0.4896	0.4898	0.4901	0.4904	0.4906	0.4909	0.4911	0.4913	0.4916
2.4	0.4918	0.4920	0.4922	0.4925	0.4927	0.4929	0.4931	0.4932	0.4934	0.4936
2.5	0.4938	0.4940	0.4941	0.4943	0.4945	0.4946	0.4948	0.4949	0.4951	0.4952
2.6	0.4953	0.4955	0.4956	0.4957	0.4959	0.4960	0.4961	0.4962	0.4963	0.4964
2.7	0.4965	0.4966	0.4967	0.4968	0.4969	0.4970	0.4971	0.4972	0.4973	0.4974
2.8	0.4974	0.4975	0.4976	0.4977	0.4977	0.4978	0.4979	0.4979	0.4980	0.4981
2.9	0.4981	0.4982	0.4982	0.4983	0.4984	0.4984	0.4985	0.4985	0.4986	0.4986
3.0	0.4987	0.4987	0.4987	0.4988	0.4988	0.4989	0.4989	0.4989	0.4990	0.4990

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

PFM 4 PUBLIC SECTOR FINANCIAL MANAGEMENT SOLUTIONS

SOLUTION ONE

(a) Start by determining the Present Value Factors for each Year. These factors are the ones that will be applied for all the three Project facilities from the bidding companies.

Year 1	$1 \div (1+15\%)^1 = 0.8696$
Year 2	$1 \div (1+15\%)^2 = 0.7561$
Year 3	$1 \div (1+15\%)^3 = 0.6575$
Year 4	$1 \div (1+15\%)^4 = 0.5717$

- Gouila Plc: Project facility (A) NPV Calculation:**

Net Cash Flows:

Year	1	2	3	4
Adj.Net Cash Flow	800,000	1,200,000	1,500,000	2,070,000
X Present Value Factor	0.8696	0.7561	0.6575	0.5717
PV Cash Flows	695,680	907,320	986,250	1,183,419

Total PV Inflows = K3,772,669

Initial Investment = (K3,000,000)

Net Present Value = +K772,669

- Kilotia Investment Ltd: Project facility (B) NPV Calculation**

Net Cash Flows:

Year	1	2	3	4
Net Cash Flows	2,000,000	3,000,000	2,000,000	4,000,000
Prob.	0.3	0.2	0.4	0.35
Adj.	600,000	600,000	800,000	1,400,000

Year	1	2	3	4
Adj.Net Cash Flow	600,000	600,000	800,000	1,400,000

X Present Value Factor	0.8696	0.7561	0.6575	0.5717
PV Cash Flows	521,760	453,660	526,000	800,380

Total PV Inflows = K2,301,800

Initial Investment=(K3,000,000)

Net Present Value= K(698,200)

- Hehi Ltd: Project facility: Project facility (C) NPV Calculation**

Net Cash Flows:

Year	1	2	3	4
Net Cash Flows	3,000,000	1,700,000	2,500,000	3,500,000
Prob.	0.2	0.40	0.10	0.5
Adj.	600,000	680,000	250,000	1,750,000

Year	1	2	3	4
Adj.Net Cash Flow	600,000	680,000	250,000	1,750,000
X Present Value Factor	0.8696	0.7561	0.6575	0.5717
PV Cash Flows	521,760	514,148	164,375	1,000,475

Total PV Inflows = K2,200,758

Initial Investment=(K3,000,000)

Net Present Value= K(799,242)

Discussion:

The present value factors used in discounting the adjusted cash flows for all the three projects was the same considering that the risk free used was at 15%.

The Net Cash flows for each project were adjusted by the probability of their occurrence. This resulted into using the Adjusted Cash Flows for each year taking into account their probability of there being achieved as stated in the question.

By using the Net Present Value (NPV) method of evaluation,

Gouila Plc, Project facility (A) will be selected and be implemented because it has resulted into a Positive NPV of K772, 669.

It should be noted that all the three projects have the same initial investment outflow of K3, 000, 000. Project (B) and (C) have negative NPVs of (K698, 200) and (799,242) respectively.

(b). The other methods that are used for project appraisal include the following:

i. Accounting Rate of Return (ARR)

This is also used to estimate whether or not to proceed with a particular investment. In order to calculate the IRR, the calculation uses the accounting profit from the project divided by the initial investment in the project. The projected would then be accepted in the event that the measure yields a percentage that is more than a certain hurdle rate used the firm as its acceptable minimum rate of return.

ii. Pay Back Period (Pbp) Method/Approach

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.*

iii. Profitability Index Method

The Profitability Index (PI) measures the ratio between the present value of future cash flows and the initial investment. The index is a useful tool for ranking investment projects and showing the value created per unit of investment.

(c). Types of Non-tax Revenues as non-tax revenue include the following:

i. Fees

This is charged by public authorities for providing a service to its citizens.

ii. Fines and Penalties

Penalties and fees are imposed as a form of punishment for breach of law or non-fulfillment or for failure to observe some regulations.

iii Surplus from Public Enterprises

Revenues are also obtained by Government by way of surplus from public enterprises.

iv Special assessment of betterment levy

This is a special charge levied on selected community residents who are beneficiaries of certain government activities or public projects.

v Grants and Gifts

Grants are non- compulsory recurrent or capital transfers received by a government unit from another government unit and is usually obtained from an international organization.

Gifts are voluntary contributions by individuals or institutions to the government.

vi Deficit Financing

Deficit implies an excess of public expenditure over revenue. This excess may be financed by borrowings from abroad, by the central bank creating currency.

(d). Stakeholders are individuals or institutions that have an influence in a situation. They can be both internal and external. For a Government Institution, internal and external stakeholders can be identified as follows:

Internal Stakeholders

- Employees
- Procurement
- Board Members

External Stakeholders

- Revenue Authority
- Service Users
- Customers
- Suppliers
- Funders
- Quality assessors
- Special interest
- Society
- Media

SOLUTION TWO

(a) **Five (5) internal controls suitable for a government printing department:**

1. Access Controls: Implement a strict access control system to ensure that only authorized personnel have access to specific areas and information within the printing facility. Use electronic key cards, biometric authentication, or other secure methods to restrict entry.
2. Document Tracking System: Develop a robust document tracking and tracing system to monitor the movement of documents throughout the production process. Utilize barcodes, RFID technology, or other tracking mechanisms to maintain transparency and accountability.
3. Quality Assurance Checks: Establish a comprehensive quality assurance program with regular checks at various stages of the production process. Conduct inspections to ensure the accuracy, completeness, and quality of printed documents, minimizing the risk of errors.
4. Data Encryption and Security Measures: Implement strong data encryption protocols to safeguard sensitive information contained in official documents. Ensure that data storage systems and communication channels are secure to prevent unauthorized access or data breaches.
5. Restricted Printing Equipment Access: Restrict access to printing equipment and machinery to only trained and authorized personnel. Implement controls to prevent unauthorized use of printing facilities and reduce the risk of document forgery.
6. Vendor and Supplier Management: Establish a vendor and supplier management system to ensure the reliability and integrity of materials supplied for document production. Regularly assess and monitor the performance of external partners to maintain quality standards.
7. Employee Training and Awareness Programs: Develop training programs to educate employees on the importance of internal controls, security protocols, and their role in maintaining the integrity of official documents. Regularly update training to address emerging risks and technologies.
8. Secure Document Storage: Implement secure storage facilities for finished and intermediate products. Ensure that access to storage areas is restricted, and use surveillance systems to monitor and deter unauthorized access.
9. Incident Response Plan: Develop a comprehensive incident response plan to address security breaches, unexpected disruptions, or emergencies. Define clear procedures for reporting incidents, conducting investigations, and implementing corrective actions to minimize the impact.
10. Regular Internal Audits: Conduct regular internal audits of the internal control systems to assess their effectiveness and compliance with established procedures. Internal audits help identify potential weaknesses, ensure ongoing compliance, and support continuous improvement efforts.

These internal controls are designed to enhance the security, integrity, and efficiency of a government printing department, addressing specific risks associated with the production of sensitive and official documents.

(b)

An internal control system provides numerous benefits for an organization. Here's an outline of some key advantages:

1. **Safeguarding Assets:** Internal controls help protect an organization's assets, including physical assets such as equipment and inventory, as well as intangible assets like intellectual property and sensitive information. This reduces the risk of theft, fraud, or misuse.
2. **Preventing and Detecting Fraud:** A well-designed internal control system includes measures to prevent and detect fraud. By establishing segregation of duties, implementing checks and balances, and conducting regular audits, organizations can minimize the likelihood of fraudulent activities.
3. **Ensuring Accuracy of Financial Information:** Internal controls play a crucial role in ensuring the accuracy and reliability of financial information. This is essential for making informed business decisions, meeting regulatory requirements, and maintaining the trust of stakeholders such as investors and creditors.
4. **Promoting Operational Efficiency:** Effective internal controls streamline operational processes by defining clear procedures and responsibilities. This helps reduce inefficiencies, minimize errors, and enhance overall organizational performance.
5. **Compliance with Regulations:** Internal controls assist organizations in complying with legal and regulatory requirements. This is particularly important in highly regulated industries, where failure to comply can result in fines, legal actions, and damage to the organization's reputation.
6. **Enhancing Decision-Making:** With accurate and reliable information, decision-makers can make informed and timely decisions. Internal controls contribute to the availability of trustworthy data, supporting strategic planning, resource allocation, and performance evaluation.
7. **Risk Management:** Internal controls are instrumental in identifying and mitigating risks. By assessing potential risks to the organization's objectives, internal controls help management make informed decisions about risk tolerance and develop strategies to manage and mitigate risks effectively.
8. **Promoting Accountability:** Clearly defined roles and responsibilities within an internal control system promote accountability among employees. Individuals are held responsible for their assigned tasks, which fosters a culture of accountability and integrity within the organization.

