
CERTIFIED ACCOUNTING TECHNICIAN (CAT)
STAGE 3 EXAMINATION
S3.6 PUBLIC FINANCIAL MANAGEMENT
PILOT PAPER

ANSWERS

Section A – Answer Grid

1. A
2. C
3. B
4. E
5. C
6. D
7. D
8. B
9. A
10. B

Section A – Suggested solutions

Marking scheme

	Marks
2 marks for each correct answer	<u>2</u>
Total marks for this section	<u>20</u>

1. A Agreeing a year-end bank balance figure to a bank statement demonstrates verifiability, as the reported figure is being supported by an external source.

The agreement of the bank balance is not timely as it has taken six months. Comparability would be if the user of the financial statement compared the bank balance to a prior year or different company. Users of the financial statement are not able to use the information regarding agreeing the year-end balance to the bank to influence the user's decision-making, so it is not demonstrating relevance.

(LO 7.1)
2. C A medium-term expenditure framework (MTEF) is an expenditure plan that is updated annually to cover a three or four year period.

A cash budget could cover one month; an annual budget would cover one year, and ten years is classed as long term.

(LO 2.1)
3. B The grant funds may only be used for a specific purpose which is known as appropriation.

Profiling is how the total annual budget is split across the months to show the timing of the budget spend over the year. Virements are where budgeted funds are moved from one budget heading to another during the budget year. Incremental budgeting is where next year's budget is prepared using the current year's as a starting point, and adjustments are made for changes, such as expected inflation.

(LO 2.5)
4. E None of the above. (i), (ii), (iii) and (iv) are all features of effective charging.

(LO 3.5)
5. C (i) and (iii). Official Development Assistance (ODA) is international aid that targets and promotes economic development and welfare of developing countries. Bilateral aid flows from the donor government sources directly to official government sources in the recipient country.

Grants are transfers made in cash, goods or services for which no repayment is required. Multilateral aid relates to contributions from government sources to multilateral agencies where it is then used to fund the multilateral agencies' own programmes.

(LO 3.7)

6. D (i) and (ii). Market research and supplier management are two elements of the sourcing stage of procurement, in addition to the establishment and signature of the short list.

Contract management is the final stage of the procurement process.

(LO 4.2)

7. D Receipts. Cash flows into the organisation are known as receipts and should be included in a cash budget.

Depreciation is not a cash flow. Income and expenditure do not have the same timings as cash, such as payments made on credit, and cash budgets should be prepared based on cash flows.

(LO 5.2)

8. B (i) and (ii). Internal audit should provide independent assurance relating to an organisation's risk management and governance, as well as their internal control processes.

It is the role of external audit to review the financial statements.

(LO 6.4)

9. A Phased implementation, such as implementing the IFMIS one module at a time, can help overcome the risks attached to it being more complex than envisaged.

Change management, legal guidance and staff training are all best practice guidelines for the successful implementation of IFMIS but not specifically responding to increased complexity.

(LO 7.8)

10. B (iii) only. Government finance statistics (GFS) are produced by governments on the general government sector (GGS) for macroeconomic analysis and decision-making purposes.

Public sector organisations produce year-end financial statements and these are published externally. Rose is likely to notice a higher volume of non-exchange transactions than in the private sector.

(LO 8.1)

Section B – Suggested solutions

11.

Marking scheme

	Marks
Define the supply chain	1
Identify components of the supply chain	1
Explain planning component of the supply chain and relate it to the scenario	2
Explain sourcing component of the supply chain and relate it to the scenario	2
Explain logistics component of the supply chain and relate it to the scenario	2
Explain return component of the supply chain and relate it to the scenario	<u>2</u>
Total	<u>10</u>

Detailed suggested answer

The supply chain is the sequence of processes involved in the production and distribution of goods or services.

The supply chain comprises the four key elements of planning, sourcing, logistics and return.

The first stage of the supply chain is planning, which relates to the overall strategy that the ministry of education has in place in relation to meeting requirements and needs. This stage may also include specifying desired or acceptable quality standards for resources, such as the ministry's requirements for the office chairs to meet health and safety requirements. There is also the need for each employee to have their own individual office chair and desk space.

