The Southern African Institute of Government Auditors

Qualifying Examination for Registered Government Auditors

Paper 2: Accounting

November 2012

INSTRUCTIONS TO CANDIDATES

1 Maximum marks: **160**.
2 Total time available: **four hours**.
3 The marks allocated to each question are an indication of the expected length and required depth of the answer.
4 Ensure proper planning and avoid exceeding the time you have allocated for each question as suggested by the number of marks allocated to the question.
5 Present your arguments clearly, using well structured, clear and precise language and appropriate professional terms.
6 No books or notes are allowed in the examination room.
7 All working papers must be handed in together with all paper provided for the examination (including unused answer sheets).
8 Answers written in pencil will not be marked.
9 You are reminded that this examination will be held under the rules as set out in the document “RGA-QE Examination Matters & Examination Policy 2012”.
10 You are required to observe all Examination Instructions on the separate sheet of paper handed to you before commencement of this examination.

SAIGA
ADVANCING AUDITING AND ACCOUNTABILITY

QUESTION 1 **(80 marks)**

PART A **(70 marks)**

The aim of the Department of Cultural Affairs is to develop and preserve South African culture, to ensure social cohesion, and to promote nation building. The Department contributes to the country's economic growth by making interventions to improve cultural industries and to promote these by facilitating access to international networking platforms and markets.

The following information is available in addition to the trial balance of the Department:

1 Aid assistance came from the South African tourism community to provide vulnerable groups with access to arts, culture and heritage programmes.

2 The debtors account increase for the 2011/12 financial year was due to a debt take-on for fruitless and wasteful expenditure on stationery and printing that occurred in the 2010/11 financial year. Of this debt R40 000 was recovered in the 2011/12 financial year but the recovery transactions still need to be recorded in the records of the Department.

3 Unauthorised expenditure not in accordance with the purpose of the vote, in the amount of R15 000, was confirmed in the 2011/12 financial year. This transaction still needs to be recorded in the records of the Department.

REQUIRED:
(No comparative figures needed for statements or notes)

(a) Compile a Statement of Financial Performance for the Department of Cultural Affairs for the year ending 31 March 2012 (15)

(b) Compile a Statement of Financial Position for the Department of Cultural Affairs on 31 March 2012. (9)

(c) Compile a Cash Flow Statement for the Department of Cultural Affairs on 31 March 2012. (16)

(d) Show the following notes to the financial statements: (21)

- i Cash and cash equivalents
- ii Voted funds to be surrendered to the Revenue Fund
- iii Departmental revenue to be surrendered to the Revenue Fund
- iv Net cash flow available from operating activities

(e) Use the information from the trial balance after the adjustments have been taken into account to present the year's opening and closing transactions for the annual appropriation, funds requisition (summarised for the year), expenditure against voted funds and departmental revenue in **ledger account format. Show only the following accounts:** (9)

i Exchequer Grant Account
ii Revenue Accrual Account

Please find the trial balance of the department as Attachment 1.

PART B **(10 marks)**

You are part of the audit team that audits the Annual Financial Statements of the Department of Cultural Affairs. A new Chief Financial Officer (CFO) has been appointed to the Department. It is his first appointment in the public service and as a result he is studying the relevant legislative requirements pertaining to the Annual Financial Statements. You have indicated that you are willing to assist him in any matter that he needs clarification on.

There is one matter that confuses him. The Public Finance Management Act (PFMA) requires departments to "prepare financial statements for each financial year in accordance with *generally recognised accounting practice*" (GRAP). GRAP is defined by the PFMA as an accounting practice complying in all material aspects with the standards issued by the Accounting Standards Board. Yet, the CFO knows that currently the Department is not applying the GRAP standards.

REQUIRED:

Write a report to the CFO of the Department explaining the current situation as described above.

