CERTIFIED ACCOUNTING TECHNICIAN

STAGE 3 EXAMINATION

S3.6 PUBLIC FINANCIAL MANAGEMENT

DATE: WEDNESDAY, 30 MARCH 2022

MARKING GUIDE AND MODEL ANSWERS

SECTION A

Marking guide

Question Number	**Answer**
1	**D**
2	**D**
3	**D**
4	**B**
5	**D**
6	**D**
7	**D**
8	**D**
9	**B**
10	**B**

		Marks
Question 1 to 10	2 Marks per each correct answer	2
Total marks for this section		**20**

Model answers

QUESTION ONE
The correct answer is D)

a), b) and **c)** are not correct. Even if they are part of government economic interventions they are not used to stabilize the economy during unusual times

There are circumstances when governments may choose to intervene in their country's economy. One of the arguments that justify such government intervention in economies is **economic stabilization**. This is where controls are applied to try to steady the country's economy during unusual times. Economic stabilization policies may be adopted by a government to try to facilitate the economy recovering from economic crisis. Controls applied by governments through economic stabilization may include **direct controls** e.g. freezing salaries and prices, setting minimum wage legislation or rationing certain goods. **Indirect control measures** may also be adopted by governments through taxation or extended social benefit programs.

QUESTION TWO
The correct answer is D) including both **a)** and **b)**

The two statements **a)** and **b)** are wrong and the correct statement is under **c)**

In economic policies, we look at the monetary and fiscal government economic policies as well as the impact of demand and supply on government policies.
Monetary policy is the action that a country's central bank or government take to influence how much money is in the economy and how much it costs to borrow. And one of the key instruments utilized to implement the monetary policy framework is the **open market operations** where the central bank mops up or injects liquidity in the banking system to keep the reserve money as desired.
Fiscal Policy is the use of government expenditure and revenue collection to influence the economy.

QUESTION THREE

The correct answer is D) including both **a)** and **c)**

a) and **c)** are correct and **b)** is wrong because the auditor general is responsible for the audit of the state finances

In the budgeting process, various parties are involved at different level of the budget cycle from the formulation stage to the evaluation. The **Chamber of Deputies and the Council of the decentralized entity** are the key players in this process with the responsibility to account on the use of public resources where they may summon members of cabinet, chief budget managers or members of the Executive Committee of a decentralized entity to come before them and explain any policies, programs and utilization of their budget.

QUESTION FOUR

The correct answer is B)

a) is wrong because it refers to tax avoidance **c)** is wrong because it is an example of tax avoidance **d)** is wrong because it combines two wrong answers **a)** and **c)**

The action of not registering employees by the construction company stated in the scenario is qualified as **tax evasion** which is the illegal misrepresentation of financial affairs to reduce tax liability. This is different from **tax avoidance** which is the legal management of financial affairs within the constraints of the tax system to minimize the amount of tax paid. **Receive tax-free benefits from employer instead of a taxable pay** is one of the examples of tax avoidance.

QUESTION FIVE

The correct answer is D) including both **b)** and **c)**

a) is wrong because the investment of cash for a short-term period is done in case of surplus cash and the scenario shows a shortage of cash.

Both **b)** and **c)** are correct because smoothing the timing of payments and negotiate for additional resources are part of responses to the period of negative cash flows.

One of the key purposes of a cash flow plan is to determine how much cash is required for each period. In order to be useful the cash flow plans must be interpreted and monitored, with corrective action taken as required.

The emergency requiring extra cash at the district hospital might affect the cash flows and lead to **negative cash flows** during the quarter three of implementation. To respond to that the cash flow officer would give the management an advice to **negotiate for additional resources** or by **smoothing the timing of payments**.

QUESTION SIX

The correct answer is D) including both **a)** and **b)**

a) and **b)** are both correct because they are part of IFMIS benefits more dependent on the successful design and features of the individual IFMIS
c) is not correct because it doesn't depend on the design and features of IFMIS

The implementation of Integrated Financial Management Information System(IFMIS) can offer to the public sector more benefits by improving their Public Finance Management(PFM). However, the achievement of any of the potential benefits from the implementation of IFMIS is dependent on the successful design and features of the individual IFMIS. Those potential benefits include the following:

- Enable efficient resource allocation mechanisms
- Improve management information for decision making
- Establish effective link between accounting and financial management
- Improve financial controls with reliable and timely financial information
- Improve accounting, recording and reporting through timely and accurate financial date provision
- Accelerate the pace or scope of economic growth

