

THE INSTITUTE OF CHARTERED ACCOUNTANTS OF SRI LANKA

Financial Reporting Framework – June 2012

The paper was well balanced in style and content thus consolidating the testing methods that could be expected in the future. Many candidates may have encountered a surprise within the examination hall as the first question referred to IFRICs that are normally available only in the international edition of IFRS. Yet, candidates should have been taught where to refer when they have doubts or problems in applying accounting standards. Question No. 8 required the candidates to think beyond the general provisions available in the standard on agriculture, more specifically to identify a biological asset for reporting purposes. The paper included fair amount of calculations and double entry book-keeping too. A major deviation from the previous papers was the question No. 2 which allowed candidates to debate the issue in free-style.

Given the above composition of the paper candidates prepared with different approaches to tackling the paper should have been able to secure a substantial score.

Examiners have observed a performance improvement for all questions. But, many candidates who did very well in some questions failed to secure an adequate score in other questions in order to reach the pass-mark level.

Examiners had to face the problem of reading illegible handwriting. Many candidates had faced with the problem of poor language skills. Other deficiencies were poor presentation and answers presented in short form without any clue as to how it could be related to the question given.

Question No. 01

Part (a)

The entire question was on leases. Candidates should have studied this in depth at CAB II level. However, except for very few candidates, others were not aware of existence of IFRICs. So the candidates had discussed leases in general. IFRICs cover matters not included in the body of the standard. So the marks earned by candidates for the part (a) were very poor.

Part (b)

Except for the valuation aspects, the question required only the knowledge gained at CAB II level. Some candidates had been confused over who the lessee was. It was up to the candidate to select a suitable accounting period for their answers. Many had covered the entire lease period. Majority of the candidates were able to earn substantial marks for this part.

Question No. 02

It was quite evident that the candidates were very familiar with the subject matter covered in this question though it covered several accounting standards. Candidates had the freedom to comment on any aspect. But many failed to identify which accounting treatment was correct and permitted by the accounting standard.

Many candidates appeared to be unaware of the fact that members (individual companies) of a group could have accounting policies that were different from group policies.

Many candidates had discussed the relevant points but the explanations given for treatments in Consolidated Statement of Comprehensive Income were inappropriate suggesting that they did not have a thorough understanding of reporting framework.

Still others had discussed the related party aspects.

However, marks earned by the majority were less than 50% of the marks allocated for the question.

Question No. 03

Part (a)

This question required candidates to show ledger accounts. Alternatively, a smart candidate could have explained that step by step with proper calculations. Since it involved some calculations, many could earn some marks by doing the calculations even though they were not sure of the exact format of the answer.

It appeared that many candidates had not read the question carefully. They failed to identify the value applicable to the points in time scale. This was evident by calculating either a present value or a future value of the given figure of Rs. 1.2 million dismantling cost. When the starting point is wrong, further calculation such as interest will naturally be wrong.

Some candidates had erroneously written off dismantling cost to the Profit and Loss Account.

Overall, majority of the candidates failed to answer this part of the question correctly.

Part (b)

This part of the question was very easy. It required only calculation of depreciation. This part carried five marks which could have been earned within less than two minutes.

Candidates knew how to calculate depreciation by dividing by the number of years. What they did not know was whether to deduct residual value or fair value. This caused marks earned by candidates to be substantially low.

Question No. 04

Part (a)

This part was from an accounting standard which had been tested repeatedly during the previous examination sessions, namely financial instruments. However, it required a very short precise answer. Accounting Standard on /Financial Instruments have been widely discussed. A plenty of papers on the subject is available in the internet.

Almost all candidates had been ready for this type of question. But major deficiency was that many candidates had indicated examples for financial instruments in place of “types”.

Part (b)

This part of the question on the same accounting standard was straightforward and easy. Yet many candidates were skeptical about this asset.

Overall this was a poorly answered question.

Question No. 05

Part (a)

This part of the question required the candidate to identify the time for making the provision among other things. Question was somewhat lengthy. It had to be read several times to identify what were exactly required of this question. Other than this timing aspect, candidates had no difficulty in answering this question. Majority earned substantial marks for this part of the question.

Part (b)

Exact answer to this part is given in the relevant accounting standard. Those who had read that would have no difficulty. Those who were not ready like that could have answered without difficulty by applying their knowledge. However, question required the candidates to write a note to be included with the Financial Statements (in the annual report). It has to be short and precise. However, candidates had written several notes in place of one which is not normally considered as suitable for inclusion in the annual report.

As a result, majority of the candidates were not able to earn sufficient marks for this part of the question.

Question No. 06

Part (a)

This part of the question required the candidates to write what was specifically stated in the related accounting standard (SLFRS – 2). Only very few candidates were able to present their answers in that manner.

A fair number of candidates had attempted to justify their answers by discussing matters relevant to share based payments.

This part of the question was not answered well.

Part (b)

This part of the question required candidates to produce a yes/no type answer. The subject matter of the question had been debated and reached consensus on what it should be. But the legal aspects are somewhat different.

So the candidates were on a win or lose situation. A reasonable number of candidates failed to obtain the allocated marks.

Question No. 07

Part (a)

This part of the question required the candidates to assess the impact of the transaction carried out on the cut-off date for preparing Financial Statements.

The other aspect was the forward contract, which the company could have sold. The time span of the series of transactions was around 03 months. So the candidates had to evaluate overall impact and comment on its impact.

The easiest way to answer was to show ledger accounts. A narrative answer was also required to discuss the impact and ways to correct the same.

Many candidates had attempted this question partially. As a result, marks earned by candidates were less than 50% allocated for this part of the question

Part (b)

This part of the question required an answer in point form. It tested candidates' knowledge of fair value model of accounting. Impairment is an integral part of the fair value model that requires fair values to be adjusted when there is a downward movement of value.

Candidates had answered this part of the question fairly well.

Question No. 08

Part (a)

Part (a) of the question could have been answered with the knowledge gained at the CAB II level. Accordingly candidates had answered this part very well.

Part (b)

It was somewhat difficult to ascertain the exact form of the answer required. But the subject matter could easily be related to the recently introduced accounting standard on agriculture.

The question had to be analysed in the manner indicated below.

- a) Whether the teak trees could be treated as biological assets?
- b) Whether the teak trees could be accounted separately even if it satisfies the requirements for biological assets?

Candidates had successfully presented requirements for treating an item as a biological asset. But they were not able to comment on the issue of accounting for the same.

So the candidates were not able to earn marks for this part of the question satisfactorily.

Question No. 09

Part (a)

This part was straight forward. There was large number of items listed in the standard as answer to this question. Candidates were not expected to list all of them.

So candidates could easily earn good marks for this part.

Part (b)

Anybody who had prepared a set of Consolidated Financial Statements could easily answer this part. Some candidates had shown journal entries and methods for calculating items to be shown in the Consolidated Statement of Financial Position.

Candidates had done fairly well in this part too. But many failed to indicate the proper order.

Question No. 10

Parts (a) & (b)

These two parts were straight forward and easy to answer. The relevant points could have been gathered from the website of the SEC. Some candidates were not sure of the 25% requirement – whether it is number of shares or the number of shareholders

Part (c)

Attention of the candidates had been drawn to the law, governing the implementation of accounting and auditing standards of the country.

