

Examiners' Comments

Executive Level Examination - September 2015

Financial Accounting and Reporting Fundamentals (KE1)

Section 1

Question 01.

Student's knowledge on theory and principles of accounting was tested in this question through 10 multiple choice questions where students were required to choose the most appropriate answer out of four given options.

A fair number of candidates have chosen correct answers for the MCQs and overall performance of the candidates was good. Majority scored more than 70% of the marks allocated to this question.

Where majority did not score marks was on the two questions relating to Accounting Standards.

Common difficulties faced by the students-

Most students made mistakes in choosing the correct answer for questions 1.9 and 1.10.

Question 1.9 tested the deferred tax impact on revaluation of a qualifying asset. Most students failed to understand that it is the tax effect that is recognized as deferred tax liability and not the full revaluation surplus.

Question 1.10 tested the students knowledge on identifying what is a financial instrument. From the options given, students were required to pick the items that did not represent financial instruments. Most students chose answer (D) instead of answer (C) .

Question 02.

There were 10 parts in this question where candidates were required to provide short answers/ calculations. An important consideration in formulating answers and managing time in this type of questions is to pay attention to action verbs used in framing the question. The structure of the answer should be based on this key point.

Specifically in parts 2.3 and 2.7, it was noted that although students have subject knowledge to perform calculations, they are unable to rationalize their answer with reference to relevant underlying principles.

Specific comments on individual questions are given below.

2.1 The question asks the need for developing accounting standards. The answers to this question was very poor. Most students wrote lengthy answers with unnecessary details wasting time. Majority scored only one mark out of the 3 marks allocated to this question. Most students explained it helps achieve comparability. None mentioned the subjectivity arising due to judgment.

2.2 This question addressed the duty of CASL in helping to improve global comparability for Sri Lankan companies in relation to financial reporting. The question clearly points out the “Global comparability and financial reporting”, but majority of students talked about areas hardly related to financial reporting. The answers addressed activities done by CASL like conducting examinations, training and seminars, developing code of ethics etc.....

The answers given showed that students start writing answers without reading the question properly. As a result more than 50% of the students did not concentrate on building up a proper answer to this question. Some have written that CASL issues accounting policies and conducts audits.

2.3 The fundamentals of accrual basis and cash basis accounting was tested in this question and the students were required to compute profit figures under both methods for a given scenario and explain the reasons for the difference in the profit figures.

Considerable number of students scored full marks for the calculation of profit under both methods, but some students failed to ascribe reasons for the difference in the profit under the two methods. In computing the profit, the mistakes made were as follows.

- i) Selling price was used to compute the cost of purchases
- ii) A few students computed the profit correctly under both methods, but incorrectly identified the accrual basis computation as the cash basis. This indicates that at this first level, the students do not know well the basic accounting principles.

2.4 This is a simple question where it tested the student’s knowledge in making correct accounting adjustments for income received in advance and income in arrears.

Majority performance was very satisfactory. However, there were some areas where a few students made mistakes.

- i) Not considering the rent received in cash for the current year.
- ii) Rent in arrears of Rs. 35,000/= was not considered in the computation of rent income for the year.
- iii) Erroneously recorded debits/ credits. Most students who used the “T” account method, debited the rent in arrears to the rent income account.

2.5 In this question students were required to List two depreciation methods. The 3 marks allocated to this question was easily achievable and almost all candidates scored full marks.

However, some students spent unnecessary time describing the methods, without properly reading the question and giving attention to the action verb used by the examiner. Therefore planning of the answer was poor, resulting in waste of time.

2.6 This asks to discuss the reasons for having different inventory values under FIFO and Weighted Average Method.

Many students explained that the reason for the difference is that in FIFO goods received first were issued first, and the answer ended up at that point. It appears that students have not understood that the fundamental point is the variation in price of the same item purchased in different batches at different time periods. If the purchase price does not change, then there will not be a difference in the valuation under the two methods. Very few students explained this in the answer. Most of the answers were incomplete and revolved round explaining that FIFO is goods purchased first are moved out first. There were a few students who incorrectly produced answers saying that WAC method is the same as LIFO.

2.7 In this question, students were required to calculate the depreciation of an asset after a valuation has revealed a change in the useful lifetime of the asset, and then to explain the accounting treatment for same under LKAS 8.

Almost all students did the calculation correctly. Although some have mixed up the dates/ periods and made mistakes in their calculations, students knew the principle.

In the theory part, the students who correctly identified this as a change in accounting estimate, described the treatment correctly, to adjust the depreciation in the current period and the future periods, i.e. prospectively. However, a few students said it is a change in accounting policy and hence should be adjusted retrospectively. These students failed to understand that the useful lifetime of an asset is an estimate, and a therefore the treatment should be as for a change in accounting estimate.

2.8 In this question, three different scenarios of leasing an asset were given where the students had to explain how the transactions should be recognized – whether as operating leases or as financial leases.

Many students identified the transactions properly, i.e. first one as an operating lease and second and third scenarios both as finance leases. But the reasons given by some students showed that they did not have a good understanding of the criteria. Therefore most students failed to score good marks for this question.

For e.g. Some students said that the first transaction is an operating lease because the useful lifetime of the Building and the lease period are not the same. And in the second transaction, it is a financial lease because the life time and the lease period are equal (both 4 years as in the question).

Some students said that in the third scenario, because the asset is a specialized one, it is an operating leases.

In common, the explanations given by most of the students were either incomplete or incorrect. Students were confused and got mixed up in the identification criteria of finance leases and operating leases.

2.9 Students were given scenarios of three categories of employee benefits and requested to define them as per LKAS 19.

Very few students defined the short term employee benefits correctly. Post-employment benefits were defined well by most of the students, but again termination benefits were also not defined properly by many.

Performance on this question was not satisfactory as students did not identify the difference between them.

There were a few students who only mentioned examples of each type of employee benefit without defining them. This is again a point in not giving attention to the action verb used. The question was not to give examples but asked to define and hence students who gave only examples failed to score any marks.

2.10 This is a theory question on LKAS 37 where students were required to identify three criteria to be satisfied for a provision to be recognized as a liability in the financial statement. General performance on this question was good.

However some students have not properly constructed their answer (worded) and lost some marks. In this also, some have just given examples for provisions without mentioning the recognition criteria.

Section 2

All 10 marks questions in this section where students have to answer 3 out of 4 questions.

Question 03.

Most of the students have attempted this question. Standard of the question was at a very basic level and quite a number of students scored the full 10 marks for this question. In general, almost all who attempted have scored well. Only about 15% of the students scored below 75% of the marks. Majority provided well-built answers while a few answers were poorly structured. The areas where the students made mistakes are given below.

- (a) Student's knowledge on preparation of journal entries to correct accounting errors was tested in this section. Some students could not obtain full marks as they failed to provide narrations to the journal entries. Without a narration, the reader may not understand as to why the entry has been passed and therefore providing narration to journal entries is a very basic requirement.
- (b) The section (b) of the question tested the ability of the student to prepare reconciliation statements reconciling the balance as per cash book with that of the balance in the bank statement. Some of the students could not obtain full marks (lost some marks) as they did not clearly separate the entries to arrive at the corrected cash book balance from the reconciliation statement. The adjustments that should be made to arrive at the corrected cash book balance were also done on the bank reconciliation statement.

A common mistake made by most of the students who failed to score full marks on this section was adjustment in relation to the cheque cancellation. Many have confused this with a cheque return adjustment.

A few students did not understand that a credit balance in the bank statement is a favourable balance. They treated this as an overdraft.

In the preparation of the bank reconciliation, some candidates did not indicate the starting balance, but proceeded with the adjustments in two columns marked as 'positive' and 'negative'. Whether the unrealized deposits are added or deducted depend on from which balance you start the reconciliation with, and therefore the few students who failed to describe the starting balance did not score any marks for the bank reconciliation part.

Question 04.

This was a question on Partnership accounting. In general most students performed well on this question. Overall students scored 70%- 80% marks on this question. Students demonstrated satisfactory knowledge except in the area of computing the minimum share of profit for one partner. Areas where students made mistakes are as below.

- fairly good number of candidates had problems in arriving at net profit available for appropriation.
- Students had difficulty in identifying which entries go to appropriation account and which go to P& L account as adjustments. Interest on the loan given by one partner was incorrectly taken under appropriation account without adjusting in arriving at the profit available for appropriation.
- Some students did not understand that the appropriation account is used only to distribute the profit as per the partnership agreement and the final profit figure after all adjustments are made should be the 'starting line' in this account. These students did the P&L account adjustments also on the appropriation account.
- Whenever a minimum profit share adjustment is given, candidates should adopt distribution of profit under normal profit share basis first and thereafter adjust for the shortfall if any. This should be the approach because the amount guaranteed is the minimum share of profit and not the maximum share. However, most students distributed straightaway giving the minimum profit share to that partner first.

Question 05

This question tested the students' knowledge of control accounts and reconciliation of control account balances with the individual accounts in the sub ledger.

The question was built on the fundamental theories in accounting on how to correct errors by way of journal entries, how these are posted to relevant ledger accounts and how the correct balances are derived for preparation of financial statements. Most of the students demonstrated a basic understanding of the topic and followed a systematic path and answered the question in a satisfactory manner. More than 50% of the students obtained 5-7 marks out of the 10 marks allocated to this question. Common mistakes made by the students are as follows.

- Students made mistakes in recording the entries on the correct side of the account (difficulty in identifying debits and credits) in reconciling control accounts.
- A few students missed out to include the cash purchases/ sales in the financial statement when computing the gross profit. This is because of a lack of time planning and planning the answer as well. After computing the credit sales and credit purchases values through the receivable and payable control accounts, students straight away extracted those two figures as sales and purchases in to the financial statement forgetting that cash sales and cash purchases figures had been separately given in the question.
- Some students used their own terminology without using the correct technical terms. E.g.: Instead of using the term "Suspense Account", students used terms such as "Difference Account", "Differential Account" etc....