The second stage of the supply chain is sourcing. This involves choosing the supplier from which the office desks and chairs will be obtained. The ministry of education has already made decisions on when the replacement office furniture is needed (within the next six months) and that 260 office chairs and 260 desks are required. This information can be used by the ministry of education to obtain quotes from suppliers in order to select a supplier offering best price, as well as meeting the requirements previously specified. The ministry's central procurement facility should oversee this process, which is likely to be based around the existing list of approved suppliers.

The third stage of the supply chain is logistics, which involves the suppliers receiving the orders placed by the ministry of education and then the ministry receiving the office furniture. Due to the number of office chairs and desks being ordered the ministry will need to carefully plan how, where and when the chairs and desks are to be delivered (eg how many to each location) and the practicalities of removing the old office furniture to make room for the new furniture. Timing will be critical as the ministry of education

will want to avoid staff being left without chairs and desks for any significant length of time. The facilities staff will undertake the physical movement of furniture and disposal of old furniture.

The final stage of sourcing is the return stage. On receipt of the office furniture, the ministry of education should thoroughly check that all the chairs and desks are not damaged and that the adjustment functions of the chairs work correctly. Any damaged or faulty furniture should be returned to the supplier. The ministry should ensure that any returns are either appropriately refunded or replaced and should ensure that such arrangements are permitted prior to ordering with any individual supplier.

(LO 4.3)

12.

Marking scheme

	Marks
Define and identify tax bases	1
Explain the income tax base within the scenario	1
Explain the expenditure tax base within the scenario	1
Identify types of tax structure	1
Explain progressive taxes and apply to scenario	2
Explain regressive taxes and apply to scenario	2
Explain proportionate taxes and apply to scenario	2
Total	<u><u>10</u></u>

Detailed suggested answer

A tax base is the value of assets, property or equivalent which are subject to a specific tax.

An income tax base is where tax is levied on earnings, such as salaries and wages. For example, all workers are charged a flat rate of 25% of their earnings irrespective of the amount they earn or how they work.

An expenditure base is where taxes are paid on what somebody spends. For example, value added tax is a tax added to all goods and services at each point in the supply chain where value is added to a good or service. Certain goods and services, such as medical supplies are exempt.

Tax bases and rates set may be linked to the type of tax structure adopted. Tax structure may be progressive, regressive or proportionate.

Progressive taxes are where taxes represent a larger proportion of an individual's income as that individual's income rises and are often seen as fairer as they are based on an individual's ability to pay. The calls for the tax payable on earnings to move to 30% for high earners and 20% for low earners would be a progressive tax.

Regressive taxes are where the taxes paid is a larger proportion of poorer individual's income than a richer person. The value added tax of 15% added to all goods and

services is an example of a regressive tax, as the amount of tax payable does not depend on the level of income or ability to pay of the consumer.

A proportionate tax (or flat rate tax) is where a single tax rate applies. The tax of 25% payable on all earnings by every worker, irrespective of how much they earn or what type of work, is an example of proportionate tax. There are arguments both for and against the fairness of proportionate taxes.

(LO 3.1 and 3.3)

Section C - Suggested solutions

13.

Marking scheme

		Marks
(a)	Explain and apply example direct control measures	3
	Explain and apply example indirect control measures	3
		6
(b)	Explain market failure and identify market failure examples	4
	Explain demerit goods and apply to sugary food	2
	Methods to address sugary food market failure	3
	Explain geographical and occupational factor immobility and apply to mine workers	3
	Methods to address factor immobility	2
		14
	Total	20

Detailed solution

- (a) The government could apply direct or indirect control measures to help stabilise the economy.

Direct control measures the government could adopt include freezing salaries and prices, setting minimum wage legislation or rationing certain goods. In this scenario, with the government keen to encourage the public to spend, freezing prices of goods and establishing a minimum wage legislation may be useful.

The government could alternatively apply indirect control measures, such as through taxation. For example, tax rates could be amended and social benefits programmes extended to increase the ability of taxpayers and benefit recipients to spend through having more cash available. This in turn would stimulate the economy.

(LO 1.2)

- (b) Market failure is where the operation of the markets distorts the economic outcome, thereby justifying government intervention to improve the situation. There are different types of market failure, where government intervention can improve efficiency. Examples of market failure include demerit goods, such as low cost sugary food; merit goods, such as healthy food alternatives; and factor immobility, such as geographical and occupational due the mine closure.