Many had attempted this part successfully. But some candidates had attempted to add creative features which were not in the law.

However, candidates scored well for the question as a whole.

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Strategic Management Accounting – June 2012

Question No. 01

Though majority of the candidates were able to score fairly, only few were able to satisfactorily answer all parts of the question.

Part (i) Majority of the candidates failed to take into account the tax savings on rental income. Some had taken the rental income foregone (opportunity cost) as a cash inflow. Instead of deducting depreciation from cost of sales some had added depreciation. Some had calculated the accounting depreciation of machinery by deducting the scrap value of the machinery from the cost. However, the question specifically states that depreciation is 20% of the cost. Many had failed to take into account the tax payable on the resale value of the machinery.

Part (ii) Some of the candidates had answered assuming that the projects are not divisible, even though the question specifically stated that the investments were divisible. Some had applied incorrect formulae in calculating the profitability index.

Part (iii) Following deficiencies were observed in respect of the formulation of the linear programme.

- (i) Variables A,B,C were not defined or incorrectly defined as the amount invested in the projects A,B,C
- (ii) Taking into consideration all 4 projects.
- (iii) Failure to include the non-negativity ($0 \leq$) constraint together with the proportion constraint (≤ 1)
- (iv) Maximising profitability indexes instead of individual NPV's. Some had interpreted the proportion of each project in the simplex tableau as the investment amount in Rs. millions.

Full interpretation of the simplex tableau was not done and some had just stated 0.45, 20.11, 12.00 as shadow prices without explaining their significance/meaning.

Only a few were able to state the limitation of (use of) LP in capital rationing problems. Most of the candidates had instead merely stated the complexity of the problem.

Question No. 02

This question was satisfactorily answered by the majority of the candidates. Only a few got Part (a) wrong mainly by not following the sequence of the events properly and also introducing unnecessary dummy activities. Many had the standard deviation incorrect due to using incorrect formula (i.e.) adding the standard deviations of the critical activities instead of adding the variances and obtaining the square root.

Parts (c) & (d)-Many candidates had read the probability off the normal curve incorrectly. Some had given as the answer the probability read off the normal curve without adding 0.5 probability. Some had failed to interpret the probability calculated in part (d) properly and had arrived at the wrong decision. Few had attempted 95% confidence level approach to work out the part (d) of the question which is not applicable in the given situation.

Many did not know what was meant by completed within 14 days. Candidate had misinterpreted it as 'in 14 days' and had worked out the probability of completing in exactly 14 days.

Instead of commenting on disadvantages some had commented on advantages.

Question No. 03

Part (i) Budget Slack was not accurately explained by many candidates. Some had identified it as the unutilized resources. Some as the excess of budget over actual. Only a few had correctly explained it to be the gap between the required and the budgeted.

Budget limitation factor – only few could give the precise explanation (i.e), the factor that restricts the performance for a given period.

Part (ii) Only a few candidates were able to explain the difference between fixed and flexible budgets correctly. (i.e.) fixed budget is prepared for a given level of output or activity whereas a flexible budget is based on actual output or activity. Many had stated the advantages and disadvantages of budgetary control in general and not specifically to fixed, flexible budget

Part (iii) Definitions of ABB given by some of the candidates were not accurate. They had not mentioned that it is based on activity framework and utilized cost driver data in budget setting and variance feedback process. Specific advantages and disadvantages applicable to ABB were not given.

Part (iv) This part of the question requires drawing up of a simple working capital budget. However, many candidates could not even state the components of the working capital, which is unacceptable at this level.

Question No. 04

Parts (i) and (ii) respectively requires determining the optimum output level when company as a whole is considered and division R only is considered. Many candidates had tried to work out the optimum output level by using $MR = MC$ approach for determining the profit maximization level. Candidates need to appreciate that in the given problem a linear relationship cannot be assumed between price and output and therefore $MR = MC$ approach cannot be applied, (i.e.) demand changes only at the stated price levels.

Many had used incorrect variable cost per unit as they had used incorrect cost components for given situations. Many had calculated net profit per unit by including the absorbed fixed cost per unit and had thereby calculated net profit at different demand levels not realising that by doing so they have made fixed cost a variable cost.

Some had taken the total fixed costs also into their calculations but had made different estimates for fixed cost at different demand levels displaying their lack of grounding in the basic principles of cost accounting. Part 5 of the question was fairly answered.

Question No.05

This question was poorly attempted by most of the candidates. Many had a difficulty in identifying the six alternate options available to the management. Many had failed to consider different forecast sales volumes under each option as separate outcomes and instead had calculated the expected sales volume under each option and had proceeded to calculate the expected net profit.

This approach is inaccurate as it does not recognize profit/(loss) on raw material sale under each outcome. Some had failed to take the increased fixed cost into their calculation of net profit and also the packaging cost in calculating the loss on sale of raw material.

Answers to the part 2(b) of the question were poor in quality with only a few candidates could identify the worst outcome in terms of net loss to be minimum (in option 2) i.e. the maximum of the worst outcomes under each option.

Question No. 06

This question was about quality control in a JIT inventory control environment. With a significant number of candidates not attempting the question, it is apparent that candidates have not dealt with a problem of this nature in their classroom/studies. However, few candidates had successfully attempted the question and had scored high marks.

Part (i) The candidates were required to reconcile the quantity invoiced with quantity manufactured. Many had erroneously taken the free replacements as unplanned replacements while some had calculated the unplanned replacements correctly but had failed to treat the gain as a negative figure in the reconciliation. Many had failed to appreciate that the unplanned loss/(gain) in manufacturing defects was the balancing figure. Some had failed to follow the prescribed format given in the question.

Part (ii) Many candidates could not interpret the results of part (i) correctly (i.e.) candidates could not appreciate that unplanned defects and replacements reflecting gains means that there was a quality improvement.

Some had tried to compare the February results with that of March by comparing the absolute figures rather than the percentages, probably due to their poor mathematical skills.

Part (iii) In calculating gross savings some had taken only the reduction in manufacturing defects (i.e.) They had not taken the reduction in customer replacement into account.

Some had tried the total cost approach without working out under two scenarios (i.e.) with and without quality control. They had merely compared the total cost per unit for February with that of March. This did not allow them to comment on the quality control under the new system.

Part (iv) Candidates were required to state two matters the management might consider in light of the answers given in part (iii) (b) of the question (i.e.) whether the cost incurred on the new system for each month is justifiable. However, candidates have not based their answers according to their answer to part (iii) (b) and had made some general considerations.

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Strategic Management Process – June 2012

Overall performance of the candidates was satisfactory. Nevertheless, common mistakes/ omissions committed by candidates for each part of the five questions are given below.

Question No. 01 – Case Study – Allocated Marks (AM)-30, Average Performance (AP)-15

(a) Profit Maximization (PM) – AM – 04, AP-03

Some candidates had given examples of shortcomings of profit maximization rather than generalizing shortcomings of profit maximization. Eg: “No benefits are given to the employees by the employer”, “No society welfare is considered”, for which only a few marks were conceded.