SOLUTION THREE

(a) The following are common stages in the budget preparation process:

1. **Budget Guidelines and Instructions.**
The process often begins with the issuance of budget guidelines and instructions from higher levels of government. These guidelines provide an overview of financial priorities, expectations, and any specific requirements for the upcoming budget cycle.
2. **Community needs assessment**
Conduct a comprehensive assessment of the community's needs. Engage with residents, businesses, community organizations, and other stakeholders to identify priorities and gather input on the services and programs they consider essential.
3. **Revenue forecasting.**
Analyze historical data, economic indicators, and potential changes in tax policies to forecast available revenues for the upcoming fiscal year. Consider various revenue streams, including property taxes, grants, fees, and other sources of income.
4. **Departmental Budget Requests.**
Engage with department heads and managers to gather their budget requests. Departments typically submit detailed plans outlining their financial needs for personnel, operations, capital projects, and other expenditures. These requests should align with the local authority's strategic goals.
5. **Budget Workshops and meetings.**
Organize workshops and meetings with key stakeholders, including department heads, elected officials, and sometimes members of the public. These sessions provide an opportunity to discuss budget priorities, address concerns, and ensure that the proposed budget aligns with community needs and expectations.
6. **Budget Development.**
Develop the preliminary budget based on the revenue forecasts and departmental requests. This involves allocating resources to different service areas, prioritizing expenditures, and ensuring that the budget reflects the local authority's strategic objectives.
7. **Review and adjustments.**
Conduct a thorough review of the preliminary budget to ensure accuracy, feasibility, and compliance with regulations. Adjustments may be necessary based on changing circumstances, unforeseen events, or feedback received during budget workshops.
8. **Public consultation**
Engage in public consultation to enhance transparency and gather feedback on the proposed budget. Local authorities may hold public hearings, forums, or use online platforms to allow residents to express their opinions on budget priorities and allocations.
9. **Approval process.**
Submit the proposed budget to the ministry of local government for approval. Elected officials review the budget, discuss proposed allocations, and may make amendments before approving the final budget.
10. **Implementation and monitoring.**
Once approved, the budget is implemented, and financial activities are monitored throughout the fiscal year. Regular reports and updates are provided to elected officials and the public to track the local authority's financial performance against the approved budget.

11. Audit and evaluation.

Conduct an audit or evaluation at the end of the fiscal year to assess the local authority's financial performance, adherence to budgetary goals, and overall effectiveness of the budget preparation process. This information informs improvements for future budget cycles.

These stages in the budget preparation process help local authorities align financial resources with community needs, ensure transparency and accountability, and maintain fiscal responsibility.

(b)

The main difference between a supplementary budget and a budget deficit lies in their nature, purpose, and how they impact an organization's financial planning. Let's define each term:

A supplementary budget is an additional budget that is prepared and implemented during the fiscal year, typically after the approval of the main (original) budget. It is used when unforeseen circumstances, new priorities, or changes in economic conditions necessitate adjustments to the initial budget. The supplementary budget allows for modifications to allocations, revenues, and expenditures to address emerging needs or unexpected developments.

A budget deficit occurs when a government, organization, or individual's expenditures exceed its revenues within a specific period, typically a fiscal year. In other words, it reflects a situation where there is a shortfall or negative balance between the total planned spending and the total revenue generated. A budget deficit may result from various factors, including economic downturns, increased spending commitments, or a decline in revenue sources.

SOLUTION FOUR

(a) Domestic Revenue:

Domestic revenue refers to the funds generated by a government from within its own borders through various sources. It constitutes the income that a government collects internally to finance its operations, public services, and development projects. Domestic revenue is crucial for sustaining government activities and reducing dependency on external sources for funding.

Examples of Domestic Revenue:

1) Tax Revenue:

Taxation is a primary source of domestic revenue. Governments levy various taxes on individuals, businesses, and other entities to generate income. Examples include income taxes, corporate taxes, sales taxes, property taxes, and excise taxes. The revenue collected from these taxes contributes significantly to the domestic revenue pool.

2) Customs and Import Duties:

Revenue generated from customs duties and import tariffs on goods and services entering the country is another form of domestic revenue. Governments can adjust these duties to control imports, protect domestic industries, and raise revenue simultaneously.

3) Non-Tax Revenue:

Non-tax revenue comprises income generated by the government through means other than taxation. This includes fees, fines, licenses, and income from government-owned enterprises. For example, fees charged for government services, fines imposed for regulatory violations, and income from state-owned utilities contribute to the domestic revenue stream.

These examples illustrate the diverse ways in which a government can generate revenue from sources within its own borders, enabling it to fund public services, infrastructure development, and other essential functions.

(b) Domestic financing

Domestic financing refers to the process through which a government raises funds from within its own country to meet its financial needs. It involves the issuance of debt instruments or other financial instruments within the domestic market to cover budgetary gaps, fund public projects, or manage deficits. Domestic financing is an essential component of a government's fiscal policy and helps to maintain fiscal stability.

Examples of Domestic Financing:

1) Government Bonds:

Governments issue bonds as a means of domestic financing. These are debt securities that individuals, financial institutions, and other entities can purchase. In return, the government agrees to pay periodic interest and return the principal amount at the bond's maturity date. The sale of government bonds is a way for the government to raise capital from domestic investors.

2) Treasury Bills:

Treasury bills, commonly known as T-bills, are short-term debt instruments issued by the government. They have maturities ranging from a few days to one year. Investors buy T-bills at a discount, and upon maturity, the government pays the face value. This is another form of domestic financing that allows the government to meet short-term financial needs.

3) Domestic Loans:

Governments may secure loans from domestic financial institutions or the central bank as a form of domestic financing. These loans can be used to bridge budgetary gaps, fund infrastructure projects, or address immediate financial requirements. The terms and conditions of these loans vary, and they contribute to the overall domestic debt.

These examples demonstrate how domestic financing involves mechanisms such as issuing bonds, utilizing short-term debt instruments, and securing loans from domestic sources. This approach helps the government manage its fiscal responsibilities and maintain financial stability within the country.

(c) Differences Between Foreign Financing and Grants:

1) Nature of Repayment:

Foreign Financing: Foreign financing involves borrowing money from external sources, such as international financial institutions or foreign governments. The funds acquired through foreign financing typically come with an obligation to repay the borrowed amount along with interest over a specified period. This repayment structure can vary in terms of interest rates, grace periods, and overall terms of the loan.

Grants: Grants, on the other hand, are financial contributions provided by foreign governments, international organizations, or donor agencies without the expectation of repayment. Unlike foreign financing, grants are considered non-repayable and are often allocated for specific projects or initiatives. They are a form of financial assistance designed to support development goals, humanitarian efforts, or other strategic objectives without creating a debt burden for the recipient country.

2) Purpose and Flexibility:

Foreign Financing: Foreign financing is typically obtained for specific projects or budgetary support. Governments may secure foreign loans for infrastructure development, economic reforms, or other strategic initiatives. The use of funds obtained through foreign financing is often tied to the terms and conditions of the loan agreements, and the borrowing country must adhere to the agreed-upon purposes.

Grants: Grants, on the other hand, offer greater flexibility in terms of their use. While donors may specify the intended purpose of the grant, the recipient country generally has more discretion in allocating and managing the funds. Grants are often directed towards addressing pressing needs such as poverty alleviation, healthcare, education, or environmental conservation, providing governments with the latitude to determine how best to achieve the specified goals.

These differences highlight the contrasting nature of foreign financing and grants, particularly in terms of the repayment structure and the flexibility of fund utilization. Foreign financing involves

borrowing with an obligation to repay, while grants offer financial assistance without the expectation of repayment and greater freedom in fund allocation.

Functions of the national Budget

- (i) **Policy Statement**
The budget as a policy statement declares the goals and specific objectives a government wishes to achieve by means of expenditure.
- (ii) **Redistribution of wealth.**
The Zambian system of progressive taxation taxes higher income earners more than lower income earners.
- (iii) **Economic regulation.**
An increase in the rate of rate of taxes reduces disposable income of individuals and hence reduces spending. A reduction in spending tends to reduce inflation. A reduction in the rate of taxes in the budget tends to increase disposable income of individuals and companies. This will result in increased spending which is likely to increase demand for goods and services. An increase in demand for goods and services will increase inflation.
- (iv) **Regulation of trade.**
The government tends to increase import taxes on certain imported goods which are also manufactured locally to stimulate demand for the local goods.
- (v) **Control Instrument.**
It can be used to check whether the tasks in the budget were executed on schedule, and according to the standards prescribed in the budget. Also the variances in spending are analyzed so as to determine the causes.
- (vi) **As an operating program.**
The budget serves as a macro operating program on which the administrative authority may base operational plans for each function which has to be carried out to deliver certain services to the public in order to ensure that the broad goals and concrete objectives of the authorities may be realised efficiently and effectively.
- (vii) **The budget can also be used as a source of information.**