Question 06

This was a question on ratio analysis and was a very easy question. However, about 70%- 75% of the candidates have chosen this as the question to leave out as this was among one of the optional questions. Hence, it appears that majority of the candidates are not familiar with computing ratios (or have not studied) to analyse the financial position/ performance.

Part (a) of the question was based on theory; it required the students to identify the reasons for variation in two given ratios namely GP ratio and ROCE. Many students lost marks on this part. The answers were very poorly structured by many. E.g.: Students said the reason for variation in GP ratio was due to change in sales or change in GP. They failed to identify why or how a change in sales or GP can occur (i.e. due to price changes or discounts or changes in the cost of purchase/ production etc.....) and therefore did not score marks.

The second part i.e. part (b) tested the ability to compute ratios. Many students made mistakes in computing ROCE and the asset turnover ratio. Students picked the profit after tax for computing ROCE. In computing the inventory holding period and receivables collection period, some students expressed the answer in times and not as a period in days and this resulted in them losing some marks.

Section 3

Question 07

This question tested the students knowledge and ability to prepare financial statements of a company for management and publication. Question specifically required the students to use the format suggested by LKAS 1.

Students have performed well in this question. Except for a few students, others have demonstrated very good knowledge of the subject/ topic. Majority scored more than 50% of the marks. However, on average only about 15% of the students were able to score more than 75% of the marks for this question. The reasons for such shortcoming is given below.

- Students lost marks due to presentation errors, not in conformity with LKAS 1. Several students failed to identify that SOCI is prepared 'for a period' i.e. for a particular length of time and did not state "for the year ended 31st March 2015.....". Similar mistake was made in the SOFP too. It is prepared as at a reporting date and should be captioned "as at.....", which was not done by some students.
- The correct wording of "Other Comprehensive Income" was not stated after the line description of "Net profit for the year". About 30%- 35% of the students omitted to show the surplus on revaluation of land in OCI.
- The order of presentation of items was incorrect under both "Current Assets" and "Current Liabilities".
- The profit on disposal of equipment was incorrect due to not taking into consideration the depreciation of the disposed of equipment.

Equip Disposal Account

01/04 Equip cost	50	01/04 Equip – Proceeds on disposal	44
Profit on disposal	<u>4</u>	Provn. for dep	<u>10</u>
	<u>54</u>		<u>54</u>

- Equipment depreciation was understated due to incorrect crediting of sales proceeds to equipment account ($44 \times 10\% = 4.4$). This should be added to the administration expenses.
- Some failed to compute depreciation for the additions to machinery purchased on 01/10/2014. ($125 \times 10\% \times 1/2 = 6.25$) This also should be added to admn. Expenses.
- Computation of taxation for the year and the tax payable was another area where many made mistakes. Taxation for the year should be ($11.2 + 2.5$ underprovision = 13.7) and Income tax payable is accordingly ($11.2 - 12 + 2.5 = 1.7$)
- Customer order invoiced and shown under debtors Rs. 22,500 but not delivered was not removed from sales and trade receivables.
- 12% bond issued on 01/10/2014 was not removed from stated capital and not shown as a non-current liability. As a result the stated capital balance in the changes in equity statement was also shown incorrectly and students lost marks for this error.
- There were quite a number of students who incorrectly showed the dividend paid (Rs. 80,000) as a deduction from the stated capital and not under Retained Earnings.
- Several students missed out to compute 6 months interest on the Bond issued nor was it taken as a current liability. ($\text{Rs.}100,000 \times 12\% \times 1/2 = 6,000$) Some students who computed this failed to recognize that interest accrual should be only for 6 months and instead computed one full year's interest.
- In some instances marks could not be awarded as clear workings were not there. Where several adjusting entries have to be made under one line item, if the students make some adjustments correctly and some incorrectly, they may lose marks allocated for the correct adjustments as well when the workings are not there. By using a calculator and entering a final figure only could result in students not scoring marks for the correct adjustments.

Examiners' Comments

Executive Level Examination – September 2015

Management Accounting Information (KE2)

General comment about submission of workings

There were a number of instances where the marking examiner could not award marks due to the failure of the candidates to submit workings; when a candidate has made a mistake, and the particular working is not shown, it may not be possible for the examiner to award marks for the correct steps in the particular working and possibly also subsequent steps which would have otherwise earned marks.

General comment about candidates' handwriting

There were a number of instances where the marking examiner found it extremely difficult to read the candidates' handwriting. If the examiner is unable to read what has been written, then no marks can be awarded to the illegible section.

Question 01

Consists of 10 multiple choice questions (MCQS) with each MCQ carrying two marks. Candidates' performance was very variable within the average of 6.8 marks out of a total of 20 for the question.

Q.

- 1.1. 14% of the candidates had indicated the correct answer (D). 54% (C) 20% (B) and 12% (A).
- 1.2. 19% of the candidates had indicated the correct answer (A). 30% (B), 30% (D) and 21% (C).
- 1.3. 41% of the candidates had indicated the correct answer (B). 20% (C), 20% (D) and 19% (A).
- 1.4. 30% of the candidates had indicated the correct answer (C). 35% (B), 30% (A) and 5% (D).
- 1.5. 70% of the candidates had indicated the correct answer (D). 14% (B), 9% (C) and 7% (A).
- 1.6. 37% of the candidates had indicated the correct answer (B), 37% (C), 16% (D) and 10% (A).
- 1.7. 30% of the candidates had indicated the correct answer (C). 40% (B), 12% (D) and 18% (A).
- 1.8. 9% of the candidates had indicated the correct answer (D), 36% (C), 31% (B) and 24% (A).
- 1.9. 18% of the candidates had indicated the correct answer (B). 40% (D), 24% (A) and 18% (C).
- 1.10. 70% of the candidates had indicated the correct answer (D), 14% (A), 9% (B) and 7% (C).

Question 02

General comment

This was a compulsory question comprised of 10 compulsory parts. Each part carries 3 marks; the question covered many areas of the syllabus and sought to test the knowledge on basic concepts in various units of the syllabus.

2.1

The overall performance of the candidates **was not satisfactory**. The average marks scored by candidates range from 1 to 1 ½ marks. The question is straightforward and it clearly requires the candidates to calculate the labour cost of the repairmen attached to the repair centre from the **employer's (i.e. repair centre) perspective**. However, a handful of candidates (8% - 10%) had taken the employees contribution to the **EPF of 8% of the earnings**.

Some candidates (about 30% - 40%) had taken 22 days as working days per month per repairman whereas the question clearly states that the workers are entitled to take 2 days **paid leave** per month and thereby erroneously arrived at the cost of lunch for 22 working days. Many candidates had not arrived at the correct labour cost per repairmen hour in order to estimate the total cost of labour for the given job that requires 28 repairmen hours.

This was based on a small scenario and candidates were required to calculate the labour cost based on job costing.

Although it was clearly mentioned that the particular job required 28 repairmen hours several candidates have calculated based on 28 repairmen days.

Several candidates have deducted the EPF and ETF cost from the salary (20% of 40,000 deducted from 40,000). Some candidates have deducted 8% from the salary considered for the calculation. Some candidates have ignored 3% ETF in the calculation. These flaws highlighted the fact that many candidates do not possess a clear understanding regarding ETF & EPF calculations.

Majority of the candidates failed to calculate the number of working hours per month correctly. Many have considered 22 days x 10 hours as the number of working hours.

Majority of the candidates did not score well on this sub question because they failed to abstract the information and understand the question well.

2.2

The question is very simple and requires the candidates to calculate economic order quantity (EOQ) and the total annual ordering cost. Majority of the candidates (about 80%) had calculated EOQ correctly and scored 2 marks out of the 3 allocated to such part. Very few of the candidates (about 3% to 6%) had displayed that they were not familiar with the formula used to calculate the economic order quantity. The overall performance on the computation of EOQ was however satisfactory.

Students have correctly substituted the numbers in the EOQ formula. But some have failed to obtain the square root of the number in arriving at the final answer.

Some candidates have calculated the holding cost instead of total annual ordering cost.

Some candidates (about 5% to 8%) had calculated the total annual ordering cost incorrectly as they have arrived at the **ordering cost by multiplying the EOQ** by cost per order and failed to understand that **annual ordering cost depends on number of orders** to be placed in the given period.

Overall performance of the candidates for the part was satisfactory. On average, candidates had scored 2 – 2 ½ marks out of the 3 marks allocated to the part.

2.3

Performance of part (a) of the question was very poor. Except for very few candidates all other candidates did not possess any idea about assessing the variability on an absolute basis and have not attempted part (a).

For part (b) of this question many candidates have calculated the coefficient of variation in assessing the variability relative to mean. But majority has just performed the calculation and had not determined which remuneration indicates the greater relative variability. This proves that the candidates did not pay adequate attention to what the examiner expected from the action verb “assess”.

Overall performance of the candidates **was not satisfactory**. Average marks scored by the candidates ranged from 1 to 1 ½ marks. Majority of the candidates (about 60% - 70%) appeared not to be familiar with the word “**relative**” and had not properly answered the question **comparing the coefficient of variance (CV) with the absolute standard deviations** already computed by the examiner for the candidates to interpret and discuss appropriately and briefly.

The candidates had failed to understand that CV measures, to what extent observations are dispersed (i.e. **deviation** from the average monthly remuneration of the division) **relative to its mean** which might be useful to the management of the manufacturing entity to design an equitable compensation scheme for both divisions. Majority of the candidates (about 60% - 70%) appeared to **have memorized the formula** without understanding the **usefulness of calculating the CV** as they failed to answer part (b) of the question. Out of those who had attempted to answer part (b), only a **negligible number** (about 1% to 2%) of candidates have been able to score the full marks allocated to part (b) of the question.

2.4

In this question the examiner has tested the knowledge in probability. Only a handful of candidates had obtained full marks for this part. The following flaws were identified.

Many candidates have calculated the probability of the item being defective from each machine separately, but majority has failed to add the two figures to arrive at the probability of the item being defective.