Some students had not elaborated the shortcomings for them to earn full marks.

Eg: “Lack of focus”, “Lack of great ideas”.

Most of the students ignored the important factors like “Short-term Orientation”. Nevertheless they have mentioned the outcome or bad effects arisen out of lack of long term orientations, for which some marks were given.

A very few candidates stated “Cost of production, Cost of acquiring new technology” etc. are shortcomings of profit maximization for which no marks were given.

(b) Interferences of PM from the given case – AM-02, AP-01

Most of the candidates had drawn inferences from the case to highlight limitations of profit maximization. However a few had cited inappropriate sentences and paragraphs of the given case to highlight the limitations.

(ii) Competitive Advantage AM-05, AP-02

Only a few candidates had mentioned that “Competitive Superiority among its customers” to be gained to have competitive advantage. They instead mentioned that competitive advantage is the advantage of a Company over its competitors without being elaborated.

Most of the candidates ignored the fact that most of the customers buy on value, that means, customer is to be provided with better benefits or lesser cost or a combination of both for anyone to ensure competitive advantage.

(iii) Core Competencies AM-07, AP -03

The term core competencies had not properly explained by most of the candidates. They just mentioned that core competencies critically underpin the Company’s competitive advantage for which only a few marks were granted.

Only a few candidates stated that core competencies is difficult to imitate since it makes a significant contribution to the customer benefits in providing customer value.

(iv) Organization Culture AM-08, AP-05

Most of the candidates had not stated the accepted definition for Organization culture i.e. “Deep rooted values and benefits that govern and shape behavioral patterns and norms or standards.

Some just mentioned that Organizational culture is practices, ethics, beliefs etc. for which only a few marks were given.

Some had cited inappropriate evidence of culture in relation to the given case, i.e. “People at HP began to believe that the culture, the practices, the traditions themselves were sacred” Just because the word “culture” is there in any sentence or paragraph, some candidates seemed citing them as evidence in this regard.

(v) Organization Culture & Strategy Implementation – AM-04, AP-01

Most of the candidates had not arrived at a conclusion that culture was the key building block in implementing strategy which the examiner expected from the candidates.

Candidates should have cited “operating practices, cultural norms, strategies tactics, processes, structures and methods in response to changing realities, lose your core values and you lose your soul; refuse to change your practices” which were not cited by most of the candidates.

Question No. 02 – National Diamond Framework – AM-18, AP-13

(i) Components of National Diamond Framework AM-05, AP-04

Some had not correctly worded the components. E.g. “Firm strategy, structure & rivalry” component was worded by some without “rivalry”.

Arrows showing inter-relationship among components were not correctly drawn by some candidates.

Some have not drawn arrows at all or any other form of relationship among the components.

(ii) Items included in each component – AM-08, AP-06

Some candidates had just mentioned “raw materials, labour, capital” under factor conditions rather than their “availability” being stated.

Some stated only basic categorizations of components. Eg. Basic factors” and “Advanced factors” for factor conditions.

Some ignored to write “market share” or size under demand condition instead they have mentioned “market growth” which was not alone helpful to assess the degree of global competitiveness.

(iii) Application of Diamond Concept – AM-05, AP-03

Some of the candidates who had selected readymade garment industry in answering this part, mentioned only availability of “cheap labour” to assess the international competitiveness. They have ignored the fact that Sri Lankan labour is relatively educated and trainable.

Some candidates who had selected readymade garment industry in answering this part ignored to mention that availability of local fabric and accessories to a limited extent under “related & supporting industries”.

Question No. 03 – SWOT Analysis – AM-16, AP-09

(i) Meaning of SWOT – AM- 04, AP-03

Most of the candidates answered correctly what SWOT stands for, for which 02 marks were allocated. Nevertheless most of the candidates were not able to explain correctly the 4 elements. For them strengths and weaknesses were internal factors whilst opportunities and threats were external factors. Only a few had clear understanding about the fact that all SWOT elements were to be identified in relation to the competition and environment.

Only a few explained that “Threat” if left alone would hinder the progress of the Organization.

(ii) Insights provided by SWOT Analysis – AM-12, AP-06

Some candidates had not shown their knowledge about “Steps” and “Tools” involved in carrying out a typical SWOT analysis.

Some have not cited important tools like Porter’s five forces model for industry environment analysis.

Most of the candidates were not aware as to why SWOT analysis should have been carried out.

Some have been silent about conversion of weaknesses into strengths whilst some did not know the requirement of matching strengths and opportunities.

Some had not drawn SWOT matrix correctly in providing insights of SWOT.

Question No. 04 – Value Chain & Benchmarking – AM-16, AP-12

(i) Value Chain Activities – AM-08, AP-06

Most of the candidates ignored the fact that (value) creating activities should begin with “designing stage”.

Some candidates had not correctly drawn the Value Chain Diagram, in that, some had not mentioned primary activities in proper order, i.e. Inbound logistics, Operations, Outbound logistics, Marketing & services. Some have indicated “Operations” after “Outbound logistics” in the diagram.

Most of the candidates ignored to mention that Organization uses value chain to understand as to how it creates value through primary and supporting activities, which would lead to understand sources of competitive advantage i.e. low cost and differentiation.

(ii) Stages of Benchmarking – AM 8, AP- 06

Most of the candidates did not indicate the stages in an orderly manner i.e. “Gaining senior management commitment to the benchmarking project” should be the first task to be fulfilled.

Some candidates had ignored to mention that understanding processes and developing appropriate measures as important stage.

Some candidates explained types of benchmarking, vis. a vis., internal benchmarking, competitive benchmarking etc. wasting their valuable time, instead they should have just mentioned the “choose appropriate organizations to be benchmarked against”.

Question No. 05 – Branding, Positioning – AM-20, AP-15

(i) Definition of Brand -AM-3, AP -2

Some candidates ignored to mention that the purpose of branding is to identify a product of one seller and differentiate it from that of competitors.

Some displayed their lack of knowledge over a combination of name, term, sign, symbol or design also, constitute a brand.

Some ignored to mention “Sign/Symbol” also a part & parcel of a brand.

(ii) Elements of a Brand – AM-06, AP-04

Some candidates did not mention “Associations” as a principal element of a brand.

Some were unable to provide examples of elements correctly. E.g; Some stated that Coca-cola is red & white rather than” Coca-cola is white on red”.

(iii) Brand to gain strategic advantages – AM-06, AP-05

Most of the candidates had answered this part successfully. Nevertheless some did not mention important advantages like building customer loyalty or attachment to the product which would make it difficult to customers to switch to a competing brand.

Some provided general answers like “Brand will help sales turnover-boost”, “Brand attracts customers” which were not elaborative enough to earn full marks.

(iv) Positioning- AM-05, AP-02

Most of the candidates just mentioned that positioning helps creating a place in the minds of customers. They ignored to mention that it is a distinctive place and the fact that positioning is the act of designing the Company’s offering in such a way, benefits of product/services will occupy a distinctive place in the minds.

Some ignored to mention that all marketing strategy is built on STP i.e. Segmentation, Targeting & Positioning, without which role of the positioning is not complete.