SOLUTION FIVE

S/N	Questions
a)	<p>Discuss Risk Assessment</p> <p>Risk assessment is a systematic process for identifying and evaluating events (i.e., possible risks and opportunities) that could affect the achievement of objectives, positively or negatively. Such events can be identified in the external environment (e.g., economic trends, regulatory landscape, and competition) and within an organization's internal environment (e.g., people, process, and infrastructure). When these events intersect with an organization's objectives—or can be predicted to do so—they become risks. Risk is therefore defined as "the possibility that an event will occur and adversely affect the achievement of objectives."</p> <p>While organizations have been conducting risk assessments for years, many still find it challenging to extract their real value. The linkage of risk assessment to drivers of shareholder value and key objectives has sometimes been lost. Risk assessments can be mandated by regulatory demands—for example, anti-money-laundering, Basel II, and Sarbanes-Oxley compliance all require formalized risk assessment, and focus on such processes as monitoring of client accounts, operational risk management, and internal control over financial reporting. Risk assessments can also be driven by an organization's own goals, such as business development, talent retention, and operational efficiency. Regardless of the scope or mandate, risk assessments must bring together the right parties to identify events that could affect the organization's ability to achieve its objectives, rate these risks, and determine adequate risk responses.</p> <p>A robust risk assessment process forms the foundation for an effective enterprise risk management program. It is important to recognize the interrelationships between risk assessment and the other components of enterprise risk management (such as control activities and monitoring) and understand the principles and steps that help ensure the relevance and effectiveness of a risk assessment.</p>

b)	<p>Explaining the three types of risk Assessment</p> <p>Strategic risk assessment.</p> <p>Evaluation of risks relating to the organization’s mission and strategic objectives, typically performed by senior management teams in strategic planning meetings, with varying degrees of formality.</p> <p>Operational risk assessment.</p> <p>Evaluation of the risk of loss (including risks to financial performance and condition) resulting from inadequate or failed internal processes, people, and systems, or from external events. In certain industries, regulators have imposed the requirement that companies regularly identify and quantify their exposure to such risks. While responsibility for managing the risk lies with the business, an independent function often acts in an advisory capacity to help assess these risks.</p> <p>Compliance risk assessment.</p> <p>Evaluation of risk factors relative to the organization’s compliance obligations, considering laws and regulations, policies and procedures, ethics and business conduct standards, and contracts, as well as strategic voluntary standards and best practices to which the organization has committed. This type of assessment is typically performed by the compliance function with input from business areas.</p>
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END OF SOLUTIONS



PUBLIC SECTOR FINANCIAL MANAGEMENT PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

PFM 5: PUBLIC SECTOR AUDITING

THURSDAY 12 DECEMBER 2024

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.

QUESTION ONE – (COMPULSORY)

You are working as Principal Auditor in the Office of the Auditor General (OAG). You have been assigned to lead a team of auditors to conduct a financial audit of Pavers Ltd, a company in which the government owns a stake of 80% while the remaining 20% is owned by the former owners of the company. You recently worked for Pavers Ltd before it was acquired by the government until six (6) months ago when you joined the Office of the Auditor General (OAG).

This is the first time that Pavers Ltd will be subjected to an audit by the Office of the Auditor General (OAG) and it has not been subject to external audits by private auditors since inception. In the current year, the company migrated from a manual accounting system to an integrated computerized system. The staff assigned to this audit, do not have an understanding of the new accounting system and will rely on in-house staff.

A whistle blower working for Pavers Ltd called the Auditor General (AG) and tipped him about a fraud involving senior members of staff of the company. The fraud involved the theft of pavers valued at over K1.2 million which were written off at the end of the previous year. The Auditor General (AG) informed you about the alleged fraud and requested you and the rest of the audit team to be skeptical during the audit because this could impact the current year financial statements and that a forensic investigation may be required.

You attended a pre-audit meeting with management of Pavers Ltd at which you were requested to consider seconding someone among the audit team members to Pavers Ltd to assist in the finalization of the financial statements. Management is concerned that the company will be audited by a private auditor as agreed with the minority shareholders and also be subject to an audit by the Office of the Auditor General (OAG). Management argued that this will be a duplication of effort and suggested that the Office of the Auditor General (OAG) undertakes a review of the financial statements rather than a full audit. You tipped the Finance Manager, your former school mate, about the alleged fraud and that this may result in a forensic investigation. He promised to carry out his own investigation and that he would get back to you.

During the planning stage of the audit, the Finance Manager informed you that the Pavers Ltd had received various gifts from its suppliers during the festive season. The gifts were shared amongst staff of Pavers Ltd and a decision had been made to extend this to the audit team and this included cash amounting to K1.2 million to be shared among the audit team members. Currently, the Office of the Auditor General (OAG) does not have an ethical code of conduct for staff to follow and you are of the view that audit team members will make their own decisions on the offer of gifts.

You called for a meeting with the rest of the audit team and emphasized the need to observe professional skepticism throughout the audit. Pavers Ltd provided you with the finance manual which contains procedures that should be followed. The Principal Auditor gave you a copy of the signed engagement letter for your records. The audit plan that has been drawn up states that the team will follow a combined approach, conduct risk assessments, evaluate the internal control systems of Pavers Ltd and perform tests of controls.

The results of the risk assessment and tests of controls suggest that audit risk in this audit is high. You are concerned that high audit risk will impact on the materiality level that will be used in the audit. This being the first audit there is no previous documentation and you are required to open both permanent and current audit files which will be used in filing the audit working papers.

Required:

- (a) Explain two (2) arguments for the independent audit by the Office of the Auditor General (OAG) of the financial statements of Pavers Ltd despite being subject to a private sector audit. (4 marks)
- (b)
 - (i) Explain five (5) fundamental ethical values and their applications that the Office of the Auditor General (OAG) should include in its own code of ethics according to ISSAI Code of Ethics. (10 marks)
 - (ii) Explain the ethical and professional matters that should be considered in the audit of Pavers Ltd and suggest suitable safeguards for each ethical matter. (8 marks)
- (c)
 - (i) Explain the importance of audit documentation in public sector audits. (2 marks)
 - (ii) State two (2) matters each that should be contained in the permanent and current audit files in the audit of the financial statements of Pavers Ltd. (4 marks)
- (d)
 - (i) Explain audit risk, using the audit risk model, in the audit of financial statements in public sector auditing and explain the element of risk that is within the control of the auditors. (4 marks)
 - (ii) Explain the impact of audit risk on materiality level at the planning and substantive stages of the audit of Pavers Ltd. (2 marks)
 - (iii) Explain the three (3) stages of public sector audits that should be followed in all public sector audits. (6 marks)

[Total: 40 Marks]

SECTION B

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

QUESTION TWO

- (a) The International Organization for Supreme Audit Institutions (INTOSAI) is a world body whose objective is to assist member countries come up with governance systems that enhance transparency and accountability in the use of public funds.

Independence of the Head of the Supreme Audit Institution (SAI) is paramount in terms of the objectivity in the performance of public sector audits. The way in which this is achieved, is by including the appointment of the Head of the Supreme Audit Institution in the country's constitution. Section 249 of the Zambian Constitution gives guidelines that assist in ensuring that the Head of the Supreme Audit Institution (SAI) is independent of the executive. Public funds are supposed to be used in the interest of the general citizenry and parliament has a role to play in ensuring transparency and accountability in the use of public funds.

The government of Zambia has put in place structures aimed at enhancing accountability in the public sector. At the Ministry of Finance, the Head of Internal Audit is responsible for all internal audit activities in ministries and public corporations. In addition, the Secretary to the Treasury who plays a pivotal role in enhancing transparency and accountability of those responsible for the management of public funds.

Required:

- (i) Explain the legal provisions contained in the constitution regarding independence of the Auditor General. (4 marks)
 - (ii) Explain the legal responsibilities of the Office of the Auditor General (OAG) with regards the use of public funds. (4 marks)
 - (iii) Explain four (4) responsibilities of the Secretary to the Treasury regarding the use and management of public funds. (4 marks)
- (b) You work for the Office of the Auditor General (OAG) in the Specialized Audits and Consultancy Directorate. You have been called to attend a high-level meeting at cabinet office regarding a fraud that has been reported in the public media.

The Secretary to Cabinet informed the attendees of a fraud that is alleged to have taken place in one (1) of the security wings of government. This involved the procurement of military hardware and it is alleged that a sum of \$1.5 million was misappropriated. Preliminary investigations revealed that high ranking officials within the security wing were involved and senior government officials implicated.

Because of the sensitivity of the matter, the Secretary to the Cabinet informed the meeting that ordinarily, matters bordering on state security, should not be investigated by OAG,

and any report should not be, made public. He suggested that a forensic investigation should be carried out by the Office of the Auditor General (OAG) and that the investigating team should include staff from the supervising ministry and a Principal Auditor at Cabinet Office. It was further alleged that more money meant for military hardware procurement could be missing necessitating the need for a forensic investigation and the determination of the extent of the fraud.

Required:

- (i) Explain the difference between forensic investigations and forensic accounting in public sector auditing using the information in the scenario. (4 marks)
- (ii) Respond to the assertion by the Secretary to Cabinet that matters of a security nature should not be subjected to investigations and findings should not be made public. (4 marks)

[Total: 20 Marks]

QUESTION THREE

- (a) The Ministry of Transport is concerned about the number of accidents in the country leading to increased numbers of fatalities over the last five (5) years. Cabinet is concerned about this and decided to take measures that will reverse this trend because a lot of money is being spent in terms meeting costs of medication for accident victims.

A project was initiated 2022 for road traffic patrols covering all the main roads across the country. This required the setting up of a separate unit under the Ministry of Transport. An amount of K50 million was injected into the procurement of new patrol vehicles and high speed cameras. The total annual budget of running the unit is K150 million.

The following statistics relate to the past three (3) years:

	2021	2022	2023
Number of recorded traffic accidents	98 124	102 077	112 300
Number of fatalities	7 121	9 671	10 213
Running costs of the patrol unit	-	K110 million	K162 million

You work for the Office of the Auditor General (OAG) and you have been assigned to conduct a performance audit of the road patrol unit under the Ministry of Transport.