Only a handful of candidates have arrived at the final answer of the ‘picked’ defective item being an item produced from machine ‘X’. They have carried out the computation calculating only the probability of the item being defective.

This shows that majority of the candidates have not understood correctly what is expected from the question.

The performance of the candidates **was not satisfactory**. The average marks range from 1 mark – 1 ½ marks. Considerable number (about 40% - 50%) of candidates had failed to **calculate the first condition** (i.e. an item produced from machine X being defective) of the conditional probability.

Majority of the candidates (about 50% to 60%) who had attempted the part had merely **drawn tree diagrams for probability without calculating the corresponding probabilities** attached to relevant trees. However, some candidates (about 20%-30%) had correctly calculated the corresponding probabilities and arrived at the final answer for the first condition.

An insignificant number of candidates (about 2% - 5%) has been able to correctly calculate the **probability of an item being defective which might be produced by either machine X or Y**, which is required to arrive at the conditional probability of an item being produced by Machine X.

2.5

Though the question seems simple and straightforward, the performance of the candidates **was not satisfactory**. The average marks range from 1 – 1 ½ marks out of 3 marks allocated for this part of the question. The question **primarily** tests the ability of the candidates to understand the **time value of money**. Majority of the candidates (about 60% - 70%) had suggested option 1 as the best investment without taking into account the **present value** of interest **received at the maturity** at the rate of 10% per annum (together with principal) under option 1.

Only one candidate was able to identify the **reinvestment opportunity** of the interest **received upfront** under option 2 and demonstrated with an excellent discussion on the usefulness of time value of money in financial decision making.

Some candidates (about 20% - 40% of those who have attempted) had just mentioned option 2 is most viable **without appropriate justification**. Some candidates had just mentioned “option one is good but we have to consider time value of money” without any reason or analysis being given or carried out.

2.6

Examiner has sought to test the knowledge of absorption costing vs. marginal costing. The following weaknesses were observed.

The examiner required candidates to ‘List’, but some candidates have wasted their time on lengthy explanations.

Some candidates have reported the same fact, that absorption costing involves ‘fixed production cost’ in all the three points.

Some candidates have incorrectly stated that marginal cost involves fixed production cost.

Average performance of this part was satisfactory. Majority of the candidates (about 60% - 70%) had listed and discussed some **factors supporting the product valuation using absorption costing** over marginal costing.

However, some candidates (about 10% - 30%) had given some irrelevant comments such as there might be variability in budgeted cost and the standard cost. A handful of candidates (about 5% to 10%) had **distinguished absorption costing from marginal costing** displaying **poor discipline in reading and comprehending** the requirement of the question.

On average, overall performance was satisfactory.

2.7

This question required the candidates to state 3 problems when using standard costing.

The following weaknesses were observed

Many candidates have written irrelevant and incomplete answers such as inflation, exchange rate fluctuations and interest rate changes only focusing on the words “modern environment”.

Many candidates have written general answers such as “standard costing involves high cost”, and “difficult for management”.

These flaws highlight the fact that the candidates should have a clear and comprehensive knowledge about these concepts.

Majority of the candidates (about 60% - 70%) scored more than 1 mark.

A noticeable number of candidates, 10% - 15%, had attempted to explain the **meaning of standard costing** and **give examples** for standard costing instead of **identifying the problems** that the companies face when using standard costing in the modern environment.

However, a handful of candidates (about 2% - 5%) had brought some **practical problems** relating to standard costing **in modern environment**, into debate and had scored the full marks allocated to the part. These candidates appeared to have a good knowledge about standard costing.

2.8

Overall performance **was satisfactory**. It is surprising to note that a large number of candidates (about 70%-80%) had computed the **NPV correctly to the appropriate approximation** and scored the full marks allocated to the computation.

However, a considerable number of candidates (about 30% - 40%) had failed to arrive at the Internal Rate of Return (IRR) to the appropriate approximation as they appeared to have **not understood how the IRR is computed** and some candidates had just “**plugged**” **NPV values into the formula incorrectly** without completing this part.

Few candidates (about 1% -3%) had computed the **Accounting Rate of Return (ARR)** instead of **IRR** and failed to secure any marks.

Overall, average marks obtained for the part range from 1 ½ - 2 marks.

2.9

The overall performance of the candidates **was not satisfactory**. The average marks scored by candidates range from 1 to 1 ½ marks. The question tests the candidates’ knowledge about **quantitative techniques relating to profit maximization**.

A number of candidates (about 30%-40%) had failed to understand and consider the **relationship between products X and Y in terms of generating contributions** and thereby lost momentum in approaching the correct answer. Some candidates (about 10% - 20%) had computed the **first derivative of total contribution function** when $Y = (42X - 2X^2 - X^3/3)$ **without incorporating the relationship $3X = 1Y$** and had scored **some marks** allocated to the part.

Only a few candidates were able identify the contribution maximizing output levels of products X and Y accurately and came up to the expectation of the examiner.

2.10

In this question the following weaknesses were observed in the answers.

- (i) Candidates have not multiplied the unit cost function by number of units to arrive at total cost. Some candidates have taken “Q” as the number of units whereas the examiner has clearly stated that number of units is “X”.
- (ii) Several candidates have not arrived at revenue function by multiplying by X.
- (iii) Some candidates have failed to understand that profit means “TR-TC”. They have also made basic arithmetical mistakes when deducting “TR” from “TC”.

Overall performance was **somewhat satisfactory**. A few candidates (about 4% - 8%) had correctly identified the total cost, total revenue and profit function accurately whereas some candidates had divided instead of multiplying **cost function by X**.

Also, some candidates (about 2% - 3%) had not arrived at the **total revenue function correctly** as they had **multiplied the demand function for the product by P** without giving any reason as to why such multiplication is necessary when **demand function could be rearranged capitalizing P**. Considerable number of candidates (about 40% to 50% of those who have attempted) had not arrived at the **profit function correctly** and many candidates had just mentioned **Profit equals total revenue minus total cost, i.e. words, $P = R - C$** , in their own words.

Average marks obtained for the part range from 1 ½ to 2 ½ marks out of 3 marks allocated to the question.

Section 02

Question 03

- (a) The overall performance of the candidates was satisfactory. Majority of the candidates scored 2 ½ marks to 3 marks out of the 4 marks allocated to the part. The question tests the ability of the candidates to demonstrate and identify the relevant cost. Majority of the candidates had identified the variable cost pertaining to the order and had accurately taken this into the computation of total cost of the order. A few candidates had incorrectly charged fixed administration overhead (5% of production) on variable production cost. A handful of candidates (8% - 10%) had not calculated the direct labour usage which is used to estimate the fixed production overheads. Very few candidates (about 3% to 4%) had not taken the initial cost of the development of graphics and printing plates into the computation of the total cost of the order, on the basis that it is ‘sunk’. Such candidates had failed to understand initial cost of the development of graphics and printing plates is relevant for the management to decide on the acceptance or rejection of the order.

Majority of the candidates had calculated the profit margin on the total cost whereas very few candidates had applied profit margin on the selling price where the question very clearly states that the mark up is on total cost.

On average, fair number of candidates had computed unit (per copy) selling price which is used to advise the management on acceptance/rejection of the order. Alternatively, some

candidates had taken total sales values expected under the company policy and the total cost of the order and had advised the management correctly.

- (b) The overall performance of the candidates was very poor. The average marks obtained by candidates ranged from zero to $\frac{1}{2}$ a mark and hardly a candidate scored 1 mark out of the 2 marks allocated to this part. It was observed that the candidates had misinterpreted the requirement of the question as to the computation of breakeven quantity of copies instead of computing minimum number of copies to be printed if JPP is to accept the offer, in accordance with the company's pricing policy.

None of the candidates scored full marks for part (b) of the question and only a very few (1% - 2%) of the candidates had been able to identify the variable cost per copy which is used to compute the minimum number of copies to be printed if JPP is to accept the offer, in accordance with the company's pricing policy. Some candidates had divided the total cost by unit price (price per copy of Rs. 500) offered and suggested as the minimum number (breakeven) of copies (i.e. their interpretation of break-even point) to be printed if JPP is to accept the offer, displaying very poor knowledge of management accounting.

A handful of candidates (3% to 4%) had been able to list some but not all the variable costs relevant to the printing job and had scored a small fraction of the marks allocated to this part of the question.

- (c) Again, overall performance of the candidates was poor. Average marks score by the candidates ranged from zero to $\frac{3}{4}$ th of a mark. The question seemed simple and tested the candidates' ability to understand the types of costs which vary with the number of copies produced and advise the management on whether the contribution could be increased with volume increments, without any capacity expansion.

A very small number (1% to 2%) of the candidates had been able to score the 2 marks allocated to the question. A very few (about 1%) of the candidates had brought some good arguments to the discussion by referring to the workings in part (a) and scored a decent amount of marks.

Majority of the candidates had failed to identify the variable costs pertaining to the order and the contribution on which appropriate advice to the management can be put forward.

- (d) The performance of the candidates was average i.e. ($\frac{1}{2}$ mark – 1 mark). A considerable number of candidates had failed to demonstrate the key distinguishing features of batch costing and contract costing i.e. time taken to recognise revenue, scale etc.

Some candidates had made irrelevant and general comments where there were enough opportunities for the candidates to demonstrate the key factors that distinguish contract costing from batch costing.

A handful of candidates had successfully discussed some practical aspects that distinguish contract costing from batch costing and scored a good proportion of the marks.

Question 04

The question sought to test the knowledge on normal distribution and its applications. This was an optional question and it was observed that many candidates have not opted to attempt this question. The performance of those who attempted the question was on the whole average.

- (a) From part (a) it was expected to estimate range of monthly profit in the given scenario at 95% of confidence level. It was observed that several candidates have not attempted this part (a) and have answered the remaining parts of the question. Many of those who have attempted the questions have scored more than half of the total marks allocated.