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Advanced Taxation and Strategic Tax Planning – June 2012

General

1. The question paper had a good coverage of the current syllabus. At the Strategic Level, the paper can be considered as a balanced one, neither too easy nor too difficult. It tested the recent amendments (effective from the Y/A 2011/2012) and affecting taxation of companies, partnerships and individuals.
2. The under mentioned strengths and weaknesses are noteworthy.
 - a. In answering the various questions, the approach adopted by a good number of candidates appears to be encouraging. They displayed good knowledge in the presentation of tax computations and ascertainment of statutory income from various sources of income.
 - b. Illegible handwriting: In some cases it was impossible to read the answer of the candidates consolidated comments.
 - c. Poor communication skills: Majority of the candidates were averse to theoretical questions requiring writing skills.
 - d. Poor time management/planning: Candidates should learn to read the question once, twice or even thrice before answering a particular question so that they can understand clearly what is required.

Some candidates write volumes for question carrying only 4 marks while some candidates answer the same question twice (duplication) with slight variation.
3. The Inland Revenue Act is subject to frequent amendments and therefore candidates should keep themselves updated.

Question No. 01

The question tested the computation of gross income tax liability of a listed plantation company owning tea and rubber estates and tea factories.

The question could have been worked within the allocated time by an average candidate.

The overall performance was disappointing as only a few candidates record more than 50% of the allocated marks. Shortcomings/weaknesses in the answers are mentioned below.

- a. Planning and time Management - Taxation of a plantation company had not been tested at least in the last 5 years. The mere sight of the word 'plantation' appeared to have shattered the hopes of the candidates of passing the subject. This was evident from the fact that a majority of the candidates chose to answer this question last in their priority of answering. This could have resulted in insufficient time to answer this question carrying 30 marks. This type of misfortune could have been avoided by proper understanding of the question and planning the answer.

- b. Presentation of income tax computation.
 - (i) Some candidates commenced the computation from “Turnover” while a few others commenced from “profit after tax”.
 - (ii) Some divided the computation into agriculture and non-agriculture.
 - (iii) Some candidates deducted (instead of adding) disallowed expenses from net profit and added (instead of deducting) allowable expenses/claims from net profit.
- c. Agriculture specific adjustments: A good number of candidates failed to make the correct adjustments in the following accounts.
 - (i) Nursery
 - (ii) Immature plantation
- d. Foreign travel expenses: Some candidates computed 2% of adjusted profit for Y/A 2010/2011 for the purpose of restriction with regard to the deductibility of foreign travel expense but failed to correctly apply it in the tax computation.
- e. Ground rent and approved donation: Some candidates split the ground rent and approved donation to ascertain assessable and taxable income separately for agricultural and non-agriculture activities. Candidates should have understood that it was the adjusted profit from agriculture (statutory income) that was taxed at the concessionary rate.
- f. Deemed distribution tax: Though the distributable profit for Y/A 2010/2011 was given in the question, some candidates computed distributable profits for Y/A 2011/2012. Candidates should have understood that deemed distribution tax chargeable for the Y/A 2011/2012 was computed on the distributable profit for the Y/A 2010/2011.
- g. Company taxation: Taxes chargeable on a company were not properly identified by the candidates, e.g. dividend tax and deemed dividend tax were not considered by many candidates.

Question No. 02

The question tested:

- (i) The computation of the gross income tax liability of an individual having income from different sources.
- (ii) Deductibility of interest paid on a loan to construct a house.

There were substantial amendments to Inland Revenue Act effective from Y/A 2011/2012 and affecting taxation of individuals. More than 10 (ten) such amendments were tested in the question and it is comforting to mention that a good number of candidates displayed fair knowledge of such amendments. The under mentioned weaknesses/shortcomings are noteworthy.

- 1. Employment Income:
 - a. Some candidates treated PAYE deducted from employment income as final tax when there were other sources of income where no final tax has been deducted.
 - b. Housing benefit: When computing rented value, some candidates applied the method of net rent income computation.
 - c. Motor vehicle benefit: Since the question did not mention whether fuel of driver was provided many candidates presumed neither fuel nor driver was provided. However, any candidate who applied a different value should have mentioned his/her assumption. A few candidates gave different values without stating the assumptions.
 - d. Exemption of vehicle benefit:
 - i. some candidates treated the vehicle allowance as liable and exempted the value of the benefit of the motor vehicles.

- ii. some candidates exempted the value of the benefit of the motor vehicle instead of exempting the higher value (vehicle allowance). Items (i) & (ii) were clear examples of misunderstanding of the candidates of the new amendments affecting employment income.
 - e. Profit from construction and sale of small houses: This profit was exempt under section 13 (zzz). A good number of candidates treated this was liable to tax.
 - f. Profit from agriculture. The exemption granted under section 16 expired on 31.03.2011 and such profits are liable @ 10% from the Y/A 2011/2012. Some candidates did not know that the exemption is over.
2. Tax free allowance: A few candidates claimed Rs. 300,000
 3. Qualifying payments. Expenditure on construction of small houses (less 500 sq.ft.) This relief cannot be claimed from employment income form Y/A 2011/2012. A good number of candidates made mistakes in their computation of the claim.

Part (2): Most of the candidates seem to have not understood the question properly.

Question No. 03

This is a tax administration question.

Part (a) tested circumstances which would make it compulsory for an individual to open an income tax file.

Part (b) tested a particular method adopted by the CGIR in the exercise of his powers to recover taxes in default.

Part (c) tested the meaning of regular profits from employment for the purpose of deducting PAYE tax.

Part (a): general performance was quite satisfactory and good number of candidates scored 100% of the marks.

Part (b): general performance was very poor. A good number of candidates had written irrelevant answers,

e.g. (i) some candidates mentioned a bank's obligation to deduct WHT on interest paid on fixed and savings accounts (section 133)

(ii) Some treated this notice as an assessment on the bank manager and mentioned that the manager should lodge an appeal against this notice.

Part (c): general performance was quite unsatisfactory. Most of the candidates gave irrelevant answers or answered in general terms. E.g. "profits earned in working as an employee".

The answers to these tax administration questions clearly expose poor reading habits of the candidates.

Question No. 04

Part (1) of the question tested the knowledge of standard value added tax (VAT) together with the new concept of simplified value added tax (SVAT).

Part (2) of the question tested the responsibilities of a VAT registered person. The under mentioned weaknesses are noteworthy.

(i) a good number of candidates treated supplies to garments exporter and value added tax exporter as exempt zero rated.

(ii) treating a supply in respect of which SVAT credit voucher is not collectible as a SVAT supply.

- (iii) VAT debit note received from a local purchases, adjusting this with output tax instead of adding to input tax.
- (iv) a good number candidates appear to have not properly understood the operation of SVAT mechanism particularly that the SVAT payable can be set off using the SVAT credit vouchers against the total VAT payable.
- (v) set off of unabsorbed input tax brought forward,
 - some candidates claimed 10% of the net unabsorbed balance as at 01.12.2011.
 - some candidates applied 5% of the total VAT payable instead of net VAT payable.

Question No. 05

The question tested the knowledge of computing the adjusted/divisible profits of a partnership and the net partnership tax payable. It also tested the computation of the tax liability of one of the partners.