ATTACHMENT 1

Trial balance for the Dept of Cultural Affairs on 31 March 2012

Accounts	R	
	2011/12	2010/11
Annual appropriation	(120 000 000)	(100 000 000)
Coat of arms registration fees	(3 100 000)	(2 000 000)
Sale of equipment (capital)	(1 893 000)	(5 790 200)
Material losses recovered	(500 000)	(1 750 000)
Aid assistance revenue	(12 500 000)	(10 000 000)
Salaries	40 500 940	35 900 000
Medical aid contribution	12 470 600	10 800 400
Pension fund contribution	11 354 000	9 570 200
Housing subsidy	6 180 600	4 176 000
Employee relocation expenses	240 000	170 000
Advertising	350 000	290 000
Catering	220 000	150 000
Property expenditure	536 000	467 000
Operating leases	251 000	231 000
Interest and rent on land	135 400	95 000
Stationery and printing	241 800	298 000
Assets less than R5000	4 280 000	2 700 600
Machinery and equipment (capital)	15 600 700	4 500 100
Land (capital)	9 462 300	3 815 700
Copyright registration (capital)	894 000	3 185 000
IT services	900 000	850 000
Auditing fees	841 300	752 000
Aid assistance expenditure (current)	11 800 000	10 000 000
Employee severance pay expenditure	2 136 000	1 200 670
Art institution transfer payment	2 000 000	1 700 000
National film and video foundation transfer	2 800 000	3 200 000
Playhouse maintenance transfer (capital)	5 614 000	4 187 000
General Account of Revenue	5 000 000	6 790 200
Paymaster General Account	3 779 910	14 493 880
Deposit account	25 600	48 750
Petty cash	45 000	45 000
Debtor account	163 900	83 000
Subsistence and travel advances	134 600	124 000
Unauthorised expenditure	56 000	56 000
Cheques payable	(120 650)	(178 900)
Unallocated receipt control account	(10 900)	(13 700)
Bank adjustment account	1 800	(4 300)
EBT payment account	(50 000)	(47 000)
Salary deductions control account	(125 000)	(95 400)
Recoverable Revenue	(80 900)	
Exchequer grant account	365 000	
	0	0

QUESTION 2 **(40 marks)**

QUESTION 2.1 **(15 marks)**

The municipality enters into a lease agreement with Nashua for a photocopier. The lease is for a period of 36 months, with the first instalment due on 31 August 2010. The rental is R12 750 per month and increases by 10% annually. A discount rate of 12.50% is used. Although the lease agreement meets the requirements of a deemed finance lease, the municipality accounted for the lease as an operating lease.

REQUIRED:

(a) Explain what the useful life of the leased asset would be. (3)

(b) Draft the journal entries that will be processed at 30 June 2012 to capitalise the asset and provide for depreciation so as to correct the prior periods. No narrative is needed. (12)

Refer to the attached amortisation table for the calculations to be used in your answer.

Provider		Nashua
Contract Number		PRT25/65/2010
Asset Description		Xerox WCP128Copier
Serial Number		3552296
Location		Budget and Treasury
Date of Contract Commencement		25 Aug 2010
Term of Contract (Months)		36
Monthly Instalment		12 750.00
Escalation per annum		10%
Interest Rate		12.50%
Prime	12.50%	
Margin		
Capital Amount		417 201.68