The following common mistakes were observed in answering this part

- Several candidates have ignored the fact that they have to estimate the mean value of the given population by standard deviation of sample means. Therefore, they have applied standard deviation of the sample Rs. 1,200 without calculating standard error of mean ($1200/\sqrt{36}$) in estimating the monthly profit at 95% confidence level.
- Further it was observed that a handful of candidates do not possess the basic knowledge regarding the normal distribution curves. That is they do not know how to refer the table “area under the standard normal curve” at 95% of the confidence level. They have taken some wrong values such as 0.095, 0.2224 instead +/- 1.96 in their answers.
- Majority of the candidates have not multiplied the answer by the value 10,000 in estimating the range of total monthly profits and therefore have earned less marks. It was observed that many candidates have done all the steps correctly up to this point and have stopped without estimating the total population.

The candidates’ performance was fairly satisfactory.

- (b) In this part the examiner has given a condition that in the given scenario management has decided to discontinue retail shops having monthly sales less than Rs. 75,000. It was required to estimate the number of such shops. The performance was poor on the whole.

The following mistakes were observed

- Majority of the candidates have directly taken the standard deviation of monthly sales for the sample (Rs. 72,000) without computing the standard deviation on the 10,000 shop population ($72,000\sqrt{36}$).
 - Many candidates have correctly taken the difference between value of the variable under consideration and the mean in obtaining the Z value.
 - A handful of candidates lost marks because of the poor knowledge in referring the values from the table “area under the standard normal curve”. These candidates have directly deducted the value of Z score from 0.5 or 50% without taking the corresponding proportion.
 - In this part served the majority of the candidates have ignored the fact that they have to estimate the number of shops to be closed using a 10,000 shop population and lost marks.
- (c) The candidates who have scored well in part (b) have scored well in part (c) too since this part is based on a similar approach. The common errors referred to in part (b) were observed in part (c) as well.
- (d) Performance of this part was very poor. Many candidates have failed to see the link between part (c) and part (d). A minimal number of candidates only scored some marks for this question.

- The candidates who had erroneously applied the standard deviation as Rs.72,000 had got the answers as more than (1% of 10,000) 100 shops. Therefore they were confused and have not answered this part.
- A handful of candidates have not multiplied the cost for exclusive branding (Rs.250,000) because they have failed to pick the information from part (c).

General comments

- Candidates should read the entire question carefully to pick up each and every crucial information before answering.
- In all four parts some careless mistakes were observed in computation as well as in copying the details from the question paper.

Question 05

General comments

This question had the highest average marks on the paper.

It is a three part question that tested the candidates' understanding of the standard costing section in the syllabus. Part (c) gives a scenario where actual utilisation of raw materials differs from the purchased quantity of raw material during the month. Candidates were required to calculate the material price and usage variances, and also direct labour rate and efficiency variances.

For part (b) and part (c) respectively candidates are required to state two causes of material usage variance and two actions to improve the direct labour efficiency variance respectively.

Specific comments

- (a) In calculating the material price variance, a disappointing number of candidates, had taken the material utilised instead of the actual quantity of material purchased. Many had calculated the rate variance by simply following the difference in actual and standard rates without multiplying by the actual hours.

Some had failed to mention that the variances calculated are either favourable or adverse.

- (b) Many candidates have done well in giving causes of material usage variance. However, a few had tried to answer it by describing the material usage variance formula and thus failed to obtain any marks.
- (c) Satisfactorily answered by majority of the candidates.

Question 06

General comment

Majority of the candidates had not attempted the question. This may be due to not being able to cover activity based costing in their studies. A significant number of those who attempted had obtained zero marks also supporting this surmise. Average marks obtained by those who attempted is 2.3.

Specific comment

- (a) Candidates were required to calculate the fixed production overhead cost per output unit, based on standard absorption costing system and the ABC principle. Many had erred in calculation of both fixed overhead costs. Common mistakes made were;
- (i) Failure to convert minutes into hours.
 - (ii) Dividing the cost of each activity by the driver utilization by each product, e.g. machinery cost per hour for products A = Rs. 2.5 m, product B = Rs. 2.5m
2,500 10,000
 - (iii) Incorrect calculation of number of units for each product.
 - (iv) Shortening of the calculations thousands and millions incorrectly interchanged.
 - (v) Arriving at the machine cost per unit of a product by dividing the machine cost per hour by labour time per product etc.
- (b) Many of the answers given for part (b) were not relevant.

Section 03

Question 07

The answers to this question varied. Although some candidates provided good answers, more than half the candidates failed to score 50% of the marks allocated to the question.

The question consisted of four parts and tested the candidates' knowledge of forecasting sales (using the trend equation and seasonal variation index values), the high-low method and budgeting.

In part (a), candidates were required to prepare the seasonally adjusted quarterly sales forecast, in units and in value for year 3.

Part (b) required the candidates to calculate the estimated variable cost per unit and fixed factory overhead per quarter using the high-low method.

The requirement in part (c) was to prepare the production budget (in units), factory overhead budget (in value) and raw material purchases budget (in value) for the first three quarters of year 3.

Part (d) required the candidates to prepare the cash budget for the second and third quarters of year 3.

Parts (a) & (b) of the question were the best answered.

In part (a), a significant number of candidates had used time periods of 1 to 4 (which are relevant to year 1) for x in the trend equation, instead of 9 to 13 relevant to year 3.

Many candidates after calculating the quarterly trend sales, ignored the seasonal adjustment. There were candidates who had substituted the seasonal variation index value for x and some others had multiplied the time period substituted for x by the seasonal variation index value. Some of the candidates had added the seasonal variation index value to the quarterly trend sales, although the question states that the multiplicative model is used.

In part (b), some candidates had failed to use both the highest and lowest levels of production in calculating the estimated variable factory overhead cost per unit. Some candidates had used the highest level of production of 50,000 units and 18,000 units in the variable factory overhead cost per unit calculation. A few candidates, after identifying the lowest level of production of 15,000 units correctly made the mistake of using the lowest factory overhead of Rs. 21M instead of Rs. 25M

applicable to 15,000 units of production, in calculating the variable factory overhead per unit. Further, many candidates failed to remove the step up cost of Rs. 7M included in the year 2 quarter 4 factory overhead of Rs. 67 M.

In part (c), many candidates failed to prepare the factory overhead budget, although they had calculated the variable factory overhead per unit and fixed factory overhead per quarter in part (b). Of the candidates who had prepared the factory overhead budget, many failed to include the step up costs.

In preparing the production budget, some candidates had failed to correctly identify the opening finished goods stock of quarter 1 of year 3 as 20,000 units, instead calculating the finished goods opening stock as 25% of year 3 , quarter 1 sales.

In preparing the raw material purchases budget, some candidates had failed to identify the opening raw material stock of year 3, quarter 1 as 40,000 units and many candidates failed to calculate the year 3, quarter 3 closing raw material stock correctly.

In part (d), in preparing the cash budget, although the question states that variable factory overheads are paid in the same quarter, many candidates had incorrectly calculated the payment of variable factory overheads to be 80% in the same quarter and the balance 20% in the following quarter. In calculating the labour payments some candidates had used sales units instead of production units. A few candidates had prepared the cash budget for the first and second quarters of year 3.

A few candidates provided excellent answers for all parts of the question.

Examiners' Comments

Executive Level Examination – September 2015

Fundamentals of Taxation and Law (KE3)

Part A

Fundamentals of Taxation

Section 1

Question 01

The candidates were required to choose the most appropriate answer in this 5 part multiple choice question.

Overall performance of this question was unsatisfactory. Majority of the candidates scored 40% or less of the total allocated marks. Only a very few candidates (less than 10%) scored 80% or more of the allocated marks.

The question tested areas in the Inland Revenue Act, Value Added Tax Act and Nation Building Tax Act.

The question was well within the syllabus and the subject matter tested is adequately covered in the study pack published by CA Sri Lanka.

Q. 1.1 Majority of the candidates furnished the correct answer to this question relating to identifying the “resident” status of a company or individual for the purposes of the Inland Revenue Act.

Q. 1.2 Majority of the candidates were ignorant of the tax treatment of interest received by a company in respect of which withholding tax has been deducted.

Q. 1.3 Many candidates appeared to be confused as to the meaning of the words “business” and “child”.

These words are defined in the interpretation section 217 of the Inland Revenue Act and candidates cannot answer questions of this nature without a proper understanding of the definitions.

Q. 1.4 All registered persons are required to pay VAT even if the value of taxable supplies per quarter is less than the threshold for registration. A good number of candidates erroneously chose option D (i.e. no VAT is payable since value of supplies is less than the threshold).

Q. 1.5 A good number of candidates were ignorant of the due dates for submission of Nation Building Tax (NBT) quarterly returns.

Question 02

Overall performance in this question was unsatisfactory. Majority of the candidates scored 40% or less of the total allocated marks. Only a very few candidates scored 80% or more of the allocated marks. The question was within the syllabus and the subject matter tested is adequately covered in the study pack published by CA Sri Lanka.

Q. 2.1 Candidates were required to list 4 main taxes administered by the Dept. of Inland Revenue. A good number of candidates incorrectly mentioned PAYE, WHT, partnership tax, etc. as main taxes.

Q. 2.2 This question requires candidates to compute the statutory, assessable and taxable incomes of a company. A few candidates made errors of a serious nature as mentioned below:

- (i) Deducting qualifying payments (section 24 deductions) from total statutory income and brought forward losses (section 32 deductions) from assessable income.
- (ii) Claiming tax free allowance (Rs. 500,000) in the tax computation of a company.

Errors (i) and (ii) mentioned above are errors of principle and therefore are of a serious nature.

Q. 2.3 The question requires candidates to state, in order to avoid deemed dividend tax,
(a) The minimum dividend that should be distributed as a percentage of the distributable profit, and;
(b) Before when the distribution should be made.

In answering (a) above, a good number of candidates mentioned the percentage of net profits or taxable profit. This is a good example of improper reading of the question. In answering (b) above, a good number of candidates were vague in identifying the correct period. A few candidates mentioned "on or before 30th September" without mentioning the year.