The question was a straight forward one devoid of complicating adjustments and, at the Strategic Level, could be considered as a bonus question.

Shortcomings/weaknesses noticed in the students answers:

- (a) Poor reading of the question, e.g. computing the income tax liability of both partners when the question requires computation of the tax liability of only one partner, a clear case of wasting valuable exam time.
- (b) Ignorance of amendments to tax law,
 - e.g. (i) taxing partnership @ 10% (the rate for Y/A 2011/2012 is 8%)
 - (ii) applying erroneous proportion for the purpose of claiming tax credit in respect of partnership tax and ESC paid against individual partner's tax liability.
- (c) Profit sharing ratio, As per the Partnership Act, the partners should share profits and losses equally in the absence of any provision in the partners' agreement to the contrary. A few candidates have taken the ratio of partners' salaries for this purpose.
- (d) Taxation of partners - The maximum sale applicable is 10% (educational services) A few candidates applied 10% to the entirety of the taxable income (i.e. ignoring 4% & 8% slabs)

Question No. 06

The question tested knowledge of the candidates in case law.

Parts (1) & (3) are based on section 25 (1) of the Inland Revenue Act. Candidates should be well conversant with this section and always quote where relevant, because this is the legal authority for the deductibility or otherwise of an item of expense or outgoing. Most of the candidates mentioned "circulating capital", "revenue nature" but only a few mentioned S.25 (1).

Only a very few discussed the deductibility of expense where the wordings in the Act are "incurred in the production of income" or "for the purpose of trade or business."

Part (2) tested whether depreciation allowance can be claimed in respect of an elephant owned and used by a tourist hotel for the purpose of providing elephant rides to tourists. A good number of candidates answered that such allowance cannot be claimed. Candidates are advised to read the case law "Yarmouth vs France for a detailed discussion on this issue.

THE INSTITUTE OF CHARTERED ACCOUNTANTS OF SRI LANKA

Commercial Law and Corporate Law – June 2012

Question No. 01

- (a) Performance in part (a) of the question is very poor. Question clearly asks to explain as to how a contract is performed under Sale of Goods Ordinance. In other words to explain the manner by which a sales transaction is completed. Majority of the candidates had not understood question and had explained numerous areas which have nothing to do with performance of a contract under Sale of Goods Ordinance. Accordingly the answers produced by candidates have covered areas like,
- i. Defining sale of goods or contract of sale of goods instead of explaining performance of such contract.
 - ii. Parties to such a contract and other requirements for same. Such as there should be goods, consideration, the consideration should be in money, seller should have a right to sell the goods and so on.
 - iii. Contract for sale of goods should be performed as per the Sale of Goods Ordinance.
 - iv. Contract of sale of goods is performed subject to conditions such as seller should have title for the goods, goods should comply with the description given. Goods must be fit for the purpose, goods should be in merchantable quality and they should be comply with sample, and so on and wasted time.
- (b) Question requires to discuss the rights of an unpaid seller under Sale of Goods Ordinance, a question appears in this paper on and off. Therefore, candidates should be familiar with those rights of an unpaid seller. Though a fair percentage of candidates were familiar with them a similar percentage of candidates were not. Many of them were not much sure regarding the rights of an unpaid seller and had tried to explain unnecessary areas stating in different forms such as;
- i. rights agent the buyer/against the goods
 - ii. action for price
 - iii. action for non-acceptance of goods.
 - iv. sue in court and recover the price/
 - v. action for damages if there is any loss to the seller.
 - vi. rights against non-payments.
 - vii. sue for breach of contract and so on.

As the candidates were not much familiar with the Ordinance they had presented their own presumed answers. If the candidates were conversant with the provisions of the Ordinance they should not have presented these types of irrelevant answers in wasting their valuable time. They have divided them into some unwarranted sub-divisions though the question did not expect to do so. As stated here above some candidates had expressed the view that unpaid seller has a right against the buyer for non-acceptance of goods. What they had failed to understand was that, if the buyer had not accepted the goods sold by the seller there would be no completed contract of sale. Also when question asked to describe the rights of an unpaid seller they had wasted time to discuss and explain regarding actions against non-acceptance of goods. Further some others had dealt with damages that could be claimed by the seller in the event if he had sustained any loss due to non-payment by the buyer. On the other hand it has no connection to an unpaid seller and they had failed to explain where the seller has sustained losses due to this. Also some others had stated that the unpaid seller had the right sue for breach of conditions of the contract of sale.

Here again those did not convey under the heading of underpaid seller though there could be instances where one party can initiate legal action against other party who had breached the conditions of contract for which they entered into

When it is summarized it could be observed that most of the candidates were not conversant with the provisions of the Sale of Goods Ordinance or not competent to produce satisfactory answers to the question as laid down in Sale of Goods Ordinance and tried to furnish some answers built up by them following the common principles applicable for any type of contract in general.

Question No. 02

Performance of this simple question which dealt with instances under which a partner could make an application to court to dissolve the partnership was not up to expectations. Though the question clearly stated that Padman seeks advices as to when a partner could make an application to court to dissolve the partnership, some candidates had tried to explain instances where a partnership could be dissolved voluntarily or automatically. Accordingly some candidates had given following instances as a partner can make an application to court to dissolve a partnership.

- i. Death or retiring of a partner
- ii. If the partnership become illegal to continue.
- iii. When partners agree to dissolve the partnership by mutual agreement.
- iv. When a partner has sold his share to an outside party.
- v. When a new partner admitted to partnership.
- vi. When partnership has achieved its objectives for which it was established.
- vii. When partners are of the view that it is better to dissolve the partnership.

Several others had wasted time to discuss in length regarding the two ways by which a partnership could be dissolved i.e. voluntarily dissolution and dissolution by court.

Some others had expressed the view that when a partner is entering into partnership or a partner sells his share to outside the partnership should be dissolved voluntarily. Accordingly Taste Tea should be dissolved voluntarily and form a new partnership. Therefore Padman need not consider the ground for dissolution of partnership under court order but it could be dissolved without court order. Few others were of the view that according to Partnership Ordinance new partner could be admitted to partnership with the approval of all the other partners and sign a new partnership agreement and no need to dissolve it.

Handful of others had confused with liquidation or winding up of a company under court order or under supervision of court with dissolution of a partnership with court order and explained various irrelevant areas. It was clear that candidates had no clear and complete knowledge on the area tested or same time they have not read the question and understood it properly as to what was expected by the question.

Further a minor percentage had dealt with completely irrelevant area such as definition of partnership various ways by which a partnership could be formed, relationship among partners, duties and responsibilities of partners and numerous other areas instead of stating as to when a partner can make an application to court to dissolve it. These types of shortcomings take place mainly due to not exercising proper care in answering the question and also due to poor reading habit of the question by candidates before starting answer the same. Writing lengthy answers glancing through the question with no sense of the same will not produce deserved results. Therefore, candidates should make it a point that the question is read and understood properly to realize as to what is expected by the examiner from the question.