Required:

- (i) Explain the objectives of the intended Value For Money audit of road patrol project. (4 marks)
- (ii) Describe the Value For Money principles in the performance audit of the road patrol project. (6 marks)

- (b) The Office of the Auditor General (OAG) is the Supreme Audit Institution (SAI) in Zambia. The mandate of the Auditor General (AG) is to conduct audits of the recipients of public funds and to report the findings to parliament and the public.

Parliament comprises the people's representatives who are voted for by the citizens during general elections. The Public Accounts Committee (PAC) is a committee of parliament and is accountable to parliament.

You work for the Office of the Auditor General (OAG) which recently recruited new staff currently undergoing induction. You are expected to give an insight of how the Office of the Auditor General (OAG) and the Public Accounts Committee (PAC) help in holding the recipients of public funds accountable.

Required:

- (i) Explain the way in which the Office of the Auditor General (OAG) and the Public Accounts Committee (PAC) fulfill their mandates regarding accountability and transparency in the public sector. (4 marks)
- (ii) Explain four (4) responsibilities of the Public Accounts Committee (PAC). (6 marks)

[Total: 20 Marks]

QUESTION FOUR

- (a) Each time there is a new government there are major changes that are made in the running of government and public institutions. A new government was voted into office and recommended changes in the way the Office of the Auditor General (OAG) should operate. The new government is of the view that the current status of the Office of the Auditor General (OAG) has not helped the government in fighting corruption and the management of public funds.

The following recommendations have been made:

1. The Office of the Auditor General (OAG) shall be directly under the Office of the President and the Auditor General (AG) shall report to the president.
2. The holder of the position of Auditor General (AG) shall be appointed by the president and tenure of office will be subject to satisfactory performance and a reduction in the misuse of public funds.

3. A committee comprising the President and three (3) Cabinet Ministers shall decide on the audits to be conducted based on their risk assessment and priority.
4. Publication of the Auditor General's reports shall be subject to the reports being cleared by the committee set by the president and reports on matters that border on the security of the country shall have restricted circulation and not be published.

You are a consultant in public sector auditing and you have been asked to attend a meeting with the Auditor General (AG) and representatives from Cabinet Office to explain the need for adhering to the legal provisions regarding the Office of the Auditor General (OAG) unless constitutional amendments are made.

Required:

- (i) Explain why constitutional amendments would be required to make changes to existing provisions regarding the Office of the Auditor General (OAG) and the Auditor General (AG). (2 marks)
 - (ii) Evaluate the new recommendations on the Office of the Auditor General (OAG) against the provisions of s249 of the constitution of Zambia. (6 marks)
- (b) A new Minister of Water was recently appointed by the president. The Minister proposed structural changes in the operations of the ministry among them, the dissolving of the current Audit Committee and appointing a new one.

The existing Audit Committee members comprise three (3) members representing professional bodies, the Permanent Secretary of the ministry, the Director of Finance and a Director within the ministry. The minister is concerned about the effectiveness of the Audit Committee which appeared to make recommendations not in line with the vision of the Ministry.

The Minister made the following proposals for the composition of an Audit Committee:

1. The Ministry's Permanent Secretary
2. The Ministry's Director of Finance
3. Three (3) Directors within the Ministry of Water.
4. One (1) representative of the Law Association of Zambia.

Required:

- (i) Explain four (4) roles of the proposed Audit Committee for the Ministry of Water. (4 marks)
- (ii) Comment on the composition of audit committee members and make necessary recommendations. (4 marks)
- (iii) Explain two (2) challenges that the proposed Audit Committee may face in the execution of its functions. (4 marks)

[Total: 20 marks]

QUESTION FIVE

- (a) In the last three (3) years there has been a noted increase in the number of Zambian citizens requiring social security support from government. Due to an increase in the cost of living, most pensions received by beneficiaries are not sufficient to support the beneficiaries.

Following a visit by the president to Nordic countries an agreement of three (3) Nordic countries, committed to support the social security scheme of Zambia. The amount is estimated to be \$2 million annually for the next five (5) years. Subject to proper management of the funds, the agreement will be extended for a further five (5) years.

The agreement with the consortium of Nordic countries includes a condition that the social security scheme should be subject to annual audits by the Office of the Auditor General (OAG) and that copies of the audit reports should be made available to the donors.

Required:

- (i) Explain the main objectives of the audits required on the social security funds. (4 marks)
- (ii) Describe three (3) stakeholders, explaining their interest and expectations, in the use of the funds meant for social security of the vulnerable. (6 marks)
- (b) You have been assigned to be part of a committee of three (3) to visit a country that does not have a Supreme Audit Institution (SAI). The country requested that the International Organization for Supreme Audit Institutions (INTOSAI) carries out an evaluation on the need for a Supreme Audit Institution (SAI).

The country has a population of five (5) million citizens with more than half of them living below the poverty datum line. This country is considered among the poorest countries in the world. The main source of funds for government is taxes levied on mining houses.

The country receives significant amounts of donor funds for specific projects carried out in conjunction with the government. Continued donor support is conditional on meeting the intended objectives and also strict financial management processes. The agreements with the donors contain the conditions that should be adhered to in managing the funds.

This includes a requirement of financial statements audited by a government agency responsible for audit, being submitted annually to the donors. This is what has prompted the decision to request the intervention of the International Organization for Supreme Audit Institutions (INTOSAI) to help set up a Supreme Audit Institution (SAI). The government of this country hopes to obtain absolute assurance regarding the use of public funds meant for the benefit of the country's citizens.

Required:

- (i) Discuss, using information in the scenario, the objectives for assurance in the three (3) main types of public sector audits in accordance with ISAI 100: Principles of public sector audits. (6 marks)
- (ii) Describe the two (2) main levels of assurance that can be given in public sector audits giving two (2) characteristics for each of them. (4 marks)

[Total:20 Marks]

END OF PAPER

PFM 5 PUBLIC SECTOR AUDITING AND PRACTICE SOLUTIONS

SOLUTION ONE

(a) Arguments for audits by the SAI in the public sector:

1. It is a constitutional requirement that all recipients of public funds should be audited by the Office of the Auditor General notwithstanding that they may be audited by private auditors.
2. The public sector auditors are the external auditors of public institutions because of their independence and objectivity. The SAI has skills to audit public sector which private auditors may not have and belong to an international body on public sector auditing the international organization for Supreme Audit institutions (INTOSAI).
3. The scope of the public sector auditors is much wider than that of private auditors whose main focus is to form an opinion on the financial statements. Public sector auditors perform other audits such as compliance and performance audits.
4. Audits ensure that public officials are accountable for their use of public resources. By scrutinizing expenditure and financial management, SAIs help ensure that funds are used for their intended purpose and in accordance with the Law.
5. SAIs can identify instances of fraud, corruption and mismanagement. By uncovering such activities, audits deter corrupt practices and promote ethical behaviors within public institutions.

(b) (i) Fundamental principles in public sector auditing:

	Ethical value	Explanation and Application
1	Integrity	<p>Integrity is the quality of being honest and having strong moral principles. It is to be honest and act in good faith and in the public interest. It is the cornerstone of trust in the auditing profession.</p> <p>Auditors should act with honesty, objectivity, and consistency in all professional and business relationship. They should avoid conflict of interest and ensure that their actions and decisions are guided by a commitment to truthfulness and transparency.</p>
2	Independence & objectivity	<p>Independence is the freedom from conditions that threaten the ability of the auditor to carry out their responsibilities in an unbiased manner. Objectivity is the impartiality and fairness in conducting audits.</p> <p>Auditors should maintain both organisational and personal independence to ensure that their judgements are not influenced by external pressures or personal interests. They</p>

		should make decisions based on objective evidence without bias or favoritism.
3	Professional Competence and Due Care	<p>Professional competence means having the necessary skills, knowledge, and experience to perform audit tasks effectively. Due care refers to the diligence and thoroughness in performing duties.</p> <p>Auditors should continuously develop and maintain their professional knowledge and skills. They should apply the appropriate level of professional judgement and diligence in their work, ensuring high quality audit outcomes.</p>
4	Professional behavior	<p>Professional behavior entails adhering to laws and regulations and avoiding any conduct that could discredit the auditor or the auditing profession and/ or the SAI.</p> <p>Auditors should act in a manner that upholds the reputation of the auditing profession. This includes complying with relevant laws and standards, avoiding actions that could bring disrepute to the SAI and conducting themselves in a way that promotes public confidence in their work.</p>
5	Confidentiality & transparency	<p>To protect information obtained in the cause of duty and disclose only under exceptions allowed and considering the need for transparency and accountability in the public sector.</p> <p>Auditors should protect sensitive information acquired during audits. They must not use such information for personal gain or disclose it to unauthorized parties, thereby safeguarding the interests of stakeholders and maintain trust in the auditing profession.</p>

(ii) Ethical matters to consider in the audit of Pavers Ltd:

No	Ethical matter	Safeguard
1	New IT system – the fact that most of the staff assigned to the audit of Pavers Ltd do not possess knowledge of the accounting system is an ethical matter in that they may not have the competence to undertake the audit.	Staff with the necessary IT knowledge should be assigned to this audit or the staff should be trained before being assigned to the audit.
2	Disclosure of pending investigation to Finance Manager – It is unethical to tip off management of the fraud. The fact that the Finance Manager is a friend the AG suggests that this was meant to warn him about what is pending.	A code of ethics should be put in place in the Office of the Auditor General. Punitive measures should be put in place to for violation of the code.