Q. 2.4 The question requires the candidates to identify the time bar for an assessment where the Assessor/Asst. Commissioner rejects an income tax Return filed on or before the due date.

Here too, a good number of candidates were vague in identifying the period.

Section 2

Question 03

Overall performance can be considered as fairly satisfactory. Most of the candidates made a good attempt at the question. Majority of the candidates scored over 50% of the allocated marks. There were some excellent answers and a few candidates scored 18-19 marks out of the allocated 20 marks.

Standard of the question can be considered as reasonable at this basic level being not too difficult nor too easy. A reasonable coverage of commonly applied sections of the Inland Revenue Act in the income tax computation of an individual who is a professional was seen. However, the question tested only two sources of income, namely, employment and trade. Inclusion of a few other common sources of income like rent, interest etc. would certainly have enhanced the standard of the assessment. The question was well within the syllabus and sections tested are adequately covered in the study pack published by CA Sri Lanka.

Most candidates displayed good application skills in the construction of the structure and in identifying the contents of an income tax computation of an individual.

Majority of the candidates demonstrated sound subject knowledge in the application of income tax law in relation to;

- Computing the statutory income from employment and trade.
- Sections 25 and 26 of the Inland Revenue Act: allowable and disallowable expenses and charges.

Where mistakes were made, these generally related to:

Lack of subject knowledge

Employment income –

- (i) Vehicle benefit. A good number of candidates stated that the use of one vehicle is exempt without mentioning the limit to the exemption (viz. Rs. 50,000 per month).
- (ii) Reimbursement of telephone bills: a few candidates disallowed 100% of the expense.
- (iii) Second employment – A good number of candidates mentioned (correctly) that this does not become part of the statutory income since VAT has been deducted.

Business income

- (i) Blood pressure meter; only a very few identified that the profit on disposal is not taxable since no capital allowance thereon has been claimed. Majority of the candidates treated the new meter as a qualifying replacement and (correctly) claimed depreciation allowance thereon accordingly.
- (ii) Foreign travel – Very few candidates mentioned that 100% of the accommodation expenses are allowable for tax purposes. A good number of candidates displayed lack of knowledge relating to the limit applicable when claiming foreign travel expense for tax purposes.
- (iii) Salaries paid to wife – Majority of the candidates erroneously disallowed this expense in ascertaining the adjusted trade profit. Only a very few candidates knew that the salary paid to wife is deemed to be the income of the husband (section 25 (6))
- (iv) Depreciation allowance - It was surprising that a good number of candidates did not know the depreciation allowance rate applicable to equipment.
- (v) Qualifying payment - Medical insurance covering incurable diseases; A good number of candidates did not know that 100% of the premia can be claimed. Most of the candidates added this to life insurance premia and applied the limitation to the claim.
- (vi) Calculation of income tax - A good majority of the candidates are ignorant of the recent amendment (section 59F) which is effective from Y/A 2014/15 relating to the taxation of professional income.

Part B

Fundamentals of Law

Section 1

Question 04

A fair percentage of candidates were capable of identifying all the correct answers out of the 4 alternatives given under parts (1 – 5) and earned 100% marks. These candidates had selected the following correct answers as they have a satisfactory knowledge of the subject area tested.

- 4.1 It must be passed by Parliament as a subordinate legislation. They know it is not a required condition for a custom to be recognised as a source of law by the courts of Sri Lanka.
- 4.2 “Placing an order with an artist to draw your portrait is a contract for work and materials”. As far as Sale of Goods Ordinance No. 11 of 1896 is concerned all the other 3 statements are not correct.
- 4.3. When a function is conferred on an agent of the state by a written law and that agent commits a delict while performing such function the state is liable. “Under the other 3 instances the State is not liable since those cannot be considered as delicts done by the parties as an agent of the State.
- 4.4. To terminate the hire purchase agreement at any time. “The other 3 facts under the “umbrella” of obligations of the hirer.
- 4.5. The theft was an inevitable accident. The other 3 instances are defences in Law for theft but when the theft is an inevitable accident the law does not recognise it as a defence for the thief.

Very high percentage of candidates were capable of identifying the correct answers for the first 4 parts of the question. However, they were not sure of the correct answer for part 5 where they had been confused by the statement given under D, i.e. the thief had the intention to return the property back to the rightful owner.

There were many who were not sure about the correct answers and had furnished answers on a “hit or miss” basis expecting to earn some marks as a matter of chance.

Question 05

- 5.1 This question on basic principles of Law of Contracts can be answered by an average accountancy candidate who has a basic knowledge in Law of Contracts. A very few candidates had furnished satisfactory answers which deserve reasonable percentage of marks. In their answers they had correctly discussed relevant rules applicable to a valid acceptance such as:-
 - Acceptance must be made when the offer is still in force.
 - Acceptance must be absolute.
 - Acceptance must be unconditional/unqualified.
 - Acceptance must be communicated to the offeror and so on. Majority had given one or two rules since they were not fully conversant with all the 4 criteria mentioned above.

There were other candidates who had failed to understand the question correctly and had focused their answers in various incorrect directions and had furnished answers like:-

- i. " The person when accept the offer he should aware of it.
- ii. The acceptance should be made through prescribed manner and it is not prescribed must be accepted in a reasonable manner.
- iii. If there is a valid contract here should be 2 parties to it and if there is no any implied authority acceptance should be in writing.
- iv. Acceptance must be made in good faith.
- v. If there is a valid contract there must be a consideration.
- vi. Acceptance must be made by the offeree or by an agent of the offeree and after the acceptance he cannot reject it.
- vii. Acceptance can be made by an agreement, by performance or by conduct legally.
- viii. If something happened to it, it is treated as breach of contract" and so on and wasted their time.

5.2 Another easy question on sale of goods covering the transfer of the title of goods from seller to the buyer. A few had furnished some satisfactory answers as they are familiar with the subject area. In their answers they had included the following points.

- i. There is an implied condition that the seller has a right to sell the goods at the time of passing of the property in goods to the buyer.
- ii. There is an implied warranty that the buyer will have and enjoy quiet possession of the goods.
- iii. Another implied warranty is that the goods will be free from any circumstances or charge which are not known to the buyer at the time of sale.

These answers deserve a higher percentage of marks as they cover the implied conditions and warranties regarding passing of the title of the goods from seller to the buyer.

But the majority of the candidates had failed to understand the question correctly and as a result they had furnished irrelevant/incorrect answers. One important point that could be observed is that in their answers majority had failed to note that the question is on terms in relation only to title to the TVs. Therefore they had built their answers based on all the conditions and warranties which are implied in a sale of good as laid down in the Sale of Goods Ordinance No. 11 of 1896 without limiting them to the title to goods.

Many others had written various completely irrelevant answers as they have failed to understand the question. In their answers they had dealt with some areas like;

- i. There is an implied condition in an agreement to sell i.e. the seller and buyer will come to a selling agreement.
- ii. If a condition is violated it is a breach of the contract and if a warranty is violated it is not a breach of the contract.
- iii. Usual agreement of sales refers to a form of implied authority which relates to a certain type of sales.
- iv. It is treated as a breach of a condition only when there is prescribed period for sale and if a warranty is breached it is treated as if there is no prescribed period for sale.
- v. Under the following circumstances it is treated as breach of condition/warranty.
 - If the TV is not working properly – breach of condition
 - If the TV is not the brand as agreed – breach of condition
 - If the TV does not have remote control – breach of warranty

- vi. Explained what an implied condition is and what implied warranty is.
- vii. When the goods are sold under the description goods should be according to the description, and when goods are sold under sample they must tally with the sample.
- viii. The goods should be fit for the intended purpose.

5.3 Only a handful of candidates had furnished some satisfactory answers which were expected by the examiner and they had dealt with some relevant areas such as:

- To encourage foreign and domestic investors.
- To assist investors at all the stages of the process from application to the commercial operation stage.
- To establish and manage export processing zones which are available to investors to set up industrial and commercial enterprises.
- To diversify the sources of foreign exchange earnings and to increase the export income.

But the majority of the candidates were not familiar with the main functions of BOI and had written in a general way what they had assumed to be main functions of BOI. In their answers they had mentioned the following functions:

- i. To provide funds to local investors/businesses. Provide securities for the local investors and provide for and protect local investor under BOI.
- ii. Discourage investments which are undesirable to society.
- iii. To control, regulate and monitor the financial investment companies in Sri Lanka.
- iv. Help to develop the economy of the country and avoid unethical and prohibited businesses & investments in the country.
- v. The primary function is to raise funds for public expenditure & social functions.
- vi. Reduce the income disparity between rich and poor. Increase economic functions.
- vii. Protect local industries from foreign companies.
- viii. BOI makes rules for every investment in Sri Lanka and contract investments.
- ix. To collect all the revenue such as customs duty excise duty etc.
- x. Providing subsidies to relevant investors and observing investment development in Sri Lanka and so on.

5.4. Question requires the process of mediation to be summarized or in other words to briefly explain the procedure followed in the method of alternative disputes resolution. Only a very few candidates have some idea about the process of mediation and had furnished some satisfactory answers which deserve reasonable marks. In their answers they had included the following important steps followed in mediation.

- i. Disputing parties appoint a neutral outside party as the mediator.
- ii. Process of the mediation is decided by the mediator and the parties collectively.
- iii. Each disputing party lists out the key issues of the dispute and submits these to the mediator and to each other.
- iv. Thereafter the mediator makes his decision on the dispute which is not binding on the parties involved as they can decide whether to accept or not.

Out of those few some had explained the entire process correctly whilst some others had explained only a few of the prescribed steps.

However majority had no knowledge of the process of mediation and tried to explain the procedure based on their own assumptions and explained several incorrect areas such as;

- i. Mediation is for criminal cases held in the villages and cities to give judgment for disputes.
- ii. Mediation reduces the work load of the high court.
- iii. Mediation is relevant for minor criminal cases.
- iv. In mediation there are some authorized persons to handle the matters relating to disputes.
- v. Mediation is a method of dispute resolution where the information on disputes is disclosed to the media.
- vi. The mediator will identify and analyse the disputes on the basis of information made available to him and makes his decision.
- vii. Mediator will analyse the dispute explain the position of the dispute to the parties concerned and finally refer it to the courts for the final decision.

