



The Southern African Institute of Government Auditors

Qualifying Examination for Registered Government Auditors

Paper 2: Accounting

November 2016

INSTRUCTIONS TO CANDIDATES

- 1 Maximum marks: **160**.
- 2 Total time available: **four hours**.
- 3 **Q1=80 marks, Q2 80 marks**
- 4 **Start each question in a new Exam Book (Green)**
- 5 The marks allocated to each question are an indication of the expected length and required depth of the answer.
- 6 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.
- 7 Present your arguments clearly, using well structured, clear and precise language and appropriate professional terms.
- 8 No books or notes are allowed in the examination room.
- 9 All working papers must be handed in together with all paper provided for the examination (including unused answer sheets).
- 10 Answers written in pencil will not be marked.
- 11 Total number of pages for this question paper is 9

Question 1

80 MARKS

Section A

The Department of Roads is responsible for facilitating, coordinating and enabling the movement of goods and people, underpinned by adequately maintained infrastructure and efficient services and operations aimed at advancing South Africa's social and economic development.

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

- 1 Possible fruitless and wasteful expenditure is expected with regard to the acquisition of a software application in 2014. The purchase amount was R15 700. No transaction has been recorded. The case is still under investigation.
- 2 A contractor presented the department with information regarding tender irregularities on a 2015/16 tender to the amount of R328 760. No transaction has been recorded. The case is still under investigation.
- 3 Movement in the unauthorised expenditure account for the 2015/16 financial year comprised of the following: Unauthorised expenditure for the current year was R150 000. Unauthorised expenditure from a previous year approved with funding was R18 678. Unauthorised expenditure from a previous year (Catering) approved without funding was R42 785. Unauthorised expenditure not approved and transferred to Receivables for recovery was R10 800.
- 4 **Find the trial balance of the department as Attachment 1**

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

- a) A Statement of Financial Performance for the Department of Roads for the year ending 31 March 2016 .
(12)
- b) A Statement of Financial Position for the Department of Roads on 31 March 2016.
(8)
- c) Compile a Cash Flow Statement for the Department of Roads on 31 March 2016.
(14)
- d) Show the following notes to the financial statements:
(22)
 - i Unauthorised expenditure
 - 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 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 marks)**

- i Exchequer Grant Account
- ii Revenue Accrual Account

(Total 65 MARKS)

Section B

The primary focus of the South African government is service delivery and the fulfilment of institutional mandates of departments. Annual appropriations received by departments, serve as the primary funding for the fulfilment of the service delivery obligations of departments. The performance of departments is therefore informed by the extent to which their service delivery obligations are executed and the manner in which their appropriations are utilised in the fulfilment of their objectives.

Required:

Explain by means of a memo to your trainee auditors the objective, format and content of the Appropriation Statement.

(15 MARKS)

Attachment 1: Trial balance for the Department of Roads on 31 March 2016

Description	2015/16	2014/15
	R	R
General Account of the Vote	(150,906,540)	(143,982,541)
Motor vehicle licences	(6,589,700)	(5,792,015)
Sale of capital equipment	(9,982,654)	(3,658,735)
Interest received	(56,987)	(48,563)
Toll gate collections	(71,563,598)	(69,521,463)
Current transfer payment - Roads inspection	3,259,854	3,896,541
Capital transfer payment - Roads development	2,587,621	2,547,364
Travel and subsistence cost	1,135,689	1,056,842
Catering	685,681	589,341
Operating leases	692,574	521,639
Interest paid	25,891	18,627
Stationary and printing	469,821	389,542
Assets less than R5000	895,241	658,412
Machinery and equipment (Capital)	5,800,652	4,476,217
Rent on land	258,412	240,145
Application software (Capital)	156,000	145,890
Information Technology services	25,986	28,641
External auditing fees	89,254	78,469
Authorised losses	25,872	20,698
General Account of Revenue	80,000,000	70,000,000
Basic salaries	67,907,943	64,792,143
Medical aid contribution	6,790,794	6,479,214
Pension fund contribution	10,186,191	9,718,822
Housing subsidy	1,358,159	1,295,843
Employee relocation expenses	172,584	158,961
Employee severance pay expenditure	1,198,542	800,952
Paymaster General Account	52,690,432	57,142,117
Uncleared deposit account	189,524	152,895
Petty cash	80,000	80,000
Debtor account	49,692	27,895
Subsistence and travel advances	185,467	165,427
Unauthorised expenditure	336,712	258,975
Cheques payable	(258,952)	(241,897)
Unallocated receipt control account	(128,965)	(785,652)
Bank adjustment account	56,487	(2,471)
EFT payment account	(256,987)	(65,897)
Salary deductions control account	(2,875,124)	(1,642,378)
Recoverable Revenue	(10,997)	
Exchequer grant account	5,319,428	
	(0)	0

Please note: Except where expressly stated you can ignore the implications of VAT in your answers to the questions listed below. YOU MUST IN EACH ANSWER PLEASE SHOW ANY CALCULATIONS VERY CLEARLY.