3	Secondment of staff to assist finalization of the preparation of the financial statements creates a self-review threat on the staff affected. They are likely to lose objectivity when reviewing their own work.	The request should be declined unless someone not involved in the audit is assigned to do this.
4	Offer of gifts will create a self-interest threat. It does not matter that the gifts were given to Pavers Ltd by its suppliers. The self-interest will impact on the objectivity of the auditors.	Unless such gifts are clearly insignificant they should be declined. Gifts including cash amounting to K1.2 million is clearly not insignificant and should be declined.

- (c) (i) Importance of documentation in public sector auditing:
Documentation of work done is one of the general principles of public sector auditing.

It is important that audit work is documented because:

- Audit documentation forms the basis for the audit opinion or conclusion.
- It helps in managing the audit through enabling reviews of work done.
- Documentation is evidence of work that has been performed and whether the audit has been conducted in accordance with relevant auditing standards.

- (ii) Matters that should be contained in the permanent audit file:

1. A copy of the engagement letter for the audit of Pavers Ltd.
2. The internal control systems of Pavers Ltd
3. The finance manual will remain relevant over more than one year.

Matters that should be contained in the current audit file:

1. The current year financial statements
2. Working paper for the work carried out during the year.
3. Any review points made at the various stages of the audit.

- (d) (i) Audit risk in the audit of pavers Ltd:

	Element of audit risk	Explanation
1	Inherent risk	This is a risk that arises because of the nature of the client company or an assertion. For example accounting estimates are inherently risk because there is no precise method of determining them and their determination involves judgment.
2	Control risk	This is the risk that the internal controls put in place by Pavers Ltd may fail to prevent or help detect misstatements. Such misstatements could cause the financial statements to be misstated and the public sector giving an inappropriate opinion/conclusion.
3	Detection risk	This is the risk that the public sector auditors may not detect misstatements that may cause the

		financial statements to be misstated despite conducting the audit in accordance with relevant auditing standards.
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Element of audit risk within control of public sector auditor:

The only element of audit risk that is under the control of the public sector auditors is detection risk. This can be reduced by the public sector auditors addressing the matter causing it. For example if the audit team lacks competence to perform the audit it could result in a misstatement of the financial statements. This can be avoided by assigning staff with the necessary skills and competences or training the staff.

(d)(ii) Impact of audit risk on materiality level at planning & substantive audit stages:

At the planning stage of the audit if risk for the financial statements as a whole is assessed as high, the materiality level will be set at a lower figure. This is the same with any assertions that may have different risk characteristics from those of the financial statements as a whole. On the other hand if risk is assessed as low, the materiality level will be set at a higher level.

In the case of Pavers Ltd, since the audit risk for the financial statements as a whole has been assessed as low the materiality figure will be set at a higher level.

If during the substantive audit stage the risk is assessed at different levels from that at the planning stage this will necessitate a revision of the materiality level. In this case, the risk during the substantive stage is assessed higher than originally assessed at the planning stage. The materiality level will be revised to a lower level which will be used in the conduct of the audit.

(iii) Three stages of public sector audits:

Planning stage:

This is the stage of the audit when risk assessment is performed .It helps auditors to decide on the nature and extent of further audit procedures to be conducted. The public sector auditors will wish to gain an understanding of the audited entity and determine the scope of the audit.

Substantive audit stage:

This is the stage of the audit when audit procedures are performed to obtain evidence about the subject matter. The evidence obtained forms the basis for the audit conclusion.

Reporting & follow up stage:

This is the stage of reviewing the audit evidence obtained and reaching conclusions. The conclusion reached is communicated to the users in audit reports issued. Follow up is done to confirm implementation of any recommendations that will have been made in the previous audit.

SOLUTION TWO

- (a) (i) Constitutional provisions on AG independence:
 - (a) The Auditor General (AG) shall not be subject to the direction or a person or authority in the performance of the functions of his/her office.
 - (b) The Auditor General may only be removed from office on grounds of mental or physical disability, incompetence, gross misconduct or bankruptcy.
 - (c) The Auditor General & his staff should have immunity from legal proceedings in the exercise of their functions.
 - (d) The Auditor General (AG) shall determine the scope and extent of audit of the accounts of each entity.
 - (e) The Auditor General should have access to all documents & records that are considered necessary for the purposes of carrying out an audit.

- (ii) Legal provisions of the OAG with regards use of public funds:

The scope of the work of the Auditor General with regards public funds is wide and the following is provided under the constitution of Zambia:

 - 1. The Auditor General shall conduct audits of state organs, state institutions, provincial administration and any other institutions financed from public funds.
 - 2. The nature of audits that will be conducted include financial audits, value for money audits and investigations.
 - 3. Regarding projects/activities involving the use of public funds, to ascertain that the public funds have been applied for the purpose for which it was given and spent in conformity with the authority that governs it taking into account the principles of value for money.

- (iii) Responsibilities of the Secretary to the Treasury:

The responsibilities of the Secretary to the Treasury with regards to the use of public funds includes the following:

 - 1. The preparation of annual estimates of revenue and expenditure for submission as budget inputs.
 - 2. Quarterly review of performance of the budget & submitting a report thereof to the Minister.
 - 3. Releasing of funds from the consolidated fund for appropriation by controlling officers.
 - 4. Ensuring the implementation of the recommendations of the Public Accounts Committee.
 - 5. Maintaining compatible, effective, efficient and transparent financial management information system.
 - 6. Monitoring & inspecting the operations of the de-centralized accounting units in ministries and departments to ensure value for money.
 - 7. Providing a regulatory framework for sound financial management to accounting units.

- (b) (i) Differences between forensic investigations and forensic accounting:
Forensic investigation is the use of investigative skills with a view to establishing facts usually related to illegal activities the results of which many lead to legal action against the people involved.

In the case at hand, this involves interviewing staff and examination of documents to confirm whether indeed a fraud took place and the identification of the people involved.

Forensic accounting on the other hand is the use of accounting skills to determine for example the extent of an alleged loss to determine how much money is involved.

In this case it will involve the public sector auditors to follow through the funding for hardware procurement and establish the extent of the amount of money misappropriated, if any.

- (ii) Response to the assertion that security matters not subject to audits:
The constitution of Zambia provides that the Auditor General shall conduct audits and investigations of recipients of public funds. There are no exceptions regarding institutions that shall be not audited by the public sector auditors.

The assertion by the Secretary to Cabinet is not correct and is not valid. The said security wing is subject to investigations by the Office of the Auditor General. Further, the suggestion that the investigation should include staff from the supervising ministry is not correct. The Auditor General shall perform his/her functions without any interference and shall obtain evidence from whomsoever they deem necessary.

SOLUTION THREE

- (a) (i) Objectives of value for Money Audit on road patrol project:
The objective of the value for money audit on the road patrol unit is for the public sector auditors to obtain evidence on whether the initial public funds and the annual running costs of the unit have been spent in line with the principles of economy, efficiency and effectiveness.

Economy – whether the amounts spent were appropriate and the best prices.

Efficiency – to determine whether the objective could have been achieved using lesser resources i.e. a comparison of the output with the input.

Effectiveness – to determine whether the objective of the project have been achieved which in this case is a reduction in road traffic accidents.

- (ii) Value for money principles in the audit of road patrol project:

Economy:

This will involve the determination of the amounts paid for the procurement of the patrol vehicles. Could the vehicles been acquired using lesser resources but without compromising on the quality. In other words, was the best price paid?

The use of the operational costs will also be subjected to the element of economy to confirm that funds were put to best use and not wasted.

Efficiency:

This will involve comparing the outputs of the project against the inputs. It measures the efficiency of the use of financial and human resources. Could the same result have been achieved using lower resources for example using fewer patrol vehicles than the ones procured? Could fewer human resources have been used to achieve the same output?

Effectiveness:

This element aims at measuring whether the objective has been achieved. In this case it will be to establish whether there has been a reduction in the number of road traffic accidents after the intervention. Considering the statistics, it would appear that in this case the objective has not been achieved considering the increase in the number of accidents despite the intervention.

- (b) (i) Role of OAG & PAC in fulfilling mandates:

The Office of the Auditor General (OAG) helps enhance accountability and transparency in the public sector by conducting audits of recipients of public funds and issue reports to parliament and the president.

By issuing audit reports, the Office of the Auditor General (OAG) enables the Public Accounts Committee (PAC) fulfill its mandate which places reliance on the audit reports.

The public Accounts Committee helps enhance accountability and transparency by calling the controlling officers with audit queries to appear before it and explain the findings. The committee writes a report to parliament which is considered by parliament.

The Public Accounts Committee also makes recommendations on what action should be taken on audit funds including referring matters to investigative wings.

- (ii) Responsibilities of the Public Accounts Committee:
1. To monitor the implementation of the budget approved by parliament.
 2. Ensure that the recommendations of the Office of the Auditor General are followed up by the executive to ensure implementation.
 3. Holding sittings with controlling officers and other stakeholders where they are requested to make submissions on issues raised by the Auditor General.
 4. Make recommendations to address issues raised in the Audit Reports and where appropriate refer matters to investigative wings.

SOLUTION FOUR

(a) (i) Need for constitutional amendments on articles on the OAG:

The constitution of the country is the supreme law which should be followed. With regards the Office of the Auditor General, the existing articles should be complied with in the running of the Office of the Auditor General.

The recommendations of the new government should be measured against the current constitution. If the new recommendations are not in line with the constitution, they cannot be implemented. There would be need to make constitutional changes to include the proposals being made. Any changes without constitutional changes will be a breach of the constitution.

The reason for inclusion of the clauses on the Office of the Auditor General (OAG), is to prevent unconstitutional changes in the way the office operates.