They have furnished those irrelevant answers as they had failed to understand the question properly and due to the poor knowledge of the subject area indicating that they have not studied the Mediation Board Act No. 72 of 1988 or the relevant study text for Executive Level which has clearly explained the process of mediation.

- 5.5. This part of the question seeks to test the knowledge of the purpose of registration, the manner of recording and validity periods including the renewal of an Industrial Design as explained in the Intellectual Property Act No. 36 of 2003. Only a handful of candidates had understood the question correctly and had tried to furnish the answer under the 3 sub headings as required by the question. Out of them, majority had dealt with the purpose of registration and validity period and the possible renewals of the registration. In their answers they had stated some areas such as;

- i. The main purpose of registering industrial design is to give exclusive ownership of the industrial design.
- ii. The registration is valid for 5 years initially from the date of the application for registration.
- iii. Subsequently this term can be renewed for 2 more consecutive 5 year terms at the discretion of the inventor/designer.
- iv. All the registered designs will be recorded in the register kept for the purpose.

Majority of the candidates failed to furnish acceptable answers under 3 sub headings as required by the question they had furnished some completely irrelevant answers which had not dealt with the areas expected by the examiner. In their answers they had covered some areas such as;

- i. The purpose of registration is to encourage industrial design.
- ii. The purpose of registration is to encourage the production of more and more intellectual proposals like software new products etc. that are 'safe'.
- iii. The purpose of registration is to avoid the unauthorized use of the industrial design.
- iv. The purpose of registration is to make sure that design engineers have designed properly to;
 - make sure the future of the industrial companies is safe.
 - make sure of increasing production of good designs.
 - File a case in court if someone is using a design without permission.
- v. It will be registered in accordance with the appropriate field, such as industrial services, banking, transport service relating to distribution and various other business services such as medical, educational services etc.

- vi. It can be recorded by the owner of the property and it can be registered under owner's name.
- viii. It will be valid for 10 years/70 years or it will be registered for the owner's life time and so on and had wasted their time.

Question 06

Simple question based on conditions and warranties of a contract and remedies available to the affected party for breach of them. According to the question Frooty the supplier of fruits to Cookies is responsible for 3 violations/conditions/warranties and candidates are expected to identify those conditions etc. separately and recommend remedies available in Law to Cookie for each of them. Fair percentage of candidates had correctly identified all 3 violations and majority of them had correctly identified whether they are conditions or warranties or fraudulent misrepresentation and they knew the available remedies for those violations.

Accordingly they had explained following points in their answers.

- (a) First Frooty has failed to supply the required quantity of fruits for August 2015 and this is a violation of a condition of the contract. They (the candidate) had realized that one of the main conditions is to supply required quantity of fruits to the hotel and that in August 2015 when Frooty failed to supply the required quantity of fruits he violated a condition of the contract. Since it is a main term of the contract which goes to the root of the contract it is very clear that it should be treated as a condition of the contract. When violation of a condition of the contract occurs the affected party has the right to rescind the contract and claim damages. Under the given scenario Cookie has a legal right to rescind the whole contract and claim damages from Frooty for violation of a condition of the contract.
- (b) Second violation: Frooty has some fruits in August 2015 which are not of good quality. It is an implied warranty that the goods should be of good quality i.e. which are fit for the intended purpose of the buyer. Since it is not specifically stated in the contract it is treated as an implied warranty of the contract because the failure to perform it does not effect the substance of the contract. For violation of a warranty the affected party has no legal right to rescind the contract but can claim damages for the violation.
- (c) Third violation is that Frooty has provided false information to the buyer (Hotel) at the time of entering into the contract with the intention of inducing the Hotel to enter into the contract in respect of his capacity to supply the required quality of fruit to the Hotel for the agreed period. Since Frooty has made this statement with the purpose of inducing the other party to enter into the contract knowing that it is a false claim it amounts to a fraudulent misrepresentation under the Law of Contracts. For such type of violation the affected party has one of the following remedies.

“Rescind the contract, claim damages, refuse to further perform the contract or affirm the contract if it wishes to do so”.

The candidates who had directed their answers in this way earned a high percentage of marks since they had disclosed their knowledge in the subject area and also indicated that they have correctly understood the question.

However a small percentage of candidates had failed to understand the question correctly and failed to furnish their answers in this way and had wasted their time to explain some areas such as:-

- i. Frooty has breached the conditions on sale of goods. The goods should be for a specific purpose and they should be of merchantable quality. It is a condition in law and the affected party can refuse further performance of the contract or sue for specific performance.
- ii. As the fruits were delivered on an instalment basis and when the goods are supplied in instalments demand for the goods cannot be met. The innocent party can refuse to pay for future goods.
- iii. The goods should be of a standard and quality which were expected by the buyer.
- iv. A sales contract means an agreement enforceable by law made by one or two parties. This is governed by law of contracts and since they have entered into the contract in writing it is an advantage to the innocent party in taking action against the other.
- v. The agreement is the foundation of a contract, but in this case because of misrepresentation by one party there is no agreement.
- vi. In the given scenario Frooty is the offeror and Cookie is the offeree. Frooty has offered uncertain or vague terms to offeree by providing false information. Therefore, the contract is void due to the uncertain offer made by the offeror to the offeree.
- vii. Frooty has provided false information at the time of entering into the contract and the agreement between the two parties becomes void as Frooty has given false information to Cookie from the beginning.
- viii. If Cookie has already paid money for the fruits he can ask for a refund of the money he had paid for the goods and he can stop buying further fruits from Frooty.
- ix. Cookie has legal rights to withhold payments to Frooty since Cookie is the innocent party and the contract can be discharged due to frustration.
- x. Under law of contracts in sale of goods the valid element is that there should be some fulfilment by both parties. Otherwise it is a violation of the conditions of the contract. The fulfilment include the following –
 - there should be capacity to contract.
 - there should be valid offer and acceptance.
 - there should be genuine consent between the two parties and so on.Some others had explained the circumstances under which a contract can be terminated, or discharged.

Question 07

- (a) The majority of candidates had understood part (a) of the question correctly, and presented satisfactory answers and their knowledge on duties of partners is satisfactory. It may be due to partners' duties towards the partnership are known to many average accountancy students since that area is generally covered in partnership accounts. In their answers they had covered relevant areas such as;
- Every partner should render true accounts and full information on all the details affecting partners/partnership.
 - Every partner should account to the partnership any benefit derived by him without the knowledge of other partners from any transaction concerning the partnership.
 - Every partner must disclose any secret profit he makes in dealing with the partnership and account for the profit to the firm.

Also they were capable of connecting these duties with the violation of duties by Bunty in the given scenario and had explained that;

- Bunty has breached the duty of rendering true accounts and providing full information about his dealings in the purchase of goods for the partnership.
- Secondly Bunty has violated the duty of accounting to the partnership, the benefit he derived without the knowledge of the other partners as he has given some of the complimentary gift items to his children without informing the other partners.

However, there were many others who did not have a satisfactory knowledge and failed to furnish acceptable answers to this easy question but had dealt with some areas such as:

- Explained as to what is a partnership and various ways by which a partnership could be formed, the purpose of forming a partnership and certain parts of the Partnership Ordinance.
- Some others had expressed the view that Bunty had purchased a large quantity of goods that is too much for the partnership and by doing so he had breached a duty of his as a partner.

- (b) Part (b) of the question is based on collective and joint liabilities of partners and this area too is familiar to any average accountancy student. But only a minor percentage of candidates had displayed satisfactory knowledge in the area tested. They had correctly identified that Chandy had lost the money while he was performing his duties as a partner and therefore all the partners are equally liable for the loss and Chandy is only liable as a partner and not as an individual. Under the circumstances all the partners/partnership have/has to bear the loss. Some of them had correctly explained that under the partnership law every partner is considered as an agent of the firm and his fellow partners for the purpose of the partnership business.

Therefore the acts of every partner in carrying on business of the firm in the normal course of business of the partnership will be binding on the firm and other partners. Accordingly Chandy has collected a sum of Rs. 700,000 from Dandy as an advance on behalf of the firm and as an agent of the firm in carrying on the business of the firm in the normal course for which all the partners are liable and not Chandy personally. Also Chandy is in charge of sales of the firm and it is directly implied that he has authority to collect the said advance as an agent of the firm and therefore the firm is liable for the loss.

Candidates who had focused their answers on those lines obtained reasonable marks. However, majority had failed to focus their answers correctly and had dealt with some irrelevant areas such as;

- i. Repeating the question (in part) and stating that Chandy has collected an advance of Rs. 700,000 from Dandy a regular customer of the partnership for an order placed by him. This money has been pick-pocketed and he has lost the entire amount.
- ii. Dandy is a regular customer and partnership must immediately investigate whether it has actually happened.

Question 08

- (a) Question is based on sale of goods, specifically the sellers liability and the implied warranty the goods should be fit for the intended purpose. Further it covers the effects on sale of goods after testing a sample. Only a few of the candidates had understood that the packet of milk powder purchased by Brenda was not fit for Brenda's purpose since milk powder was purchased for the purpose of 'drinking' (consumption as food) and not for any other purpose for which wheat flour can be used.

Also she purchased milk powder but the packet contained wheat flour, therefore it is not in merchantable quality. Accordingly the implied warranty has been breached by Anton. Under the circumstances Brenda is in a strong position to recover damages from Anton for breach of implied warranty.

Also they have realized (correctly) that Anton has purchased the goods after testing a sample but it is a fact that the defect could not be discovered by a reasonable examination of a sample because unless he tests all 150 packets the defects in all the packets would not be discovered as they are different individual packets.

Against this background Anton has a legal right to recover damages from Titus in the following manner.

- i. To recover damages to compensate the cost he incurred in paying damages to Brenda.
- ii. For breaching an implied term of Sale of Goods in relation to Sale of Goods by sample.