Question 2

(80 MARKS)

After years of hard work and dedication you have recently been promoted to a senior manager position in the Audit Research and Development (**ARD**) division at the Auditor General (SA) head office in Tshwane / Pretoria. You are determined to make an impression quite early after joining the unit.

Your first day at the office is 1st of October 2016. Upon opening your email at 08:00 you receive a rather urgent email from an AGSA audit team based in Mpumalanga who is busy auditing Ubuntu Municipality. Below follows an extract of the email which has then been divided into further subsections pertaining to each technical query.



From: Rudolf.Ralefe@agsa.gov.za

To: Herbert.Mojalefa@ard.agsa.gov.za

Date: 1 October 2016

Subject: Assistance with technical queries please

Dear Herbert,

By way of introduction my name is Rudolf and I am the team supervisor managing the audit for client Ubuntu Municipality. The background of the client is such that CFO resigned in April 2016 with the managers of revenue and expenditure as well as the acting CFO working on their own accord without the guidance of a senior CFO. There are thus a number of technical issues I urgently need your assistance with please as these are all likely to result in audit adjustments being proposed to the client. The audit manager who I report to for this engagement has been ill for a week and thus need your prompt assistance.

Ubuntu Municipality is considering utilising ASB Directive 11 due to an inappropriate accounting policy choice regarding the subsequent valuation model relating to Investment Property – we need guidance on the implication of Directive 11 please, see further down below.

For ease of reference I have broken down my queries into subsections below:

QUERY 1

(20 MARKS)

I have just received the valuation from the service provider (Environmental Impact Assessor) which indicates the total environmental rehabilitation cost expected to be incurred upon closure of the municipal landfill site at the end of **20 years**.

The best estimate per the valuation report of the cost for rehabilitation of the section of the landfill site where waste dumping has already taken place at the end of 20 years is **R20, 000,000**. After analysing the report in taking the risks associated with landfill site into account it is appropriate to discount the environmental cost at a rate **9%**, which gives rise to a discounted value ("Present Value") of R3, 568,617.80 at 1 July 2015.

It is my understanding that GRAP 17, GRAP 19 and IGRAP 2 may be applicable.

Please assist me with the following as the acting CFO omitted to process these journals during the financial year:

A. All required initial recognition journal entries to be processed on 1 July 2015 as well as subsequent measurement and unwinding of discount entries for the year ending 30 June 2016. Please indicate your calculations clearly.

(13 marks)

B. Provide the recommended disclosure (on a high level) required in the **notes** to the annual financial statements (excluding accounting policies and also excluding a narrative description of the environmental rehabilitation provision).

(7 marks)

QUERY 2

(24 MARKS)

Whilst walking down the corridor in the mornings on route to the council chamber (where the audit team is based) I have noticed a very expensive looking photocopy and scanning machine. I am anticipating that this photocopier is being leased by the municipality as lessee and that GRAP 13 Leases may apply.

Upon further enquiry from the acting CFO I have been able to ascertain the following:

- A copy of the lease agreement was obtained. A three year (36 month lease) was entered into on the 1st of July 2015. The monthly rental fee per the lease agreement (exclusive of consumables such as ink and paper) is R3000 (excluding VAT) and made at **month end**.
- The economic life of similar photocopiers is four years.
- If the municipality had decided to purchase such a photocopier outright in cash then fair value of a similar photocopier would have amounted to R100,000.