(ii) Evaluation of new recommendations on OAG:

1. The recommendation to have the Office of the Auditor General (OAG) to fall under the Office of the President is contrary to the current provisions of the constitution which requires that the office shall be independent and shall operate autonomously.
2. This provision is not in line with the constitutional provisions which state that the Auditor General shall be appointed by the President on recommendation of the State Audit Commission and shall be ratified by parliament. This is done in order to maintain the independence of the office.
Further, the constitution clearly spells out when the Auditor General can be removed from office which does not include the appraisal and reduction in misuse of public funds.
3. The constitution provides that the Office of the Auditor General (OAG) shall decide on the topics to be audited and shall not be directed as is the recommendation here. The President may however request the Office of the Auditor General (OAG) to conduct audits or investigations and this is not taken as interference or direction.
4. The constitution provides that the Auditor General (AG) shall report on his/her findings and will determine the content of the report. Clearance of reports by a committee of parliament will be contrary to constitutional requirements and the constitution does not provide for exemptions from audit on account of matters bordering on state security.

(b) (i) Roles of proposed Audit Committee:

- To apprise the rest of the board on how it has fulfilled its responsibilities.
- To monitor and ensure continued independence of the auditors.
- To monitor and evaluate management systems regarding risk and internal controls.
- Review financial reports and other board reports before they are referred to the board.
- To monitor the working of the internal auditors and ensure they are independent of management.
- Provide a link for the public sector auditors when they have matters of concern regarding management performing its duties.

- Help resolve disputes within management and provide an independent view over such disputes.

(ii) Composition of audit committee with justification:

The proposed audit committee comprises largely of people who work for the ministry. Of the six committee members five are employees within the ministry. One of the roles of the committee is to oversee the operations of the ministry and when it comprises people who work within the ministry they will lack the objectivity to oversee their own operations.

The previously disbanded committee had half of the committee comprising independent people.

Best practice requires that the committee should comprise largely independent members with one who has knowledge of finance and accounting. The proposed audit committee does not appear to have someone with accounting knowledge.

The proposed committee should be changed to comprise more of the independent members and also to include a member with accounting knowledge.

(iii) Challenges that may be faced by audit committee:

1. Committee members will not be objective and there will exist self interest in making decisions.
2. Being members of staff they may be subject to political pressure in making certain decisions.
3. There being no member who has finance knowledge they will not be able to constructively review internal controls and financial statements prepared by management.

SOLUTION FIVE

(a) (i) Objective of audit of social security funds:

The main objective of requiring the audit of social security funds by the Supreme Audit Institution (SAI) will as highlighted below:

- To verify compliance with the relevant legal and regulatory framework governing social funds.
- Confirm that there is no misapplication or misappropriation of the social security funds and that money is used for the intended purpose.
- Confirm that the money reaches the intended beneficiaries.
- To verify compliance with the relevant legal and regulatory framework governing social funds.
- To assess the effectiveness of social programs and projects funded by social funds in achieving their intended outcomes.
- To examine whether social funds are managed efficiently and economically.
- To enhance transparency and accountability in the management and utilization of social funds.
- To detect and prevent, corruption and mismanagement of social funds.
- To strengthen the governance and internal control systems related to the administration of social funds.

(ii) Stakeholders in the use of social security funds:

- **Beneficiaries (Vulnerable Population).** The primary interest of beneficiaries is to receive timely, adequate and reliable financial and social support to improve their quality of life. This includes access to basic needs such as food, shelter, healthcare and education.

Beneficiaries expect that the funds will be used effectively to provide the services and support they need without bureaucratic delays or corruption. They seek transparency and accountability to ensure that they are rightfully receiving the benefits intended for them.

- **Government and Public Authorities.** Government bodies, including Ministries of Finance and social welfare, are interested in ensuring that social security funds are used efficiently and effectively to meet goals and improve social outcomes. Their interest lies in achieving maximum impact with the available resources, reducing poverty and promoting social inclusion.

The government expects proper administration, monitoring and evaluation of social security programs to ensure compliance with laws and regulations. They also seek to maintain public trust and demonstrate to taxpayers or donors that funds are managed responsibly.

- **Taxpayers and donors.** The donors who donate the funds or taxpayers who fund social security program through their contributions and have a vested interest in seeing these funds used wisely and for the intended purpose. They

are interested in the effectiveness of social welfare programs in reducing societal inequalities and supporting vulnerable populations.

Taxpayers and donors expect transparency, accountability and efficiency in the use of public funds. They want assurance that their contributions are making a real difference and are not being lost to inefficiencies or corruption. Additionally, they seek regular reporting and audits to ensure that funds are managed with integrity.

(b) (i) Need for assurance in the three main types of public sector audits:

Financial audits:

The need for an assurance in the financial public sector audit is for the auditor to obtain evidence that the financial statements have been prepared in accordance with the applicable financial reporting framework.

Compliance audits:

The need for assurance in compliance audits is for the public sector auditor to obtain evidence that there has been compliance with the applicable authority for subject matter information.

Performance audits:

The objective of performance audits is for the public sector auditors to obtain evidence that public funds have been spent in accordance with the Value For Money principles of economy, efficiency and effectiveness.

(ii) Levels of assurance in the public sector audits:

Reasonable assurance – this is a high but not absolute level of assurance where the public sector auditor concludes in a positive manner after performing substantive audit procedures.

The main characteristics:

- High level of assurance
- Positive form stating that based on evidence obtain a true and fair view is or is not given.
- Substantial amount of work performed in accordance with auditing standards.

Limited assurance – Is a lower level of assurance given by the auditors based largely on inquiry and analytical procedures as methods of obtaining evidence. The main characteristics:

- Lower level of assurance
- Main methods of obtaining evidence are inquiry and analytical procedures
- Conclusion in a negative way stating that nothing has come to the attention of the auditors that suggests that accounts do not show a true and fair view for example.

END OF SOLUTIONS



PUBLIC SECTOR FINANCIAL MANAGEMENT PROGRAMME EXAMINATIONS

DIPLOMA LEVEL

PFM 6: FINANCIAL REPORTING FRAMEWORK FOR PUBLIC SECTOR ENTITIES

MONDAY 9 DECEMBER 2024

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

INSTRUCTIONS TO CANDIDATES

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

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

SECTION A

This question is compulsory, and MUST be attempted.

QUESTION ONE

You have just been recently posted to Vubwi Town Council in the Finance Department. You have been presented with the following information for the year ended 31 December 2023.

	K
Cash and cash equivalents	8,900,000
Trade and other receivables (less than one year)	54,678,690
Other financial assets (less than a year)	345,000
Revaluation reserve	7,800,000
Accumulated surpluses	47,173,090
Trade and other receivables (more than one year)	45,300,000
Other financial assets (more than one year)	50,000
Inventory as at 1 January 2022	600,000
Investment property	1,800,000
Provision for depreciation Investment property	900,000
Property, plant and equipment	9 0,000,000
Provision for depreciation property, plant and equipment	9,000,000
Intangible assets	3,695,000
Short term trade and other payables	16,045,600
Short term borrowings	5,000,000
Long term trade and other payables	15,000,000
Long term borrowings	64,500,000
Levies and charges	15,000,000
Fees and charges	4,300,000
Rental income	2,140,000
Interest received	500,000
Tax revenue	900,000
Other income	670,000
Revenue grants	21,000,000
Capital Grants as at 1 January 2023	13,240,000
Salaries and wages	10,500,000

Materials and services	6,540,000
Finance costs	760,000

Additional information:

1. Revenue grant is to be treated as a credit in the statement of financial performance.
2. Capital grants are treated as deferred income and 10% is transferred to statement of financial performance annually.
3. Depreciation policy: investment property 20% on cost; property plant and equipment 10% on cost.
4. Closing inventory as at 31 December 2023 was K200,000.00.
5. Tax revenue of K100,000.00 was posted to rental income in error.
6. A transfer from revaluation reserve of K800,000.00 should be made to accumulated surplus.

Required:

- (a) Prepare the trial balance as at 31 December 2023. (14 marks)
- (b) Prepare the Statement of Financial Performance for the year ended 31 December 2023 in accordance with IPSAS 1. (12 marks)
- (c) Prepare the Statement of Financial Position as at 31 December 2023 in accordance with IPSAS 1. (14 marks)

[Total: 40 Marks]

SECTION B

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

QUESTION TWO

The Ministry of Finance and National Planning (MoFNP) is preparing its financial statements for the year ended 31 March 2023 using the accruals basis of accounting as required by International Public Sector Accounting Standards (IPSASs). You are the Director in the department of Financial Reporting and Information Systems at the Ministry of Finance and National Planning and have been asked to review the accounting treatment of some transactions.

Transaction One

The Ministry of Finance and National Planning entered into a lease contract for land cruiser motor vehicles with a local bank on 1 April 2022. The lease term is 4 years and represents the majority of the motor vehicles' life. The present value of the lease payment is K180 million and the ministry is to pay lease rentals of K47 million per annum at interest rate of 12%. The Ministry of Finance and National Planning is responsible for maintenance and insurance of the motor vehicles throughout the lease term.

The preparer of the financial statements has accounted for the lease as an operating lease.

Transaction Two

A former Director has sued the Ministry of Finance and National Planning for wrongful dismissal. On 31 January 2023, the industrial claims court awarded the former director damages to the value of K7 million.

The preparer of financial statements at the Ministry of Finance and National Planning has not included any amount in relation to these damages on grounds that they were not budgeted for.

Transaction Three

The Ministry of Finance and National Planning received notification on 20 April 2023 that one of the youth groups that were loaned empowerment funds for purchase of Marcopolo buses had been disbanded and non-operational with the buses parked at one member's house as non-runner with multiple mechanical problems. Preliminary investigations revealed that the group is unlikely to continue in operation and they owe loan money to the ministry of finance of K190 million.