The candidates who had based their explanation on the aforesaid, furnished some satisfactory answers and earned reasonable marks as they had displayed satisfactory knowledge in the subject area tested by the question.

But the majority had dealt with various irrelevant areas such as;

- i. From the point of view of Anton before he purchased the milk powder from Titus he was satisfied with the results of testing a sample. So he cannot make a claim against Titus.
- ii. There has been a misrepresentation made by Titus and Anton did not get what he had ordered. Therefore, Titus is liable to compensate Anton.
- iii. Anton can repudiate the contract due to a breach of condition and so on.

(b) Simple question to cover a popular area in insurance i.e. the principle of Uberrimae Fidei or utmost good faith which can be answered by an average accountancy candidates with his/her general knowledge. But only a handful had furnished satisfactory answers. In their answers some relevant principles had been discussed including the following.

- i. The fundamental principle in insurance law is the principle of Uberrimae Fidei or utmost good faith which imposes on the insured the duty to disclose every material fact he/she knows to the insurer in the proposal form. This enables the insurer to evaluate the risk that he is going to undertake.
- ii. In the given scenario Wilfred the insured, failed to honour this principle. His non-disclosure of material facts could have affected the insurer in deciding the risk. Had the insurer been aware of the conviction he may not have accepted the risk.
- iii. The case law Woolcott vs. Sun Alliance and London Alliance Ltd. (1978) had been quoted by them in supporting their answer.
- iv. Accordingly it appears that Wilfred has breached the principle of Uberrimae Fidei and therefore the insurer is entitled to avoid the policy and reject payment on it.

The answers on those lines deserved reasonable marks, but majority had only provided various irrelevant answers.

Question 09

- (a) Another simple question this time on Negotiable Instruments. Candidates are expected to explain the applicable legal provisions and the steps that should be followed in validly handing over a cheque received from another party to a third party i.e. how Sunil should handover the cheque received from one of his debtors to Hardy. Only a very few candidates had furnished some satisfactory/acceptable answers to this 'normal' question on Bills of Exchange. In those answers they had dealt with some relevant areas such as;
- i. This is an order cheque as the drawer had given an order to Sunil and not anyone else with direction to the paying bank that it should be realized only through a bank account.
 - ii. Even though it is an order cheque it can be 'regularised' for this purpose by making an endorsement on it.
 - iii. To be a valid endorsement it should be written on the face of the cheque itself and be signed by the endorser.
 - iv. The detail amount of the cheque should be endorsed and not part of it in terms of section 32 the Bills of Exchange Ordinance.
 - v. When the cheque has been endorsed in the aforesaid manner it could be accepted by the endorsee (Hardy) but he has to encash it only through a bank account and not over the counter.

A few others who had attempted this question were not familiar with the legal provisions applicable and procedure to be followed in a valid handing over of the cheque and had furnished some answers based on their own assumptions.

- (b) This is also a simple question for the candidates who had studied the Termination of Employment of Workmen (Special Provisions) Act No 45 of 1971. Question covers the termination of services of Scheduled Employment employees in terms of the Act. Only a negligible percentage of the candidates had attempted this question and out of them had understood the question and furnished answers to meet the expectations of the examiner. Those few candidates who are familiar with the said Act had dealt with relevant provisions of the Act including the following;

- i. Services of employees in scheduled employment can be terminated by an employee provided he has fulfilled following conditions.
 - (a) The prior written consent of the employee to be terminated should be obtained or
 - (b) The prior written approval of the Commissioner of Labour for termination of such services should be obtained.

Had the tea factory where Edgar is employed adhered to the above conditions, termination of the services of Edgar would be valid and if not it is not a valid termination. Candidates who had focused their answers on the lines detailed above had earned reasonable marks on this easy straightforward question.

But the rest of the candidates who had attempted this question were not familiar with the Act and had furnished some irrelevant answers.

General: As usually candidates failed to read the questions carefully and understand what is asked for by the questions before answering them. Grammatical mistakes and weakness in expressing themselves could be observed very often. Also there were candidates who merely repeated the question in different words or terms since they are not capable of answering those questions.

Examiners' Comments

Executive Level Examination – September 2015

Processes, Assurance & Ethics (KE4)

Section 1

General Comments

Many candidates have performed well at this sitting. Some candidates demonstrated sound knowledge of business risks, processes and audit principles. However majority failed to understand the business processes; they have mixed up business risks with audit risks. In many of the weaker scripts it was apparent that they have not studied the study text.

The examination consisted of three sections, and candidates were required to answer six questions. Section 1 contained question numbers one and two both of which were compulsory. Question one carried 20 marks and question two carried 30 marks. Section two comprises of four questions, each carrying 10 marks. Three of the four should have been attempted. Section three was a compulsory question which carried 20 marks.

It was noted that section one was popular and often well attempted. It was a deciding factor for the candidates to obtain pass marks.

A number of common issues arose in candidates' answers that contributed to the disappointing pass rate.

- Not following action verbs
- Some candidates have wasted time in writing lengthy answers
- Lack of basic knowledge of the processes
- Some have not understood the syllabus

Specific comments

Question 01

This was a multiple choice question and based on the study text.

- 1.1 Learning outcome 1.1.2
This part was answered well but there were some common irrelevant answers such as consultancy only.
- 1.2 Learning outcome 1.2.2
This was based on business processes but some candidates have chosen operational risk and internal risk.
- 1.3 Learning outcome 2.1.1
This question was not answered well which reflected that many are not familiar with the procurement process. The common errors were, requisition for purchases, and although not mentioned in the question 'review of age analysis'.

- 1.4 Learning outcome 2.2.3
Most of the candidates have answered well, but common errors such as resigned employees being paid, and delay in making salary payments were observed.
- 1.5 Learning outcome 2.2.1
Almost all the candidates have answered well.
- 1.6 Learning outcome 3.1.1
This question was based on debtor control. Although the candidates have answered well there were irrelevant answers such as remind all debtors as well.
- 1.7 Learning outcome 3.4.1
This question was based on inventory control. It was observed that candidates have not answered well. Most of the candidates have written irrelevant answers such as the person responsible not checking the goods dispatch notes with sales invoices.
- 1.8 Learning outcome 5.1.2
It was observed that some candidates have not answered well. Most of them have written irrelevant answers such as factual findings.
- 1.9 Learning outcome 5.2.1
It was observed that the candidates did not have knowledge in the areas of assurance and review reports. The common irrelevant answers were compilation of financial statements for the period and factual finding report for the period.
- 1.10 Learning outcome 5.4.1
This was based on gathering audit evidence. It was noted that the knowledge of the candidates was poor. They have written, reliable only, and, in good quality.

Question 02

This consisted of ten short questions. It was based on business risks, processes and ethics.

- 2.1 This question was based on the learning outcome 1.3.1. Candidates were expected to identify the different types of risks that an entity is exposed to, which include those arising from both the internal and external environment of an entity. This question referred to the factors in economic environment which change the economic conditions. Some candidates have identified the risks but failed to explain how those affect the economic environment. Some candidates have written irrelevant answers such as;

- Government policies
- Export policy
- Legal system
- New labour laws

Some have written the following which has no relevance at all.

- Control environment
- Risk assessment
- Information technology

In spite of such answers the overall performance was good. Most of the candidates have written correct answers. This reflects that the majority has studied the text. Answers have been planned to be brief.

2.2 This question was based on the learning outcome 1.6.3. It was expected to identify the internal control monitoring mechanism designed to ensure its effectiveness. Most of the candidates have written relevant answers, but some were unable to distinguish between the management and the board of directors. They have written the functions of the audit committee.

2.3 This question was based on the learning outcome 2.3.3. It was expected to assess the business risks connected with sub activities relating to cash management process. It tested awareness of risks in the cash collection process where the cash receipts are issued manually for all cash sales and cash is banked daily. This question was expected to check the knowledge on business risks and was relatively well attempted, with the majority of answers covering a range of relevant matters and associated procedure. It was clear that many candidates had studied this part of the syllabus. However there were several irrelevant answers as well which reflect that some of the candidates were unable to visualize the particular business risk. Some of the irrelevant answers are as follows;

- No responsible person for cash collection
- Any person can write the receipt
- No division of labour
- No bank reconciliation prepared
- Less reliability
- Less acceptability

2.4 This question was based on the learning outcome 2.1.3. Candidates were expected to identify the control activity and the business risks connected with sub activities. The quality of the answers of some candidates was quite good but some candidates were not able to identify the business risks separately from the audit risks. Their answers were based on audit risks. The scripts which carried low marks reflected lack of knowledge on business processes. Many were unable to identify the activity which is missing in the flow chart. The common irrelevant answers were as follows;

- GRN
- Delivery order
- Bill of lading
- Shipping documents

2.5 This question was based on the learning outcome 2.5.2 and on business risks connected with sub activities relating to the inventory management. It attempted to test two areas which address the access control and dispatch of goods on authorized requisition.

Access control- It attempted to test the risks that the entity intends to address. Many candidates have written that restricting access to the retail stores prevents stealing. They were unable to think beyond that if, they had referred to the study text they could have given more appropriate answers. Most of them were unable to identify the risk of physical control of inventory items.