QUESTION SEVEN

The correct answer is D
Because it relates to the specific period for budget planning i.e. September to December

a) is wrong because August to September is a budget reporting period at the agency level, **b)** and **c)** are wrong because they don't relate to any specific period

Various stages of the budget cycle within the public sector follow a specific timing at the national as well as agency level. At the agency level, the budget process follows the calendar below:

Budget process	**Period**
Budget Planning	September - December
Budget Formulation	December - March
Budget Execution	July - June
Budget Reporting	July - September

QUESTION EIGHT

The correct answer is D)

a), **b)** and **c)** are not correct because the supreme audit institution is the one having the mandate or the responsibility to audit state finances

The core audit structure comprises the Supreme or State Audit Institution (SAI), external audit and internal audit. In Rwanda, the SAI is the Office of the Auditor General (OAG) with the following responsibilities:

- Audit revenues and expenditures of the State, as well as other local administrative entities and government projects
- Audit the finances of the public sector, verifying whether the expenditures were in conformity with laws and regulations in force and sound management and whether they were necessary
- Carry out all audits of accounts, efficient management, control of the functioning of state organizations
- Submit an annual report to each Chamber of Parliament, prior to the commencement of the session devoted to the examination of the budget of the following year, on the consolidated state accounts for the previous year indicating the manner in which the budget was utilized

It is also important to note that within the role of the SAI, the OAG is responsible for the external audit of the country's public sector entities. However, the OAG also has the mandate to authorize other qualified auditors to undertake the external audit of Government entities on its behalf.

Internal audit provides independent assurance that an organization's risk management, governance and internal control processes are operating effectively.

QUESTION NINE

The correct answer is B) because the evaluation is not part of the key elements supply chain.

a), c) and **d)** are part of the key elements of supply chain

The supply chain is the sequence of processes involved in the production and distribution of goods or services. The key issue within the supply chain is that the purchasing organization is reliant on the supplier or components within the supply chain and some of these are outside their direct control. The supply chain management is concerned with these activities outside their direct control e.g. quality, dependability, cost or flexibility of the suppliers.

The Core elements of the supply chain are:

- **Plan** – this relates to the overall strategy that an organization has in place in relation to meeting requirements and needs. This stage may also include specifying desired or acceptable quality standards for resources.
- **Source** – choosing the supplier as to where the goods or services will be obtained from or who will provide them. Decisions may also be made on when and how much is needed, depending on demand and existing inventory levels.
- **Logistics** – receive orders, network of warehouses where deliveries will be stored
- **Return** – this relates to the arrangements in place to permit the return of damaged or incorrect goods received through the network

Evaluation is not part of the core elements of the supply chain.

QUESTION 10

The correct answer is B)

a) and **c)** are not correct because proportionate tax and regressive tax are not based on an individual's ability to pay

d) is not correct because it is a combination of a wrong (proportionate tax) and correct answer (progressive tax)

Governments set rates of tax on a tax base and the impact of the tax base and rate may be linked to whether the tax structure is progressive, proportionate or regressive.

Progressive taxes mean that the taxes represent a larger proportion of an individual's income as that individual's income rises and they are often seen as fairer as they are **based on an individual's ability to pay** e.g. income tax.

On the other hand, **regressive taxes** are considered as the opposite of progressive taxes and these are where taxes paid is a larger proportion of poorer individual's income than a richer person e.g. value added tax. A **proportionate tax** is considered as flat rate tax and is where a single tax rate applies.

SECTION B

QUESTION 11
Marking guide

	Marks
Define recurrent budget	1
Define development budget	1
Explaining with examples the difference between recurrent and development budget	5

1. Everyday costs Vs long term benefit (1 mark)
2. Presentation of recurrent and development budget (1 mark)
3. Implications of development budget to recurrent budget (1 mark)
4. Integration of both budgets in the budget formulation process (1 mark)
5. Any other relevant point (1mark)

Classification of items provided under recurrent or development budget (0.5 mark per item classified properly)	3
Total	**10**

Model answers

The **recurrent or revenue budget** refers to the annual budget that covers a single financial year.

The **development or capital budget** refers to the budget that tend to cover several years because expenditure on a development project will usually be over a number of financial years.

The main difference between the recurrent and development budgets comes from the benefit and timing of their respective expenditures.

For instance, recurrent or revenue expenditures relate to everyday running costs or payments on items that will not have a long-term benefit to the organization these include everyday expenses such as staff salaries, office supplies, employees training costs, water and electricity bills, communication costs, etc.

The development or capital expenditures on the other hand, relate to payments on items that will benefit the organization in the long term, usually taken as more than one financial year. These refer to construction of office building, purchase of hospital ambulances, purchase of laboratory equipment, etc.