	Opening balance	Instalment	Present Value of Instalment	Capital portion	Effective Interest Rate	INTEREST PORTION	CLOSING BALANCE	Periods remaining	TOTAL PAYMENTS	Total Loan Repayments	TOTAL INTEREST
Jul-10											
Aug-10	421 778.23	12 750.00	12 644.63	10 790.94	5.57%	1 959.06	410 987.28	36			
Sep-10	410 987.28	12 750.00	10 841 .07	10 668.87	5.57%	1 908.93	400 146.22	35			
Oct-10	400 146.22	12 750.00	12 436. 49	10 891.42	5.57%	1 858.58	389 254.80	34			
Nov-10	389 254.80	12 750.00	12 333.71	10 942.01	5.57%	1 807.99	378 312.79	33			
Dec-10	378 312.79	12 750.00	12 231.78	10 992.83	5.57%	1 757.17	367 319.96	32			
Jan-11	367 319.96	12 750.00	12 130.69	11 043.89	5.57%	1 706.11	356 276.07	31			
Feb-11	356 276.07	12 750.00	12 030.43	11 095.19	5.57%	1 654.81	345 180.88	30			
Mar-11	345 180.88	12 750.00	11 931.01	11 146.72	5.57%	1 603.28	334 034.16	29			
Apr-11	334 034.16	12 750.00	11 832.41	11 198.49	5.57%	1 551.51	322 835.67	28			
May-11	322 835.67	12 750.00	11 734.62	11 250.51	5.57%	1 499.49	311 585.16	27			
Jun-11	311 585.16	12 750.00	11 637.64	11 302.76	5.57%	1 447.24	300 282.4	26	140 250.00	121 495.83	18 754.17
Jul-11	300 282.40	12 750.00	11 541.46	11 355.26	5.57%	1 394.74	288 924.14	25			
Aug-11	288 927.14	14 025.00	12 590.68	10385.55	15.12%	3 639.45	278 541.59	24			
Sep-11	278 541 .59	14 025.00	12 486.63	10 516.37	15.12%	3 508.63	268 025.22	23			
Oct-11	268 025.22	14 025.00	12 383.43	10 648.84	15.12%	3 376.16	257 376.39	22			
Nov-11	257 376.39	14 025.00	12 281.09	10 782.97	15.12%	3 242.03	246 593.41	21			
Dec-11	246 593.41	14 025.00	12 179.59	10 918.80	15.12%	3 106.20	235 674.61	20			
Jan-12	235 674.61	14 025.00	12 078.93	11 056.34	15.12%	2 968.66	224 618.27	19			
Feb-12	224 618.27	14 025.00	11 979.11	11 195.61	15.12%	2 829.39	213 422.66	18			
Mar-12	213 422.66	14 025.00	11 880.11	11 336.63	15.12%	2 688.37	202 086.03	17			
Apr-12	202 086.03	14 025.00	11 781.93	11 479.44	15.12%	2 545.56	190 606.59	16			
May-12	190 606.59	14 025.00	11 684.55	11 624.04	15.12%	2 400.96	178982.56	15			
Jun-12	178 982.56	14 025.00	11 587.99	11 770.46	15.12%	2 254.54	167 212.10	14	167 025.00	133 070.30	33 954.70
Jul-12	167 212.10	14 025.00	11 492.22	11 918.72	15.12%	2 106.28	155 293.38	13			
Aug-12	155 293.38	15 427.50	12 536.97	11 059.02	33.76%	4 368.48	144 234.36	12			

Sep-12	144 234.36	15 427.50	12 433.50	11 370.12	33.76%	4 057.38	132 864.24	11			
Oct-12	132 864.24	15 427.50	12 330.60	11 689.96	33.76%	3 737.54	121 174.28	10			
Nov-12	121 174.28	15 427.50	12 228.69	12 018.81	33.76%	3 408.69	109 155.47	9			
Dec-12	109 155.47	15 427.50	12 127.63	12 356.90	33.76%	3 070.60	96 798.56	8			
Jan-13	96 798.56	15 427.50	12 027.40	12 704.51	33.76%	2 722.99	84 094.05	7			
Feb-13	84 094.05	15 427.50	11 928.00	13 061.89	33.76%	2 365.61	71 032.16	6			
Mar-13	71 032.16	15 427.50	11 829.42	13 429.33	33.76%	1 998.17	57 602.83	5			
Apr-13	57 602.83	15 427.50	11 731.66	13 807.1	33.76%	1 620.40	43 795.73	4			
May-13	43 795.73	15 427.50	11 634.70	14 195.50	33.76%	1 232.00	29 600.22	3			
Jun-13	29 600.22	15 427.50	11 538.55	14 594.83	33.76%	832.67	15 005.39	2	183 727.50	152 206.71	31 520.79
Jul-13	15 005.39	15 427.50	11 443.19	15 005.39	33.76%	422.11	0	1			

QUESTION 2.2 **(15 marks)**

A municipality brings a new land fill site into operation by 30 June 2011. In terms of its licensing conditions, it must rehabilitate the land fill site at the end of its estimated useful life. The estimate of the rehabilitation costs is R1 200 000.