- For purposes of performing the present value of minimum lease payments calculation a discount rate of 9% per annum is deemed appropriate.
 - There is a purchase option clause in the lease which would enable Ubuntu Municipality to purchase the photocopier at a value seemingly lower than the fair value at the date the option becomes exercisable. At the inception of the lease there was uncertainty as to whether Ubuntu municipality will exercise such an option.
 - During the year the manager of expenditure booked the debit leg of the journal entry to the "rental expense vote – performance statement/ expenses" each time the R3, 000.00 payment was made. Had the manager expenditure accounted for this lease as a finance lease, the interest expense related to the first year of this lease would have been R7, 327.00
 - The financial year end applicable is again 30 June 2016.
- A. Please assist in advising whether the lease would be classified as a finance lease or operating lease. For audit documentation purposes please assess the lease info above against the requirements of GRAP 13 in making such a determination, clearly stating all of the requirements/ classification criteria of GRAP 13 considered. **(10 marks)**
- B. Please provide assistance in providing me with the initial recognition journals at 1 July 2015 as well as the required journals to be processed at 30 June 2016. **(14 marks)**

QUERY 3

(8 MARKS)

My team member who has been assigned grants revenue and unspent conditional grant audit section brought the following technical query to me which I require your assistance with please:

The manager of revenue only records the equitable share grant revenue upon receipt of each tranche which occurred in July 2015, December 2015 and March 2016. The total equitable share grant for Ubuntu Municipality amounts to R90,000,000 with the manager of revenue only recording R30,000,000.00 of revenue each time a tranche / transfer was received.

In addition to the above the manager of revenue recognised R25,000,000.00 of revenue relating to the municipal infrastructure grant (MIG) when the funds were received in Ubuntu Municipality's bank account. There are however stipulations relating to this grant as contained in the correspondence/ contract between the municipality and the MIG which states that any funds not used for purposes of the transfer must be returned at year end to the MIG, unless "rolled over" by way of an approved adjustments budget - at year end R7, 000,000.00 of this grant remained unspent but have been committed by way of an approved MBRR Schedule B adjustments budget.

- A. Taking **GRAP 23** and the Division of Revenue Act (**DORA**) into account please explain if the manager of revenue appropriately accounted for the revenue. If revenue was accounted for incorrectly then please state when and which

amount the equitable share grant should have been recognised.

(

3 marks)

- B. Please provide the correcting entry as at 30 June 2016 in order to appropriately account for the MIG revenue and any related liability. Also briefly justify the necessity of such a journal. **(5 marks)**

QUERY 4

(15 MARKS)

The Ubuntu municipal building in which all the municipality's employees work from was damaged on the 1st of June when a mild earthquake caused by a nearby mine resulted in structural damage to the building. Shortly after on the 15th of June violent protests by residents (due to perceived lack of service delivery) caused further damage to the building.

The acting CFO is aware that GRAP 21 is applicable and that an impairment adjustment should be made to the municipal building. No adjustments were made by 31 August 2016.

During the performance of audit procedures, I have been able to ascertain the following:

- The office building was built at a cost of R30 million and construction was completed on 1 July 1995 – at this dated the building was commissioned from Work-in-progress to an Active Asset. Upon initial recognition the building was expected to provide future economic benefits for 50 years.
 - The replacement cost of a similar new municipal building is R70 million.
 - In order to restore the municipal building to a condition whereby municipal employees can occupy the building again repairs amounting to R25.5 million is required.
- A. From a technical point of view please assist in calculating the recoverable service amount of the building as well as the resulting impairment charge that needs to be recognised as at 30 June 2016.

(12 marks)

- B. Propose the adjusting journal (together with journal narration) for purposes of communicating the audit adjustment to the client.

(3 marks)

QUERY 5

(7 MARKS)

Whilst performing audit procedures in relation to GRAP 12 Inventory the following was noted during the verification of consumable stores.

- A line item called "adaptors – FP 25" was found in the stock listing being carried a cost of R999 per unit.
- After obtaining a quote from the hardware store (which is adjacent to the municipal office) it was found that the item sells for **only R14, 50** per unit.
- At year end 283 adaptors were counted during the consumables stores inventory count.

A. Please assist in calculating the value of the net realisable value adjustment showing your calculations for purposes of audit file documentation.

(4 MARKS)

B. Propose the adjusting journal for the NRV adjustment to be communicated to the acting CFO.

(3 MARKS)

QUERY 6

[6 MARKS]

The acting CFO recently brought up *Directive 11 – Change in measurement bases following the initial adoption of Standards of GRAP*.

A. As team supervisor it is required to be technically be up to date on this. Please assist in providing a synopsis as to what Directive 11 enables a municipality to achieve so that the appropriate conversation can be held with the Acting CFO in the event that the municipality wants to change its measurement basis on any of the allowed classes of assets.

(6 marks)

END OF PAPER