The preparer of financial statements at the Ministry of Finance and National Planning has not made any adjustment for this transaction before finalizing the year end accounts for submission to the users of financial statements.

Required:

Assess the appropriateness of the treatment of the items above by MoFNP officer, assuming first a cash basis, and then an accruals basis of accounting.

[Total: 20 Marks]

QUESTION THREE

The International Public Sector Accounting Standards Board (IPSASB) has developed the Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities. The framework provides guidance on the elements to be included in General Purpose Financial Reports (GPFRs). One element among others is 'liabilities'. The framework further states that, 'for an element to be recognized in general purpose financial reports, it must meet the definition of such an element in accordance with the framework; and the element can be measured reliably, that is, in a way that achieves the qualitative characteristics of financial information.

Required:

- (a) Briefly explain 'liability' according to conceptual framework for general purpose financial reporting by public sector entities. (7 marks)

Distinguish between legally binding and non-legally binding obligation, giving two (2) examples of each. (5 marks)

- (b) Briefly describe each of the following methods of measuring liabilities:

- (i) Cost of release
- (ii) Historical cost
- (iii) Assumption price
- (iv) Cost of fulfilment.

(8 marks)

[Total: 20 Marks]

QUESTION FOUR

The secretary to the treasury of country P attended a workshop on public sector accounting at which the facilitator indicated that IPSAS 23 revenue from non-exchange transactions (taxes and transfers) was extremely important for public sector.

Required:

- (a) Explain non-exchange transactions and revenue according to IPSAS 23. (4 marks)
- (b) Explain the recognition criteria for revenue arising from non-exchange sources according to IPSAS 23. (6 marks)
- (c) Describe assets that are received but not reported as non-exchange revenue. (4 marks)
- (d) What are the main differences between IFRSs and IPSASs? (6 marks)

[Total: 20 Marks]

QUESTION FIVE

You have been requested to assess the financial performance of the Government of the Republic of Zambia (GRZ) for the year ended 31 December 2022 based on the published Financial Report for the year 2022. Below is an extract from the GRZ Financial Report for the year ended 31 December 2022:

Government of the Republic of Zambia

Extract of Statement D – Comparison of budget and actual (functional classification) for the year ended 31 December 2022

	Approved K'million	Actual K'million
Receipts		
Income tax	14,514	12,752
Customs and excise	3,946	3,958
Fuel levy	759	795
Value Added Tax	6,445	10,126
Fines	35	53
Licenses	631	622
Commissions	25	21
Fees of court and office	371	327
Other revenue	684	996
Bilateral grants	289	-
Multilateral grants	1,253	-
Program grants - general budget support	-	145
Program grants - sector budget support	-	146
Bilateral external Borrowing	312	1,710
Multilateral external Borrowing	7,802	7,349
Domestic borrowing	2,199	2,543
Total Receipt	<u>39,265</u>	<u>41,543</u>
Payments		
Personal emoluments	16,204	15,404
Use of goods and services	19,758	12,583
Financial charges	5,300	4,435
Social benefits	259	172
Grants and other payments	7,237	6,048
Constitutional & statutory Expenditure	-	17
Non-financial assets	1,369	471
Payment of arrears and debt service	391	400
Total Expenditure	<u>50,518</u>	<u>39,530</u>
Net Surplus/(Deficit)	<u>(11,253)</u>	<u>2,013</u>

Required:

- (a) Explain the purpose of Statement D. (2 marks)
- (b) Calculate variances and variance percentages (12 marks)
- (c) Comment on the financial performance of the Government of the Republic of Zambia for the year ended 31 December 2022, utilising the variances you calculated in part (b). (6 marks)

[Total:20 Marks]

END OF PAPER

PFM 6: FINANCIAL REPORTING FRAMEWORK FOR PUBLIC SECTOR ENTITIES SOLUTION

SOLUTION ONE

Vubwi Town Council

(a) Trial balance for the year ended 31 December 2022

	DR	CR
	K	K
Cash and cash equivalents	8,900,000	
Trade and other receivables (less than one year)	54,678,690	
Other financial assets (less than a year)	345 000	
Revaluation reserve		7,800,000
Accumulated surpluses		47,173,090
Trade and other receivables (more than one year)	45,300,000	
Other financial assets (more than one year)	50,000	
Inventory as at 1 January 2022	600,000	
Investment property	1,800,000	
Provision for depreciation Investment property		900,000
Property, plant and equipment	90,000,000	
Provision for depreciation property, plant and equipment		9,000,000
Intangible assets	3,695,000	
Short term trade and other payables		16,045,600
Short term borrowings		5,000,000
Long term trade and other payables		15,000,000
Long term borrowings		64,500,000
Levies and charges		15,000,000
Fees and charges		4,300,000
Rental income		2,140,000
Interest received		500,000
Property tax revenue		900,000
Other income		670,000

Revenue grants		21,000,000
Capital Grants as at 1 January 2022		13,240,000
Salaries and wages	10,500,000	
Materials and services	6,540,000	
Finance costs	760,000	
	223,168,690	223,168,690

(b) **Statement of financial performance for Vubwi Town Council for the year ended 31 December 2022.**

Receipts	K'
Levies and charges	15,000,000.00
Fees and charges	4,300,000.00
Rental income (W5)	2,040,000.00
Interest received	500,000.00
Tax revenue (W4)	1,000,000.00
Other income	670,000.00
Amortization of capital grant (W1)	1,324,000.00
Revenue Grants	21,000,000.00
Total Receipts	45,834,000.00
Payments	
Salaries and wages	10,500,000.00
Materials and services (W3)	6,940,000.00
Depreciation (W2)	9,360,000.00
Finance costs	760,000.00
Total Payments	27,560,000.00
Surplus for the year	18,274,000.00

Vubwi Town Council Statement of Financial Position as at 31st December 2022

ASSETS

Current assets

Cash and cash equivalents	8,900,000.00
Trade and other receivables (less than one year)	54,678,690.00
Other financial assets (less than a year)	345,000.00
Inventory at 31st December 2022	200,000.00
Total current assets	64,123,690.00

Non-current assets

Trade and other receivables (more than one year)	45,300,000.00
Other financial assets (more than one year)	50,000.00
Investment property (W9)	540,000.00
Property, plant and equipment (W10)	72,000,000.00
Intangible assets	3,695,000.00

Total non-current assets **121,585,000.00**

Total assets **185,708,690.00**

Liabilities**Current liabilities**

Short term trade and other payables	16,045,600.00
Short term borrowings	5,000,000.00

Total current liabilities **21,045,600.00**

Non-current liabilities

Capital grants	11,916,000.00
Long term trade and other payables	15,000,000.00
Long term borrowings	64,500,000.00

Total non-current liabilities **91,416,000.00**

Total liabilities **112,461,600.00**

Net assets **73,247,090.00**

Net assets/equity

Revaluation reserve (W6)	7,000,000.00
Accumulated surpluses (W7,W8)	<u>66,247,090.00</u>

Total net assets/equity **73,247,090.00**

Workings**W1: Amortization of capital grant**

Grant amount	13,240,000.00
10% thereof	<u>(1,324,000.00)</u>
	<u>11,916,000.00</u>

W2: Depreciation

Investment property at cost	1,800,000.00
20% thereof	(360,000.00)
Property, plant and equipment at cost	90,000,000.00
10% thereof	<u>(9,000,000.00)</u>
	<u>9,360,000.00</u>

W3: Materials and services

Opening inventory	600,000.00
Purchases	6,540,000.00
Closing inventory	<u>(200,000.00)</u>
	<u>6,940,000.00</u>

W4: Tax revenues

Revenues	900,000.00
Misposting to rental income	<u>100,000.00</u>
	<u>1,000,000.00</u>

W5: Rental income

Rental income	2,140,000.00
Misposting of tax revenues	<u>(100,000.00)</u>
Total tax revenues	<u>2,040,000.00</u>

W6: Transfer to accumulated surpluses

Revaluation reserve	7,800,000.00
Transfer to accumulated surpluses	<u>(800,000.00)</u>
	<u>7,000,000.00</u>

W7: Transfer from Revaluation reserves

Accumulated surpluses	47,173,090.00
Transfer from revaluation reserves	<u>800,000.00</u>
	<u>47,973,090.00</u>

W8: Accumulated surplus

As per w7	47,973,090.00
Surplus for year	<u>18,274,000.00</u>
	<u>66,247,090.00</u>

W9: Investment property

Investment property at cost	1,800,000.00
Less accumulated depreciation b/f	(900,000.00)
Less depreciation charge for year	<u>(360,000.00)</u>
NBV	<u>540,000.00</u>

W10: Property, plant and equipment

Property plant and equipment at cost	90,000,000.00
Less accumulated depreciation b/f	(9,000,000.00)
Less depreciation charge for year	<u>(9,000,000.00)</u>
NBV	<u>72,000,000.00</u>

SOLUTION TWO

TRANSACTION ONE

The accounting treatment applied by the preparer of financial statements on the lease contract is incorrect

The lease contract states that lease term is the majority of the assets useful life.

It also states that the lessor is responsible for the maintenance and insurance of the motor vehicles. This means therefore that risks and rewards associated with the asset are with the lessee hence the lease to be accounted for as a finance lease.

This means the lessee should recognize assets acquired under finance lease and obligations as liabilities in their statement of financial position based on the fair value of leased motor vehicles or if lower, present value of minimum lease payments, in this case K180 million. Finance cost will be K21.6 million with non-current lease obligation of K 126.2 [K154.6M + 18.6M (12% x K154.6M) - K 47M]. The current portion of lease obligation to be K28.4M (K154.6M – K126.2M).