Though the recurrent and development budgets are presented separately, it is important to note that they should not be isolated as often capital projects will actually have implications on the recurrent budget e.g., if a government builds a district hospital which will be operational in four years' time, from that point in four years' time the recurrent budget must include running costs for doctors and other medical staff, medical supplies, etc. The integration of both budgets is highly important during the budget formulation process.

From items provided in the scenario, laboratory equipment and office building fall under development or capital expenditures while medical staff salaries, electricity bills, training of medical staff and office supplies fall under recurrent or revenue expenditures.

QUESTION 12
Marking guide

	Marks
Define internal audit	1
Define external audit	1
Suggest the correct argument	2
1. Correct argument (1 mark)	
2. Justification of the argument (1 mark)	
Explain the difference between internal and external audit	6
1. Internal audit	
• carry out audits on different systems and activities throughout the year (1 mark)	
• provide recommendations for the necessary improvements on the systems or implementation of activities (1 mark)	
• employees of the organization being audited (0.5marks)	
2. External audit	
• review the year-end financial statements (1 mark)	
• give an opinion as to whether the statements represent a fair view of the organization (1 mark)	
• not employed by the organization being audited (0.5 marks)	
• any other relevant point (1 mark)	
Total	**10**

Model answers

In the public sector, internal audit provides independent assurance that an organization's risk management, governance and internal control processes are operating effectively while external audit is involved in financial, compliance and performance audits.

The argument of postponing internal audit activities planned in the boarding schools of Eastern Province because a planned external audit should not be accepted because the two audits are distinct given their respective objectives. It is preferable to have an internal audit first in order respond to the internal audit recommendations and ensure everything in order when the external audit starts the assignment. It is also important to recognize that external auditors may rely on the work undertaken by internal auditors.

As stated above internal audit and external audit have different roles and objectives.

The external auditors review the year-end financial statements, and give an opinion as to whether the statements represent a fair view of the organization. These auditors are not employed by the organization being audited.

In contrast, the internal auditors are based at a single public sector entity and they carry out audits on different systems and activities throughout the year where recommendations are given for the necessary improvements on the systems or implementation of activities. These are employed by the organization being audited.

SECTION C

QUESTION 13
Marking guide

	Marks
a) identify other sources of revenue to government in the scenario (1 mark per identified source)	6
b) Discuss other sources of government revenue identified	
Customs duties and tariffs	4
Licenses	2
Royalties	2
Fines	2
Profits from state owned enterprises	2
Asset sales	2
Total	**20**

Model answers

Apart from taxes and international aid (i.e. grants and donor aid) there are other potential **sources of** revenue available to government.

In the given scenario other sources identified are charges on/or from imported goods, started business activities, mining industries, business companies which did not issue an EBM receipt to their customers, sale of government unused cars and dividends declared by government business enterprises.

When a company has imported goods a levy or tax has to be charged on those goods and this is known as customs duties and tariffs which are part of other sources of revenue to government. These duties and tariffs may vary depending on country and nature of those goods. Note that goods that meet certain Customs Rules of Origin will enjoy preferential community tariffs. E.g. member states of East African Community enjoy the later due to East African Community Customs Act signed by member states.

Any person starting up a profit-oriented activity in the country is also required to pay a certain fee calculated on the basis of turnover. This fee is known as trading license and is part of other sources of revenue for the government

Royalties as other potential source of government revenue might come from tax due for the extraction of minerals. This means that holders of mining rights are liable to mineral royalty on minerals produced under their respective licenses.

Every business is required to comply with laws, regulations or pay required taxes. Due to noncompliance government bodies may choose to enforce fines or impose penalties. e.g. a VAT registered company not issuing EBM receipts to its client, or a driver violating traffic lights may be charged a fine or penalty due to noncompliance. These fines or penalties are part of other sources of revenue to government.

At the end of the year, every Government Business Enterprise is requested to prepare the financial statements. Once these are audited and dividends are declared, government is entitled to its share of dividend and this qualify to be another source of revenue for the government.

Last but not least, the government may plan to sale some of its unused or old assets e.g. cars, IT equipment, office equipment, etc. Once sold, the money goes to the account of the national treasury and this is also another source of revenue to the government.