Question No. 03

This was a simple question on normal contract. In the given case what happened was that Mr. Clean had not disclosed the actual terms and conditions to Jane in spite of her clarifications at the time of handing over her dress for dry cleaners Mr. Clean has induced Jane to enter into the contract by misrepresenting the facts applicable for the contract. The issue was when there were stains on her dress after dry cleaning it, whether Mr. Clean can rely on the exception clause which he had tried to introduce to Jane by misrepresenting the facts. Had the candidates analyzed the problem on those direction they would have furnished satisfactory answers for this simple question on Law of Contracts.

Instead of doing so they had explained various facts or areas which had no connection to the case given. In their answers some had tried to define exception clause or stated that this kind of agreements were very serious and if one party breach the conditions of the agreement other party can take legal action against the party breached the conditions. Some had expressed the following views.

- i. This is a commercial agreement. Commercial agreement means a contract between two parties with the intention of creating legally binding contract.
- ii. At the time of handing over the dress Jane signed a receipt. This written document is sufficient to create legally binding contract between the two parties and it was done with serious intention.
- iii. Jane cannot take any action against Mr. Clean for damages in her dress because at the time of handing over the dress she signed a receipt which states that the company is not liable for any kind of damages that may arise out of the cleaning.

There were few others who had opposed the above views. Jane has several remedies for breach of contract namely;

- (a) refuse to further performance of the contract.
 - (b) take actions for damages
 - (c) sue for specific performance
 - (d) get an injunction against Mr. Clean and so on and wasted their time.
- (b) Another simple question on Law of Contract where the candidates were expected to identify the two terms i.e. conditions and warranties in Law of Contracts. Further what are the effects on contracts for breach of conditions and breach of warranties. In the given case definitely the main term is to play for the said club for 2012 season and taking part in at least term practice sessions is a subsidiary of the main term i.e. a warranty. Accordingly it is very clear that participating in practice sessions is not a term which goes to the root of the contract but it is a subsidiary term to the main term or only a warranty and not a condition. So what is the effect of breach of a warranty?

If the candidates were capable to analyze the case on those lines definitely they would have furnished satisfactory answers. But the candidates were not much competent or capable of doing so and had wasted time to deal with various irrelevant areas and following are some of the answers given by them

- i. Contract could be terminated by following methods.
 - (a) by giving notice
 - (b) by breach of the contract
 - (c) by agreement
 - (d) by performance
 - (e)

In Law of Contract there are some methods to terminate a contract such as

- a. revocation
- b. rejection

- c. laps of time
 - d. failure to fulfill a condition in the contract
 - ii. Mr. Credit could not play the 1st match because he has not practiced enough since he had not participated 10 practice sessions and so on.

Question No. 04

- (a) Candidates were expected to discuss the rules applicable for insurable interest in life insurance. Especially when one person want to obtain a life policy on the life of another. In the given case it was stated that Mr. Debtor owes Rs. 1 million to Mr. Creditor and Mr. Debtor has requested credit period of 1 year to settle his due to some reasons . Mr. Creditor is willing to give 1 year period provided that he can obtain a life policy on the life of Mr. Debtor, therefore he wished to get advise in that respect. An insurable interest means that the person affecting the insurance will sustain financial or pecuniary loss on death of the whose life is to be insured. In problem given in the question it was very clear that if Mr. Debtor would die during the one year period for which credit period was extended, definitely Mr. Creditor would have suffered a pecuniary loss of Rs. 1 million. Therefore it is evident that Mr. Creditor has an insurable interest on life of Mr. Debtor up to Rs. 1 million. This position has been laid down in certain case law too. Candidates have same idea on those areas and had discussed re-insurable interest Mr. Creditor has on the life of Mr. Debtor but they are not much competent build up a suitable answer to the question applying their knowledge on the subject matters as required by the question. Further it could be observed that majority of the candidates used to just state that Mr. Creditor has a right to obtain life policy on the life of Mr. Debtor without explaining the principle and connecting the same with Mr. Creditor's eligibility to obtain the life policy. It is very important to discuss the principle first and to connect same to the case given in question.

A minor percentage of candidates had dealt with irrelevant areas and had tried to discuss 3 most important elements in insurance namely premium, uncertainty and utmost good faith or some other elements in insurance and named them as indemnity, utmost good faith, subrogation and insurable interest and so on. Few others has wasted their time to discuss ways by which the business of Mr. Debtor can be improved so that he can settle the amount due to Mr. Creditor without postponing the payment.

- (b) Part 'b' is too in insurance but the person who insured the property has done deliberate act by setting the fire on his armchair with the view of making an insurance claim. It is also very clear that no insurance claim could be made for the damages caused by the deliberate acts done by the insurer himself with the malicious intention of making an insurance claim. The question clearly explains that Mr. Raux has set fire on broken armchair since he has no money to repair it. This has been done with very purpose of claiming damages under the fire policy he had already obtained. Here the simple question that could be raised is that whether an insurance claim could be made on damages caused on deliberate acts done by the applicant himself. Had the candidates analyzed the problem in those directions they would have furnished acceptable answers for this simple question. Although some candidates had given some relevant answers they are not much competent to furnish fully acceptable answers by analyzing the problem on correct directions.

There were some others who had expressed the view that the insurance company is liable to pay compensation even it is a case of willful distraction of the insured property. They have stated this by ignoring the insurance principles. Further few others had wasted time to explain numerous irrelevant areas and the following answers had been furnished.

- i. The following must be existed in insurance contract
 - a. Periodically payments – premium
 - b. An uncertain event.

- c. The uncertain event should adversely affected the insured and so on.

Question No. 05

- (a) Performance in this direct question is better when compared with other questions and large number had correctly given the three main contents that should be included in an Articles of Association as laid down under section 13 of the Companies Act and scored full marks allocated for part (a). However there was a minor percentage of candidates who were not familiar with said section and had written some irrelevant answers and following had been given as contents of an Articles of Association.
- i. The structure of the shareholders' ownership and other provisions
 - ii. Contents according to part I of the 4th schedule of the Act
 - iii. Required reports according to part ii of the 4th schedule to the Act such as Auditors' report, Accountants' reports and so on and wasted their time.
- (b) Candidates have some knowledge on areas tested by the question as they were familiar with section 15 to a certain extent. The main weaknesses that could be observed was that though they had some idea on contents of section 15 they were not capable in presenting a suitable answer to the question. In furnishing the answers they had unnecessarily wasted their time to explain the procedure to be followed in passing a special resolution though it is not expected by the question . Although section 15 (i) of the Act specifically states that subject to the provision of the Act, a company may at any time alter its articles by passing a special resolution, the candidates had not understood it in the same manner but stated that according to section 15 (i) company can alter its articles which is not the correct section.

There were few others who were not familiar with the section and had written completely irrelevant answers. As per their answers the contents to be included in communication to Registrar of Companies when altering the articles are;

- i. The name of the company.
- ii. The number and address of the company
- iii. Copying of the new articles (not the full text of the resolution)
- iv. Signatures of the directors and so on.

Handful of others had stated that within 20 working days of altering the articles of association the company should send the amended articles to all the shareholders of the company whilst some others had expressed the view that the company should include the following into the alteration.