An appropriate discount rate is 5%.

REQUIRED:

(a) Indicate how you would use your financial calculator to calculate the amount of the provision that must be raised and show the journal entry to be passed as at 30 June 2011. (5)

(b) Show what journal entries will be processed for the years ending 30 June 2012, 30 June 2013 and 30 June 2014. (10)

The following amortisation table can be used to support your workings/journals.

Initial		736 695.90
Year 1	36 834.80	773 530.70
Year 2	38 676.53	812 207.23
Year 3	40 610.36	852 817.59
Year 4	42 640.88	895 458.47
Year 5	44 772.92	940 231.39
Year 6	47 011.57	987 242.96
Year 7	49 362.15	1 036 605.11
Year 8	51 830.26	1 088 435.37
Year 9	54 421.77	1 142 857.14
Year 10	57 142.86	1 200 000.00

QUESTION 2.3 **(10 marks)**

REQUIRED:

Indicate whether each of the following statements is true or false. Record the reasons for your answer.

(i) A contingent asset must be included as either a current or a non-current asset in the Statement of Financial Position.

(ii) Conditional government grant, which is received in advance, is revenue and must be recorded as revenue when the grant is received.

(iii) A municipality must only include items that have future economic benefit, in respect of property, plant and equipment, in the fixed asset register. Where an item of property, plant and equipment only has a potential service provision, it must be excluded from the fixed asset register.

(iv) When a municipality sells land, the sale must only be recorded when the title deeds are transferred to the buyer.

(v) There is no need for a municipality to include in its inventory the medicine given to the municipality free of charge by the provincial government as the medicine has no cost. The medicine is stored at a municipal clinic.

QUESTION 3 **(40 marks)**

Waltons Limited was incorporated on 1 April 2006 and has a 31 March financial year end.

The following information on Waltons Limited, for the year ended 31 March 2012, is provided to you:

1 **Land and office building**

The owner-occupied land and office building was acquired on 1 April 2007 and was immediately available for use as intended by management.

The following information regarding the land and office building is provided to you:

		Land	Office building
1 April 2007	Cost	500 000	4 140 000
1 April 2009	Net replacement cost	515 000	3 850 000
1 April 2011	Net replacement cost	538 000	3 300 000

On 1 April 2009, the land and office building were revalued for the first time, by an independent sworn appraiser, who holds an appropriate professional qualification, and who has been doing revaluations like these for the past ten years. The revaluation on 1 April 2009 resulted in a **total** revaluation surplus of R139 000 for the land and office building. On 1 April 2011, the second revaluation was done.

Land and the office building are revalued at net replacement value in terms of the revaluation model in IAS 16, *Property, Plant and Equipment*. They are revalued every two years, at the beginning of the year, unless movements in the market value necessitate earlier revaluation.

Office buildings are depreciated over their estimated useful life of 20 years, using the straight-line method, with no residual value. On revaluation, the accumulated depreciation of the office building is offset against the gross carrying amount.

Any revaluation surplus on the office building realises as the building is used. Any revaluation surplus on land realises on the sale thereof.

2 **Machinery**

2.1 **Second hand machinery** was acquired on 15 April 2009 and was available for use as intended by management on 1 June 2009, but only taken into use on 15 June 2009. The cost of the machinery amounted to R1 470 000. Initial direct costs paid by Waltons Limited on 15 April 2009 amounted to R110 000. The originally estimated residual value was R260 000.