One type of market failure is the availability of low cost sugary foods which may be deemed demerit goods, as they are thought to be bad for the consumer. There is widespread obesity and associated health problems in the country, resulting from excessive consumption of low cost sugary foods.

Consumers of demerit goods, such as sugary foods, may underestimate the disbenefits to themselves due to lack of information. Therefore, the government could act to discourage the consumption of sugary foods such as through a health campaign to warn people of the harmful effects of sugary foods and resulting obesity. Alternatively, the government could introduce an additional tax charge on sugary foods, which would deter people purchasing them by making them more expensive.

Factor immobility relates to the occupational or geographical immobility factor of production, and is another market failure example that is evident in this country. The closure of the last mine is likely to result in factor immobility, particularly occupational immobility as the mine's employees are not trained for any other type of employment. With so many people losing their jobs, there is likely to be high unemployment in the region. As this last mine is based within a close knit community, there may also be geographical immobility as workers may not want to move away to other areas to find work.

To address factor immobility market failure, the government could provide funds and support initiatives, such as to provide retraining opportunities or subsidise relocations to other areas of the country where additional labour is required.

(LO 1.2 and 1.3)

14.

Marking scheme

		Marks
(a)	Effect of unemployment (reduced taxes received and increased benefits payable)	3
	Impact of high inflation	1
		4
(b)	Define ZBB	1
	Identify and apply ZBB advantages to the scenario	3
	Identify and apply ZBB disadvantages to the scenario	4
		8
(c)	Define performance-based budgeting (PBB)	1
	Identify three types of PBB	2

Explain application of different PBB types	3
Identify and explain implementation of PBB (eg top down, incremental)	2
	<u>8</u>
Total	<u><u>20</u></u>

Detailed solution

- (a) The government will be restricted to set the revenue budget within affordable limits.

Inflation being higher than expected will mean that the cost of items within the revenue budget is likely to be higher than expected and higher than the previous year.

Increased unemployment levels will also impact on the revenue the government is likely to receive and increase their expenditure. Revenue from income taxes will be reduced as the number of workers who are now unemployed so will not be paying income on their earnings has increased. Additionally, many of these unemployed individuals will consequently claim benefits which will then increase the government's expenditure.

(LO 2.6)

- (b) Zero-based budgeting (ZBB) is a method of budgeting that requires each cost element to be specifically justified as though the activities to which the budget relates were being undertaken for the first time.

One advantage of ZBB is that it would enable the government department to identify and remove inefficient or obsolete operations that may be simply carried forward with incremental budgeting. ZBB would also force employees to avoid wasteful expenditure, as well as increasing motivation. ZBB responds to changes in the business environment, so would help the government department respond to the implications of high inflation and increased unemployment, such as reduced income from taxes and increased costs or social benefit payments. Overall, the ZBB documentation provides an in-depth appraisal of an organisation's operations, enabling the government department to challenge the status quo and enable more efficient allocation of resources.

The major disadvantage of ZBB is the volume of extra paperwork created, particularly in comparison to the government department's existing incremental approach. The government department would need to continually assess and update the assumptions about costs and benefits for all activities, as well as for any new activities that emerge. Managers within the government department may then feel under pressure to respond to unforeseen opportunities and threats that arise that were not included within the original ZBB ranking assessment. Implementing ZBB is also very complex, particularly compared to the department's incremental approach, and the existing staff are unlikely to have such skills having worked in the public sector for many years. The department may, therefore, need to invest in managers being trained in ZBB techniques which will be costly both financially and time wise. Even with training, ZBB can be difficult to undertake particularly due to the nature of the public sector, with the government department required to provide statutory services meaning that managers will need to rank activities based on qualitative rather than quantitative benefits. The government department's information system is old and simple, meaning that it may not be capable of providing suitable information and may need investment to upgrade and make it suitable.

(LO 2.7)

- (c) Performance-based budgeting is an approach to budgeting that links allocated funds to measurable results. There are different ways of applying performance-based budgeting, such as presentational performance budgeting, performance-informed budgeting or direct performance budgeting.