TRANSACTION TWO

The accounting treatment applied by the preparer of financial statements at the ministry of finance is incorrect.

As the former director has been awarded damages before the end of an accounting period, a provision should be recognized in connection with the damages and a reliable measure of the amount granted by the court of K7 million to appear as liability for the year ending 31 March 2023 and expense in the statement of financial performance.

TRANSACTION THREE

Not accounting for this transaction before submitting results for approval is incorrect and would be misleading.

This situation is an adjusting event to be accounted for as per the provisions of IPSAS 14 events after the reporting date.

The youth group is a receivable to the ministry of finance that are unlikely to meet their obligation. IPSAS 14 requires that such occurrence should be adjusted for from the financial statements despite having been confirmed after the reporting period.

This means the preparer of financial statements to have written off the amount owed by the youth group of K190m, from statement of financial position and the calculation of the surplus for the year should be reduced by the same amount. This will mean financial statements will be a faithful representation as they would have captured all events transpiring before submission of year end results to the minister.

SOLUTION THREE

- (a) **Liability:** A present obligation of the entity for an outflow of resources that results from the past event.

Present obligation: A present obligation is a legally binding obligation (legal obligation) or non-legally binding obligation, which an entity has little or no realistic alternative to avoid. Obligations are not present obligations unless they are binding and there is little or no realistic alternative to avoid an outflow of resources.

Past event: The past transactions or other events that result in an entity gaining control of a resource and therefore an asset may differ.

Outflow of resources: A liability must involve an outflow of resources from the entity for it to be settled. An obligation that can be settled without an outflow of resources from the entity is not a liability.

- (b) **Binding obligations:** Binding obligation can arise from both exchange and non-exchange transactions. An obligation must be to an external party to give rise to a liability. An entity cannot be obligated to itself, even where it has publicly communicated an intention to behave in a particular way.

Legal obligation is enforceable in law; such enforceable obligation may arise from a variety of legal contracts. Exchange transactions are usually contractual in nature and therefore enforceable through the laws of contract or equivalent authority or arrangements.

Obligations that are binding through such processes are considered legal obligations in the conceptual framework.

Examples:

- Taxes payable
- cost of decommissioning an asset (via legal obligation)
- legal obligation
- loans payable
- payables for supply of goods and services

Non-legally binding obligations: Liabilities can arise from non-legally binding obligations; non-legally binding obligations differ from legal obligations in that the party to whom the obligation exists cannot take legal (or equivalent) action to enforce settlement.

Examples:

- cost of decommissioning an asset (via constructive obligation)
- Dividends payable
- Political promises
- effecting a budget
- announcement of policy

- (c) **Cost of release:** it is the term used in the context of liabilities to refer to the same concept as net selling price in the context of assets. Cost release is the amount that either the creditor will accept in settlement of its claim, or a third party would charge to accept the transfer of the liability from the obligor.

Historical cost: The historical cost for a liability is the consideration received to assume an obligation, which is the cash or cash equivalent, or the value of the other consideration received at the time the liability is incurred.

Under the historic cost model initial values may be adjusted to reflect factors such as the accrual of interest, the accretion of discount or amortization of a premium

Assumption price: in the context of liabilities, assumption price is the same concept as replacement cost for assets. Just a replacement cost represents the amount that an entity would rationally pay to acquire an asset, so assumption price is the amount which the entity would rationally be willing to accept in exchange for assuming an existing liability.

Cost of fulfilment: Cost of fulfilment is the cost that the entity will incur in fulfilling the obligations represented by the liability, assuming that it does so in the least costly manner.

Where the cost of fulfilment depends on uncertain future events, all possible outcomes are considered in the estimated cost of fulfilment, which aims to reflect all those possible outcomes in an unbiased manner.

SOLUTION FOUR

- (a) **Non-exchange transactions:** Are transactions where an entity receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange.

Non-exchange transactions are a characteristic feature of public sector financial reporting. Non-exchange transactions arise rarely, if at all, in the private sector and consequently there is no International Financial Reporting Standard (IFRS) covering non-exchange transactions, *(To merit the marks allocated, it is appropriate that examples are stated here).*

- (b) **Recognition of revenue from non-exchange revenue sources:** The principle underlying the recognition of revenue from non-exchange transactions is that if an entity receives an asset in a non-exchange transaction it recognizes revenue in the same amount, provided that the asset can be measured reliably.

IPSAS 23 Defines assets as resources controlled by an entity as a result of past events and from which economic benefits or service potential are expected to flow to the entity.

Under accruals accounting, the public sector entity will recognize revenue when it directly exercises control over these resources or has reliable information on enforceable claims on these resources.

Revenue should only be recognized when control has passed to the receiving entity, on the basis of information which is sufficiently reliable.

- (c) **Assets received but not reported as non-exchange revenue:** These occur when a contributing entity provides and designates funding or other assets as being a permanent contribution, establishing a financial interest in the net asset/equity of the receiving entity. These transactions are disclosed separately and are not part of revenue.

- (d) **The Key differences between IFRS and IPSAS.**

- IPSASB develops accounting standards specifically for government entities. Although it is independent of IASB which develops and issues IFRS, the two standards setters are closely connected with IPSAS being based as far as possible on equivalent IFRS.
- IFRS is aimed at the private-profit seeking sector, where commercial transactions are presumed to take place subject to market conditions.

- IFRSs focus is to provide investors, lenders and other users of the financial statements with information about the entity's financial performance and financial position to help those users make investment and credit decisions; IPSAS financial statements are designed to provide information about how entities utilize resources, and about the cost of service delivery.
 - IPSASs are designed to take care of users' needs. For instance, information about how an entity has performed in relation to its authorized budget is of interest to users. Non-exchange transactions and non - cash generating assets which are prevalent in the public sector, but almost unheard of in the commercial sector enterprises also need to be catered for.
 - IPSAS recognizes the concept of non-exchange transactions and includes public sector specific standard that has been derived from IFRS- IPSAS 23: Revenue from non-exchange transactions covers revenue arising from transfers, grants, taxes, fines and levies. IFRS has no equivalent standard and presumes such transactions are unlikely for private sector entity. One exception of this is IAS 20 government grants which recognizes that entities may receive various forms of government assistance and as such deals with accounting treatment thereof. In contrast, IPSAS has no IAS 20 equivalent and deals with government assistance as part of IPSAS 23. Consequently, the treatment of government grants under IPSAS is significantly different from IFRS.
 - In line with the increased focus on stewardship of, and accountability for, public funds, IPSAS 24 presentation of budget information in the financial statements requires entities that make their budgets publicly available to present a comparison of the budgeted and actual information as part of the financial statements (either separate statements or in the notes). This disclosure is not required under IFRS.
 - IPSAS 21 impairment of non-cash generating assets provides additional guidance on the valuation methods that should be used when determining the value in use of non- cash generating assets. There is no equivalent guidance under IFRS.
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SOLUTION FIVE

(a) Importance of Statement D

- The Statement of Budget Execution shows a comparison between the approved budget and the actual performance.
- Reporting against budget is commonly the mechanism for demonstrating compliance with legal requirements relating to public finances.

(b) Assessment of the financial performance of the Government of the Republic of Zambia for the year ended 31 December 2022.

	Approved	Actual	VARIANCE	VARIANCE %
	K'million	K'million	K'million	
Receipts				
Income Tax	14,514	12,752	(1,762)	-12%
Customs and Excise	3,946	3,958	12	0%
Fuel Levy	759	795	36	5%
Value Added Tax	6,445	10,126	3,681	57%
Fines	35	53	18	51%
Licenses	631	622	(9)	-1%
Commissions	25	21	(4)	-16%
Fees of Court and Office	371	327	(44)	-12%
Other revenue	684	996	312	46%
Bilateral Grants	289	-	(289)	-100%
Multilateral Grants	1,253	-	(1,253)	-100%
Program Grants - General Budget Support	-	145	145	100%
Program Grants - Sector Budget Support	-	146	146	100%
Bilateral External Borrowing	312	1,710	1,398	448%
Multilateral External Borrowing	7,802	7,349	(453)	-6%
Domestic Borrowing	2,199	2,543	344	16%
Total Receipts	39,265	41,543	2,277	6%
Payments				
Personal Emoluments	16,204	15,404	800	5%
Use of Goods and Services	19,758	12,583	7,175	36%
Financial Charges	5,300	4,435	865	16%
Social Benefits	259	172	87	34%
Grants and Other Payments	7,237	6,048	1,189	16%

Constitutional & Statutory Expenditure	-	17	(17)	-100%
Non-Financial Assets	1,369	471	898	66%
Payment of Arrears and Debt Service	391	400	(9)	-2%
Total Expenditure	50,518	39,530	10,989	22%
Net Surplus/(Deficit)	(11,254)	2,013	13,267	118%

C) Explanation of the variances

- The total revenue recorded was 6% above budget whilst total expenditure recorded was 22% below budget. As a result of this overall performance the Government recorded a surplus of K2,013m compared to a budgeted deficit of K11,254m.
- The major variances in terms of revenue were recorded in respect of income tax which was below budget by 12%, value added tax which was above budget by 57%, no multilateral grants were received, bilateral external borrowing was 448% above budget, and domestic borrowing was 16% above budget.
- On the expenditure side, the major variances were recorded in respect of constitutional and statutory expenditure at 100% above budget; non-financial asset at 66% below budget; Use of goods and services which were 36% below budget, grants and other payments were 16% below budget.

END OF SOLUTIONS