QUESTION 14

Marking guide

	Marks
a) Identify 7 elements of PFM	**7 Marks**
National Priorities	1
National MTEF	1
Agency budget and MTEF	1
Finance law	1
Budget Execution	1
Accounting and Monitoring	1
Reporting and Audit	1
b) Discuss how they may be applied to a public sector organization of your choice	**13 Marks**
National Priorities	2
National MTEF	2
Agency budget and MTEF	2
Finance law	2
Budget Execution	2
Accounting and Monitoring	2
Reporting and Audit	1
Total	**20**

Model answers

a) There are seven key elements of Public Finance Management (PFM) cycle namely:
National priorities, National Medium-Term Economic Framework (MTEF), Agency budget and MTEF, Finance law, Budget execution, Accounting and monitoring, Reporting and auditing

b) The specific details will vary by the chosen public sector organization. However, the key elements of the generic PFM cycle should be discussed as follows:

1. National priorities- the public sector organization should have strategic objectives/plan in place aligned to national priorities.

2. National MTEF- these should be MTEF in place which links the strategic objectives to the annual budgeted expenditure. Ensuring that planned expenditure is focused on the key priorities.

3. **Agency budget and MTEF-** this element will depend on the public sector organization chosen, but the central governments overall budget will need to be fed down to government department and agencies, as relevant and their expenditure allocations should be based on their strategic priorities.

4. Finance law -there should be legal arrangements for process to be followed and the budget formally approved, such as through parliament.

5. Budget execution- this covers the day-to-day processes for the budget year, with expenditure being authorized and surplus invested, for example. Ideally, the budget holders should be ensuring that authorized expenditure is consistent with the budget.

6. Accounting and monitoring- this covers procurement, revenue collection and recording transactions on the financial accounting systems. There should also be monthly budget monitoring reports produced to compare actual and budgeted expenditure, with significant variances investigated

7. Reporting and audit- this includes the preparation and submission of the annual financial statements and also ensure they are audited by the external auditor with an opinion given on whether the financial statements give a true and fair view or are free from material misstatement.

QUESTION 15
Marking guide

a) Identify supporting International Public Sector Accounting Standards (IPSAS) to each item	**Marks**
Intangible assets	1
Cash and cash equivalents	1
Inventories	1
Property, plant, and equipment	1
Financial assets	1
Investment properties	1
b) Which International Public Sector Accounting Standards (IPSAS) should guide Robert on this scenario and explain why	
Action to take upon receipt of the information	1
Identification of the guiding IPSAS	1
Providing reasons behind the selection of the guiding IPSAS above	6
Total	**20**

Model answers

a)

#	Items in the statement of financial position	Specific supporting IPSAS
1	Intangible assets	IPSAS 31
2	Cash and cash equivalents	IPSAS 2
3	Inventories	IPSAS 12
4	Property, plant and equipment	IPSAS 17
5	Financial assets	IPSAS 41
6	Investment properties	IPSAS 16

b)

Immediately after getting the information, Robert should ask for the signed minutes of the meeting approving the performance bonus to confirm the validity of the information received and the amount of performance bonus approved.

Robert will be guided by IPSAS 14 Events after the reporting date. Because the approval of the bonus occurred after 30th June 2021.

Events after the reporting date are those events both favorable and unfavorable that occur between the reporting date and the date when the financial statements are authorized for issue. Those events can be adjusting or non-adjusting.

Adjusting events are those events that provide evidence of conditions that existed at the reporting date and these should be recognized in the financial statements. Non-adjusting events refer to those that are indicative of conditions that arose after the reporting date and these should be disclosed.

Since the performance bonus was approved before the financial statements are authorized for issue Robert should adjust the amounts recognized in the financial statements to reflect adjusting events after the reporting date because the entity had a present legal obligation at the reporting date to make such payment as a result of events before that date.

c) Currently, the public sector financial reporting usually is based on modified cash basis of accounting, where the books are held open for a specified period after year end, such as one month to recognize the cash flows which relate to the current year spending that may not occur until after the end of the year but the receipts and payments that have been occurred during the specified period and originated in the previous reporting period should be recognized as receipts and payments of the previous financial year. i.e., modified cash basis recognizes the outstanding invoices and receipts at the end of reporting period.

The public sector also they base on International Public Sector Accounting Standards (IPSAS) to report their financial statement.

So, the main issues particular to public sector financial reporting encountered when producing a statement of financial position are:

- ✓ IPAS 1 does not set a specific format for statement of financial position (SOFP), this may ready to different reporting format as each reporting entity may use its own format.
- ✓ Each individual of public sector entity sets its format for reporting, hence during consolidation may not be easy for consolidating entity.
- ✓ Due to different format, some may produce its SOFP in vertical or horizontal format, hence during the comparability may creates an additional job so that the comparability should be easy to interpret.

END OF MARKING GUIDE AND MODEL ANSWERS