2.2 **New machinery** was acquired from overseas. The new machinery was ordered on 1 June 2011 and shipped free on board on 15 July 2011 from the United States of America. The price of the machinery was R634 260.

The machinery was transported and delivered on 22 August 2011 to the premises of Waltons Limited at a cost of R92 000. Installation costs amounted to R48 000. Initially the machinery could not be used effectively, resulting in an operating loss of R100 000 during the first month. Thereafter the machinery was used profitably.

Management estimated a residual value of R105 000. The machinery was available for use on 30 October 2011 as intended by management.

There had been no indication of impairment of any of the machinery at the end of any of the financial years since acquisition and there were no changes to the useful lives or residual values of any of the machinery.

2.3 Machinery is depreciated on the straight-line method over its estimated useful life of ten years, in accordance with the cost model in IAS 16, *Property, Plant and Equipment*.

3 **Office equipment**

The office equipment was acquired on 1 April 2010 and was immediately available for use as intended by management. The cost of the office equipment amounted to R356 000 and on 1 April 2010 a further R34 000 was paid in cash for delivery and installation.

Office equipment, with a cost price of R125 000, that was purchased as part of the acquisition on 1 April 2010, was sold for R75 000 on 31 October 2011.

Office equipment is depreciated at 25% per annum on the reducing balance method, in accordance with the cost model in IAS 16, *Property, Plant and Equipment*.

The original estimated current residual value of Rnil has remained unchanged.

On 31 March 2012 it was decided to change the depreciation method of the office equipment to the straight-line method over an original total useful life of five years.

4 **Vehicles**

Four similar vehicles were acquired on 1 April 2010 at a total cost of R616 000 from Oasis Asset Finance Limited in terms of a finance lease. Initial direct costs were incurred by Waltons Limited of R44 000, in cash.

The number of kilometers travelled **in total** for all four vehicles was as follows (it is assumed that each vehicle travels the same number of kilometers per annum):

Year ended:	
31 March 2011	63 500km
31 March 2012	71 000km
	134 500km

Vehicles are depreciated using the production unit method, over their estimated useful life of 105 000 kilometers (km) per vehicle, in accordance with the cost model in IAS 16, *Property, Plant and Equipment*.

There had been no indication of impairment at the end of any of the financial years since acquisition of the vehicles.

5 The details of the lease agreement with Oasis Asset Finance Limited are as follows:

- Five lease payments of R146 236 are made annually in arrears on 31 March.
- The lease term is five years.
- Annual interest rate implicit in the agreement is 6%.

6 The following amortisation table is provided to you and you can assume that it is correct:

Date	Payment	Capital	Interest	Balance
01/04/2010				616 000
31/03/2011	146 236	109 276	36 960	506 724
31/03/2012	146 236	115 833	30 403	390 891
31/03/2013	146 236	122 783	23 453	268 108
31/03/2014	146 236	130 150	16 086	137 958
31/03/2015	146 236	137 958	8 278	-

General

7 The estimates of depreciation method, useful life and residual values were reviewed annually and have remained unchanged for all assets, unless otherwise stated.

8 No items were sold during the financial year ended 31 March 2012, unless otherwise stated.

REQUIRED:

(a) Prepare the journal entries for the capitalised leased liability, excluding taxation journals, of Waltons Limited for the year ended 31 March 2012, in accordance with International Financial Reporting Standards. (5)

(b) Prepare the Property, Plant and Equipment and Capitalised lease liability notes to the Statement of Financial Position of Waltons Limited for the year ended 31 March 2012, in accordance with International Financial Reporting Standards. (29)

(Only the columns for the Office building, Office equipment and Machinery are required for the Property, plant and equipment note.)

(c) Prepare the Profit before tax note to the Statement of profit or loss and other comprehensive income of Waltons Limited for the year ended 31 March 2012, in accordance with International Financial Reporting Standards. (6)

Round all final amounts to the nearest R1.
No accounting policy notes are required.
No comparative figures are required.
No total columns are required.