To apply presentational performance budgeting, the government department would need to present performance information in budget documents or other government documents.

Performance-informed budgeting is where resources are indirectly related to proposed future performance or to past performance. So, when setting the budget, the government department would need to review past or targeted future performance and use this as a base on which to allocate resources.

Direct performance budgeting is where resources are allocated based on results achieved, so the government department would assess past performance and use this as a base to allocate resources.

To measure performance, the government department could use outputs of the services being delivered, or outcomes which are the expected results from delivering these services.

Implementation of performance-based budgeting could be led by central government, which would be a top down approach, or developed, implemented and reviewed by the government department itself which would be a bottom-up approach. The bottom-up approach would appear to fit more closely with current arrangements. Additionally, the government department could choose to fully move from incremental to performance-based budgeting completely from a set date and across the full department or even government. Alternatively, performance-based budgeting could be implemented gradually over several years, perhaps for certain activities or sections of the department.

(LO 2.7)

15.

Marking scheme

		Marks
(a)	Identify three types of external audit (financial, compliance, performance)	1
	Explain and apply each of the three types of external audit to the scenario	3
		4
(b)	Identify OAG as Rwanda's SAI	1
	Explanation of INTOSAI	1
	Explanation of ISAAI11	2
		4
(c)	Identification of ISSAI standards	1
	Identification of ISA standards	1
	Explanation and application of ISSAI with examples	5
	Explanation and application ISA with examples	5
		12
	Total	<u><u>20</u></u>

Detailed solution

- (a) There are three main types of external audit; financial, compliance and performance.

A financial external audit involves the external auditor examining an organisation's financial statements and providing a view on the fairness of the information presented. The audit of the government's consolidated financial statements comprising central and local government entities would be a financial external audit.

A compliance audit is concerned with whether the audited body has complied with relevant regulations and standards. The review of policies and procedures expected by the government entities, and whether their expenditure is lawful, would be part of a compliance audit, along with the opinion provided on adherence to laws, regulations and procedures.

Performance audits or value for money (VFM) audits involve external audit providing an independent review on whether a particular service is economical, efficient and effective. Such an audit would be applicable to services provided by the central and local government entities, but there is no suggestion the forthcoming audit will involve a VFM element.

(LO 6.3)

- (b) The SAI in Rwanda is the Office of the Auditor General (OAG).

The OAG of Rwanda is a member of the International Organization of Supreme Audit Institutions (INTOSAI). The INTOSAI issue the International Standards of Supreme Audit Institutions (ISSAI) with which the OAG should comply.

One key standard is the ISSAI 11 Guidelines and Good Practices Related to SAI Independence, which covers the essential underlying principles of audit independence. The ISSAI 11 standard sets out principles, guidelines and good practices in relation to the independence of SAIs such as legislation setting out the SAI's independence and that the SAI should have unrestricted access to information.

(LO 6.1)

- (c) There are two main types of standards with which the OAG as SAI should comply; the International Standards of Supreme Audit Institutions (ISSAI) and the International Standards on Auditing (ISA).

The International Auditing and Assurance Standards Board (IAASB) is the independent standard-setting body that develops and issues international standards for auditing and other assurance or related services. Specifically, the IAASB produces ISA and the OAG in Rwanda is committed to complying with the IAASB's ISAs.

There are numerous ISAs but some key ones with which the OAG must comply within their external audit of the government's consolidated financial statements would include ISA 230, Audit Documentation; ISA 300, Planning and Audit of Financial Statements; ISA 500, Audit Evidence and 610, Using the Work of Internal Auditors.

An essential ISA is the 200 Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing, which covers the basics of audit.

As the SAI, the OAG is also required to comply with the ISSAI, which are developed and published by INTOSAI. There are many ISSAI, including the ISSAI 11 on independence.

Another key ISSAI is ISSAI 100 Fundamental Principles of Public-Sector Auditing, which covers the framework for public-sector auditing, elements of public-sector auditing (including parties involved and types of engagements and assurance) and principles to be applied in public-sector auditing, including ethics, independence and professional judgement.

A specific ISSAI that covers financial auditing is ISSAI 200 Fundamental Principles of Financial Auditing. As the OAG is preparing to undertake a financial audit, this standard is particularly relevant.

(LO 6.2)