- i. The new object of the company
- ii. The amended rights, obligations and additional rights of the shareholders.
- iii. The changes established in the management and administration of the company .

Some had wasted time to deal with the following areas instead of detailing the methods followed for alteration of articles of a company.

- i. The registrar may replace the new (amended) Articles of Association in place of the previous articles they had delivered at the time of incorporation and update company documents.
- ii. Company should give public notice within 5, 10 or 14 working days from amendments. This is an indication that they failed to understand the question properly.

Question No. 06

Direct simple question from the Act to test the knowledge on provisions laid down under sections 49 & 52 of the Company's Act. The question could be answered by an average final level accountancy student with his/her general knowledge in accountancy since the subject areas like rights of shareholders, different classes of shares that can be issued by a company under the provisions of the Act and different form of consideration which are generally covered in company accounts.

Performance in all 3 parts of the question was better than that of other questions and majority has scored higher percentage of marks allocated. However there was a minor percentage who has failed to furnish acceptable answers, since they were not much familiar with sections 49 and 52 of the Act. Due to that reason some had furnished irrelevant answers and few examples for each part is given below.

- Part (a)
- i. There are mainly 2 sources by which shareholders rights are set out namely Company's Act & Articles of Association.
 - ii. Possess ownership (to some extent) of the company
 - iii. Can take part in decision making process.
 - iv. Can have some interest on activities of the company.
 - v. Can be appointed as directors of the company.
 - vi. Right to take part in right issues and bonus issues. .
- Part (b)
- i. Shares which confer no rights.
 - ii. Non-redeemable shares
 - iii. Convertible and non-convertible shares.
 - iv. Cumulative and non-cumulative shares
 - v. debentures
 - vi. differed shares and so on.
- Part (c)
- i. Bills of exchange, credit rates or any other benefits.
 - ii. Financial instruments
 - iii. Consideration for issue of shares in determined by Board of Directors.
 - iv. Consideration should be fair and equal with the existing shareholders and of the company.
 - v. Mobile phones, trade stocks .
 - vi. Shares of other companies.

Failure to understand the question and their poor knowledge on relevant provisions of the act were the main reasons for poor performance in this easy question.

Question No. 07

Performance in this question was below the average and it indicates that they have not paid sufficient attention regarding procedure followed in voluntarily winding up.

Part (a) of the question clearly states that the company seeks an advice on notice of resolution of winding up voluntarily but instead of dealing with the advice on notice of said resolution, candidates had written numerous irrelevant points or discussed irrelevant areas as they were not familiar with notice of resolution of voluntarily winding up. Few examples of answers produced by candidates are as follows:

- i. If the Articles provides dissolution of the company after specific period or activity of any specific task, after expiring such period or achieving such task company may voluntarily wind up after passing an ordinary resolution for that effect.

- ii. Company can pass a special resolution to wind up voluntarily if it cannot continue with its business due to liabilities of the company.
- iii. Company should send notice of the resolution of winding up voluntarily to the Registrar of company.
- iv. Company should give notice to its shareholders by calling for a general meeting by giving 15 working days notice to them.
- v. Voluntarily winding can be under court order and under the supervision of the court.
- vi. The court may appoint an additional administrator and take the administration of the company under the supervision of the court.
- vii. If the company wishes to wind up the company voluntarily under the supervision of the court it may request to court to do so.

Part (c) -This part clearly asks to advise on effect of voluntarily winding up on business and status of the company but instead of advising of said areas the candidates have wasted time to explain following areas which have no connection to the question.

- i. Name of the company is removed by registrar from the register.
- ii. Directors and employees of the company are removed and the liquidator is appointed.
- iii. Assets and liabilities of the company settled by the liquidator
- iv. Shareholders cannot transfer their shares to others.
- v. No alterations to the articles of association could be effected and sale of assets of the company is void.
- vi. In terms of the provisions of the Companies Act upon commencements of winding up of the company Board of Directors has to make a declaration of solvency. This will state that they have made a full inquiry into the affairs of the business and are satisfied that the company will be able to pay off its debts within 12 months from the commencement of the winding up.
- vii. After company pass the special resolution for winding up voluntarily court may order the voluntary winding up should be subject to the supervision of the court. Court can appoint a receiver/liquidator for winding up process and company should settle its liabilities.
- viii. Company should call a general meeting to appoint one or more liquidators and to fix their remuneration. After winding up, liquidator has to give notice to court and get the dissolution order and it should be sent to the Registrar of Companies.

Here again the very clear indication is that candidates were not familiar with section 322 and other relevant provisions of the Companies Act and presented their own presumed answers

Answer No. 08

Performance in this question is below the expectations. It is well known factor that though there was age restriction to appoint as a director of a company in Companies Act No. 17 of 1982, this restriction has been removed for the directors of private limited companies which are not subsidiaries of public companies by the new Companies Act, No. 07 of 2007. Also it is well known that the new Act too permits appointment of a person who is over 70 years of age as a director of a private company which is a subsidiary of a public company or to a public company after passing ordinary resolution of a general meeting of that company for a period of 1 year from the date of such appointment. If the candidates were conversant with the said provisions of the act definitely they would have furnished satisfactory answers. But the answers furnished by the candidates clearly indicate that they were not much familiar with the provisions and they have produced answers based on their general knowledge which do not deserve higher percentage of marks.

Candidates were not aware that, to be appointed as a director of a private company the said age limit of 70 years is applicable only for private companies which are subsidiaries of public companies.

They have commonly explained that to appoint a person over 70 years of age as a director of a company, an ordinary resolution has to be passed. By such resolution it should be declared that the age limit of 70 years shall not be applied to the proposed person for director who is over 70 years and he must give notice of his age to the company without making no differentiation as to what companies those rules should be applied. In other words they are of the view that the rules explained above would commonly apply for all the companies whether it is a private company, public company or private company which is a subsidiary of a public company. Candidates were not very clear on those rules.

Many others had explained various other irrelevant areas such as;

- i. Directors can be appointed by the Board of Directors.
- ii. According to the Company Act the minimum age is 18 years and maximum is 70 years.
- iii. When appointing a director there are some restrictions such as;
 - a. Court may disqualify persons to appoint as directors.
 - b. People who are unsound mind, who are not compiling with Companies Act/Articles of the Company.
 - c. They could be disqualified under section 202 & 213 of the Act.
 - d. Person whose nationality is of another country.
 - e. If Mr. Snow is to be appointed as one of the initial director of Traditional (Pvt.) Ltd he will have to be named in the application for incorporation of the company and he should give his consent in writing to be appointed as an initial director of the company.

These answers clearly indicate that candidates have not read the question properly before answering it.

Part (b) - answers to this part were also not satisfactory. Candidates were expected to deal with duties of a director when he believes that the company is unable to pay its debits as they fall due. Instead of answering to that specific issue large number of candidates had dealt with duties of directors in general such as duty of care, not to make secret profit and so on. Some others had referred to some sections of the Act which deal with duties of directors of a company including the following.

- 187 to act in good faith and in the best interest of the company.
- 188 to comply with articles of the company and Companies Act.
- 189 duty of directors for standard and care.
- 190 use of information by directors
- 197 provide information when necessary.
- 220 duty of directors in serious loss of capital .

