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## AGA Examination 3: Governmental Financial Management and Control (GFMC) Sample Questions (Q101-Q106):

### NEW QUESTION # 101

Given the information below, which control would be the lowest priority?

Asset \$Amount at Risk Cost of Control

- A. Asset B \$6,000 \$ 2,500
- B. Asset C \$2,000,000 \$50,000
- C. Asset D \$500,000 \$20,000
- D. AssetA \$ 150,000 \$15,000

**Answer: A**

Explanation:

How to Prioritize Controls Based on Cost and Risk:

\* The priority of a control is based on its cost-effectiveness. Controls that protect assets with higher risk exposure relative to the cost of the control should be prioritized. The formula to calculate cost-effectiveness is:  $\text{Cost-Effectiveness} = \frac{\text{Cost of Control}}{\text{Asset Amount at Risk}}$

\* Lower ratios indicate more cost-effective controls.

Calculations:

\* Asset A:  $\$15,000 / \$150,000 = 0.10$  (10%)

\* Asset B:  $\$2,500 / \$6,000 = 0.42$  (42%)

\* Asset C:  $\$50,000 / \$2,000,000 = 0.025$  (2.5%)

\* Asset D:  $\$20,000 / \$500,000 = 0.04$  (4%)

Lowest Priority:

\* Asset B has the highest ratio (42%), meaning it is the least cost-effective and should be the lowest priority for controls.

References and Documents:

\* COSO Internal Control Framework: Discusses cost-benefit analysis for prioritizing controls.

\* GAO Risk Management Guide: Emphasizes evaluating control cost-effectiveness relative to asset risk.

### NEW QUESTION # 102

Management segregates duties among staff in order to reduce the risk of fraud

- A. rationalization.
- B. pressure.
- C. detection.
- D. opportunity.

**Answer: D**

Explanation:

Segregation of Duties and the Fraud Triangle:

\* The Fraud Triangle identifies three conditions that contribute to fraud: pressure, opportunity, and rationalization.

\* Segregating duties (e.g., separating authorization, recordkeeping, and asset custody) is specifically designed to reduce opportunity, which is the chance for an employee to commit fraud without detection.

Why Opportunity Is Key:

\* If one person has too much control over a process, they may exploit it for personal gain. Segregating duties creates checks and balances, making it harder for fraudulent activities to go unnoticed.

Why Other Options Are Incorrect:

\* A. Pressure: Pressure refers to personal or financial stresses that drive someone to commit fraud, but segregation of duties does not address this directly.

\* C. Rationalization: Rationalization involves justifying fraudulent behavior, which segregation does not prevent.

\* D. Detection: While segregation can aid in fraud detection, its primary role is to reduce opportunities for fraud.

References and Documents:

- \* GAO Standards for Internal Control (Green Book):Emphasizes segregation of duties as a control to mitigate opportunities for fraud.
- \* COSO Internal Control Framework:Identifies segregation of duties as a key tool to reduce fraud risk.

### NEW QUESTION # 103

When creditworthiness is a criterion for government loan approval, loan applicants must provide

- A. a promise to pay interest at the government borrowing rate.
- B. a credit rating from a major bank.
- C. a satisfactory history of repaying debt.
- D. sufficient capitalization.

**Answer: C**

Explanation:

Creditworthiness and Loan Approval:

\* When creditworthiness is a criterion for government loans, the applicant must demonstrate a satisfactory history of repaying debt, as this reflects their ability to fulfill repayment obligations in the future.

Why a Satisfactory History Is Required:

\* Past repayment behavior is considered the best indicator of future performance. Government agencies prioritize reducing the risk of defaults by ensuring applicants have a proven history of managing debt responsibly.

Why Other Options Are Incorrect:

\* A. A credit rating from a major bank:While a credit rating is helpful, it is not typically required for government loans. Instead, creditworthiness is evaluated based on repayment history and other financial factors.

\* C. Sufficient capitalization:This is important for business loans, but it does not address creditworthiness.

\* D. A promise to pay interest at the government borrowing rate:A promise is not sufficient to establish creditworthiness.

References and Documents:

\* OMB Circular A-129:Requires agencies to assess creditworthiness before granting loans.

\* GAO Loan Management Guide:Highlights repayment history as a key criterion for loan approval.

### NEW QUESTION # 104

A material weakness in internal control over financial reporting is defined as a deficiency that

- A. results in a misstatement to the basic financial statements.
- B. creates a reasonable possibility of a material misstatement to the financial statements that will not be detected in a timely manner.
- C. did not allow management to perform their assigned responsibility to prevent, detect and correct misstatements in a timely manner.
- D. results in a material misstatement in other accompanying financial information.

**Answer: B**

Explanation:

Definition of a Material Weakness:

According to auditing standards, a material weakness in internal control over financial reporting is a deficiency or combination of deficiencies that creates a reasonable possibility of a material misstatement in the financial statements that will not be prevented or detected on a timely basis.

Key Characteristics of a Material Weakness:

\* Reasonable Possibility:The likelihood of a misstatement is more than remote but less than certain.

\* Material Misstatement:The error or omission could impact the decisions of users relying on the financial statements.

\* Timely Detection:The deficiency allows errors to go undetected for an extended period, potentially affecting financial statement reliability.

Why Other Options Are Incorrect:

\* A.A misstatement in the basic financial statements may result from a material weakness, but the definition focuses on the reasonable possibility, not the actual result.

\* B.A material weakness impacts the financial statements, not "other accompanying financial information."

\* C.While timely detection is part of the issue, the definition focuses on the reasonable possibility of a misstatement, not management's inability to perform specific duties.

References and Documents:

- \* GAAS (AICPA SAS No. 115): Provides the formal definition of material weaknesses and guidance for auditors in evaluating control deficiencies.
- \* COSO Framework: Emphasizes the need for effective internal controls to mitigate material misstatement risks.

### NEW QUESTION # 105

Government entity SEA reporting provides users of general purpose financial reports with an

- **A. evaluation of the efficiency and effectiveness of governmental programs.**
- B. assessment of financial condition and results of operations.
- C. assessment of the accountability of the public administrators.
- D. evaluation of the effects of changes in public policy.

**Answer: A**

Explanation:

\* Service Efforts and Accomplishments (SEA) Reporting:

\* SEA reporting is designed to provide non-financial performance information about the efficiency and effectiveness of government programs.

\* It evaluates how well resources are being used to achieve desired outcomes, helping stakeholders assess program performance and accountability.

\* Explanation of Answer Choices:

\* A. Evaluation of the effects of changes in public policy: Incorrect. SEA reporting does not focus on policy changes but on program performance.

\* B. Assessment of financial condition and results of operations: Incorrect. This is the role of financial statements, not SEA reports.

\* C. Assessment of the accountability of the public administrators: Incorrect. While SEA reports indirectly support accountability, their main purpose is to assess program efficiency and effectiveness.

\* D. Evaluation of the efficiency and effectiveness of governmental programs: Correct. This is the primary focus of SEA reporting.

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GASB, Concepts Statement No. 2: Service Efforts and Accomplishments Reporting.

GFOA, Performance Reporting in Government.

### NEW QUESTION # 106

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