Had the candidates read the question carefully and understood as to what was expected by the question they would not have wasted their time to explain unwanted areas without gaining any marks.

Few others had stated that if the director is unable to fulfill his duties in this respect and if the business of the company continued and had to wind up in near future that the director will be personally liable for the losses arising from the winding up. Whilst handful of others had expressed the view that this one of the statutory provision for lifting of veil of incorporation. Here again the clear indication is that candidates were not much familiar with the provisions of the Act in the areas tested by the question.

Question No. 09

Mr. Earl an engineer has given his written consent to include his statement as an expert in the prospectus to be issued by company X, and the question asks whether he can withdraw his consent from the prospectus since the prospectus has still not been sent for registration to the registrar. The simple answer would be he can do so at any time before it is sent for registration. However if he had any other obligation to the company in that respect the answer could have been different.

Had the candidates thought the situation in that point of view and considered any normal instance where any person has given his consent for certain task or activity and wishes to withdraw the given consent before the said activity is finalized definitely he has a right to do so. It is very clear the same thing has happened here. Therefore Mr. Earl does have a right to withdraw his written consent given originally. If the candidates had developed their answers in a similar manner as discussed above there would have been some acceptable answers which deserve reasonable marks. Instead of looking at the issue in that manner some candidates had dealt with various irrelevant areas such as;

- i. Mr. Earl has submitted a letter to the Board of Directors of the company.
- ii. Defining the prospectus and stated prospectus means a notice, circular, advertisement or prospectus offering shares to the public for purchase of shares of the company.
- iii. Prospectus shall include two parts as part (i) and part (ii).
- iv. There are some information in part (i) of prospectus such as objects of the company, list of directors, minimum no. of shares required to purchase and time of opening and closing of subscriptions.
- v. Part (ii) of prospectus includes auditors' report, and accountants reports and so on and engineer's statement is not needed unless the articles provides to do so. Therefore Mr. Earl can prevent from including his statement in the prospectus.

What could be observed is that they have furnished those completely irrelevant answers mainly due to not reading the question properly before starting answering the question.

Part (b) of the question too is very simple and answers to this part of the question indicate in part (a) of the question i.e. if the part (a) is read carefully one can find answers to part (b) within the question itself. In part (b) it says that company Z wants to include Mr. Lawson, an attorney at law as company's lawyer in the prospectus of the company and requesting to briefly explain the guidelines that should be followed by company Z prior to including his name in prospectus, whilst part (a) clearly explains the guideline that should be followed in this respect i.e. including of a statement of an expert. Had the candidates compared the two parts of the question they would have found the answer for part (b) in part (a) of the question. In other words before including Mr. Lawson's name in the prospectus company Z should obtain his written consent for the purpose and make sure that he has not withdrawn the given consent before it is sent for registration.

Very high percentage of candidates had failed to analyze the problem in an acceptable manner or to understand it correctly and furnished their own presumed answers which were hardly relevant or not at all relevant to the question.

Part (c) of the question expects to deal with the provisions laid down under section 36 of the Companies Act. Here again it is clear that when a prospectus is issued there should be a date for it (section 36) and in addition to that the section explains that the said date shall be treated as the date of publication of it unless there is something contrary to it. Some candidates were not much familiar with said section and were not competent to furnish satisfactory answers. Under the circumstances some had furnished irrelevant answers such as:-

- (i) The company should clearly mention the following:
 - a. The date of which the offer is opened.
 - b. The date of which the offer is closed. Otherwise the prospectus is not valid under the Companies Act
- (ii) The date of the prospectus should be the date given by registrar.
- (iii) Dates should be specified in prospectus such as date of issuing shares, date of closing the issue of shares and so on

Another possibility that could be observed that some candidates have studied only some selected areas from the Act instead of studying it as a whole. This practice may not be much useful since questions are set to cover the whole Act. Therefore candidates are expected to have some reasonable knowledge on the whole Act and not from selected areas according to their own wishes.

Question No. 10

Part (a) of the question requires to explain the formalities to be observed when a company wishes to enter into a major transaction as laid down under section 185 of the Companies Act. Candidates were familiar with the first out of the four requirements that should be followed when a company enters into a major transaction i.e. it should be approved by passing a special resolution. Few others knew the balance 3 requirements whilst the majority knew only another one or two only. Requirements like contingent on approval by special resolution or consented to in writing by all the shareholders of the company are not known to the majority. Had the candidates presumed that there should be some special features on this type of transactions they would have paid special attention for them but it appears that they have not.

Since a fair percentage of candidates were not conversant with section 185, it appears that they were not sure of the answer for the question. As a result they have presumed some of their own answers which were not relevant to the question and some of the answers furnished by them are;

- (i) Explained as to what is a major transaction.
- (ii) What includes to a major transaction namely
 - a. Acquisition/disposal of whole or more than 50% of the assets of the company.
 - b. Acquisition proposal of obligations, whole or more than 50% on assets of the company.
 - c. Transactions which has the purpose of substantially altering the nature of the business of the company.
- (iii) Board of Directors of the company must approve such major transaction.
- (iv) If it is a private company there should be a unanimous agreement to enter into a major transaction.
- (v) If the major transaction is directly or indirectly related to financial benefits of directors it should be disclosed to an independent Board of Directors and enter in the interest register.
- (vi) The directors of the company should satisfy that immediately after entering into the major transaction company will satisfy the solvency test and so on.

What could be observed is that these answers were purely based on their own presumptions and no connections to legal provisions.

The practice followed by majority of candidates when they were not familiar with the areas tested by certain questions was to presume some answers and write whatever they think to be correct answers. By doing so they have eventually wasted their considerable length of time even without their knowledge and deserve no mark for them

Part (b)-This part is very simple and deals with solvency test. After the new Companies Act came into application candidates are supposed to have a very high standard of knowledge on solvency test since it is dealt in accountancy subject too. With this background candidates are expected to furnish very high standard answers. Although a minor percentage had furnished satisfactory answers the answers furnished by the balance are not up to expectations. Also it could be observed there were handful of candidates who are still not familiar as to what is solvency test and how it should be calculated at their Strategic Level.

A further handful of others had furnished irrelevant answers such as;

- i. Naming documents or financial statements that should be used in carrying out the solvency test instead of using the information given in question.
- ii. Method of valuation of financial statements for the purpose.
- iii. Views should be obtained from directors for any possibilities of any acts which may have serious effects on company's assets and liabilities.
- iv. Methods that should be used for valuation to identify the value of assets and liabilities.
- v. Before company going to declare dividend the directors should state that the company will satisfy the solvency test immediate after declaring dividend and so on as they are not sure as to what is tested by question. Here again it is very clear that they had no sufficient preparation for the examination which is adequate to earn pass marks.

General

It is usual that candidates do not have a habit of reading the question properly before they start answering it. They should never give up reading the question till they clearly understand it. Spending even 4 – 5 minutes is not definitely waste of time.

The other weakness is the inability to express their views in English language.

The other common problem is the illegible handwriting of the candidates.

Therefore, it is very important that candidates should make every possible effort to further improve their language and writing skills. This is very important specially when answering the theory questions.