Goods dispatched on an authorized requisition-Many candidates were unable to identify the risk that issuing goods on authorized requisition prevents issues to unauthorized persons. Most have written irrelevant answers such as;

- Avoid issue of unauthorized goods
 - Avoid issue of excess goods
- 2.6 Candidates were expected to summarise the importance of the operating effectiveness of the pending order reports. This was based on learning outcome 3.2.1. Many students' performance was unsatisfactory. They have written irrelevant answers such as ability of the purchasing manager to monitor the purchase orders and to cancel the orders.
- 2.7 This question was based on the learning outcome 3.3.1I. Candidates were expected to summarize the importance of restricting access to the database. Although many have understood the issue some have written irrelevant answers such as;
- Identify those who have committed dishonest acts
 - Risk of having technical faults
 - Reduce frauds and errors
- 2.8 Candidates were expected to identify the difference between two compliance requirements and it was based on the learning outcome 4.1.1. Although a small number has understood the question majority has merely repeated the content of the question. Some have given irrelevant answers such as;

Code of ethics

- improve the profession
- Increase business reputation
- Employees become accountable

Laws and regulations

- Reduce the risks
 - It is a social responsibility
 - Accountable to political environment
 -
- 2.9 The candidates were required to explain the necessity for complying with Sri Lanka Auditing Standards. They were expected to apply the knowledge gained from learning outcome 5.3.2. A very few have given appropriate answers. Those answers which carried marks were;
- Enhance public confidence
 - Required to form an audit opinion

It was clear that the candidates lack the knowledge to visualize the importance of SLAuS. Most of them have written irrelevant answers such as;

- Perform the audit in an ethical manner
- Report on the opinion
- To be used as a suitable parameter
- To reconcile financial statements
- To reduce competition among audit firms
- To reduce audit risks
-

2.10 Candidates were expected to explain the characteristics of appropriate subject matter in an assurance engagement, using the knowledge of learning outcome 5.1.2. Only a very few candidates have explained the characteristics of appropriate subject matter. Some have identified the characteristics but were unable to explain them accurately, and as a result they were unable to score full marks. The following irrelevant answers were noted;

- Relevance
- Reliability
- Confidentiality
- Acceptability
- Objectivity
- Legality

Section 2

Question 03

This question carried 10 marks. It consists of four parts. Its aims was to test the knowledge of candidates based on the learning outcome 1.5.3.

- a) Candidates were expected to identify business risks in the procurement cycle which are reduced by effective internal control. Most of the candidates were not able to identify the risks that can be reduced through proper internal control. This reflects that they lack knowledge of the procurement process. Many have given general answers such as ;
- Making payments to wrong suppliers
 - Selection of unsuitable suppliers
 - Not following tender procedure
 - Awarding contracts to get commission
- b) Candidates were expected to explain the role of internal control within the entity in reducing the risks of the purchasing process. Majority have not understood the question. They have wasted time explaining each step of the procurement procedure. They were unable to explain the role of internal control such as effectiveness and efficiency of the process, reliability of financial information and compliance with rules and regulations. It was evident that they have not studied the text.
- c) Candidates were expected to identify the responsibility of the internal auditor for the internal controls of the entity. The satisfactory answers demonstrated subject knowledge. Majority has not performed well. Some have written that the internal auditor is responsible for the design and implementation of internal controls. Majority has written that internal auditor expresses an opinion. It reflects that they are unable to identify the difference between the external auditor and the internal auditor.
- d) Candidates were expected to identify the responsibility of the board of directors for internal controls. A large number have written answers which have no relevance at all such as;
- Whether cash disbursements are done properly
 - Segregation of duties
- Some answers reflected that the candidates have mixed up the responsibility of the management with that of the board of directors. They have mentioned that the directors should report to the management. In spite of these deficiencies the average performance was good; the common correct answer was that the board of directors is ultimately responsible to the shareholders.

Question 04

This question carried 10 marks .It was based on learning outcome 4.2.2 and 4.2.3. This was based on ethics.

- a) Candidates were requested to list (04) threats to the professional behavior of an accountant. This was answered well. However some have not used the correct terminology and some have written instead of;
- Intimidation -forcing
Familiarity –Friendly
- b) This part was based on the scenario and the requirement was to explain the (02) fundamental principles of professional ethics that could be violated due to the given issue. The performance was good .There were some candidates who have mentioned independence as a professional ethic.
- c) Candidate were requested to identify the threat to the professional behaviour as the accountant in the given scenario, and the safeguards available for the threat identified. Although many have written correct answers some have written all the threats without identifying the particular threat. Almost all have written the correct safeguard.

Question 05

This question carried 10 marks, and is based on the learning outcome5.5.2/5.5.3.This question was not attempted by many candidates.

- a) The requirement was to explain the difference between test of controls and substantive procedures. It was disappointing that the basic principles of auditing have not been understood by the candidates.
- b) Candidates were requested to identify two procedures that the auditor uses in carrying out of test of controls. The most frequent correct answers were inspection and observation.
- c) Candidates were expected to explain the audit evidence that the auditor will gather in testing the mentioned controls.

Sequential order most have repeated the question without identifying the principle. Most have written that a sample check should be carried out ignoring the fact in order to check the sequential order a list of invoices should be obtained.

Approval of invoices – Most of the candidates have written correct answers.

- d) Candidates were requested to identify two substantive procedures that the auditor may perform on sales. This was poorly answered, and reflected that they have not studied the text.

Question 06

This question was based on the learning outcome5.5.4.It carried 10 marks, and consisted of four parts.

- a) Candidates were requested to explain the concept of relevance and reliability of audit evidence. It was observed that the candidates have ignored the action verb and not explained giving examples. Many have written incomplete answers such as the audit evidence should be relevant and reliable.
- b) The question required the identification of alternative audit evidence in the absence of original vehicle registration books. Most of the candidates have written correct answers, but some have written to;
- carryout physical verification
 - Check the fixed asset register
- c) Candidates were required to state the risk of accepting photocopied invoices for the vehicles in the given scenario. Many were unable to express their answers clearly. The only available answer was that the company would not have recorded the correct value.
- d) The objective was discussion of professional skepticism in relation to conducting an audit. Most of the candidate have answered well. There were isolated answers which are not relevant. About 30% have not answered this part.

Section 3

Question 07

This was a compulsory question that carried 20 marks. It consisted of five parts and tested learning outcome 2.4.2/2.5.2 based on a scenario.

- a) Explanation of the business risks associated with the critical fixed assets in the given scenario was required. It was observed that the planning of the answer was poor, as they have not explained when they were asked to do so. Most of the candidates have written responses and measures to reduce the risks, instead of explaining the business risks, such as engage security staff, have access restriction and fix cameras. Some have written irrelevant answers such as depreciation is a business risk and keeping excessive assets will create business risks.
- b) It was requested to explain the importance of having a fixed asset register in carrying out physical verification. This was a straightforward question and direct from the study text. Following irrelevant answers were observed;
- Easy to calculate depreciation
 - Can identify date of purchase
 - Selling price can be determined easily
 - All information such as carrying value, opening balance and accumulated depreciation is available
- c) Discussion of business risks associated with the inventory management process of the given scenario was required. It was disappointing that the candidates have answered this part poorly. This reflected that they lack knowledge in risks associated with inventory management. They have written irrelevant answers such as ;
- Physical risk to the inventory
 - In the absence of segregation of duties fraudulent amendments will be made by the warehouse manager
 - There will be system failures due to hacking

- d) Candidates were expected to explain to the management the control mechanism that should be in place over the stock taking process. This is a basic question which all the candidates should be aware of. Most of the candidates have not understood the question, and have written the stages of annual stocktaking. There were irrelevant answers such as;
- Plan the stock taking exercise
 - Control over records
 - Application controls and general controls in an IT environment
 - Safeguard the stocks from damage ,theft, and obsolescence
- e) The requirement was to discuss the impact of slow moving inventory items on the valuation of inventories in the given scenario. It was disappointing that the candidates have not referred to the LKAS2 with regard to the inventories. None has got full marks for this part. There were irrelevant answers such as;
- Reduce prices of slow moving items
 - There is a risk of slow moving items being stolen
 - Slow moving items should be placed in a lockable space

Conclusion

Candidates seemed quite well prepared for some of the questions in this paper. Almost all candidates were able to identify the relevant issues given in the questions, but not all were able follow the action verbs and explain adequately. This is often what makes the difference between a 'pass' and a 'fail'. Candidates are encouraged to read the text and read examiners' comments that accompany the past exam papers. It is important to gauge the style of question requirement that regularly appears and to gain an appreciation of what it means to explain an answer point rather than just identifying the answer point.

Examiners' Comments

Executive Level Examination – September 2015

Commercial Insight for Management (KE 5)

Section 1

Question 01

The ten numbers Multiple Choice Questions (MCQ) carry 20 marks. Overall performance of the candidates was satisfactory. MCQs were on skills required by accountants, effectiveness, market structures, inflation, money supply, Colombo Stock Exchange, operations management, economies of scope, line productions etc.

Specific comments

- A fair number of students were unable to select correct answer for Q. no. 1.10 i.e. line production involves “dedicating parts of the production process to make a single product”.
- Most appropriate answer for Q. no. 1.4 i.e. “A firm has some degree of market power” was not chosen by a fair number of students.

Question 02

General comments

Overall performance of the candidates was satisfactory. This question consists of 10 parts and carries 30 marks.

- 2.1 requires listing of new skills that are important for accountants in today's changing work environment.
- 2.2 requires “internal environment” to be explained.
- 2.3 requires advertising elasticity of demand and its effectiveness to be explained.
- 2.4 requires (03) benefits to an organization of having a number of suppliers to be stated.
- 2.5 requires 3 items which can affect business operations under the economic dimension of PEST analysis to be stated.
- 2.6 requires 3 government policies to control “demand-pull inflation” to be stated.
- 2.7 requires listing 3 action steps to ensure a delegated task is performed successfully.
- 2.8 requires explain concepts of economies and dis-economies of scale to be explained.
- 2.9 requires identify 3 activities involved in human resource planning to be identified.
- 2.10 requires identify 3 types of information systems and their main functions to be identified.

Specific comments

- 2.1 Only a few students mentioned skills such as use of tools that support data modelling and analysis, use of technology to attract, develop and manage talents, knowledge management etc. Some just mentioned skills on globalization, technology needs to be developed by accountants.
- 2.2 Some students explained internal environment correctly stating the factors mission statement, leadership styles, culture, technology etc. Some stated that owners, employees and resources are regarded as internal environment which earned no marks.

- 2.3 Only a few explained effectiveness of advertising using the concept of Advertising Elasticity of Demand. Some defined Advertising Elasticity of Demand (AED) correctly. But they were unable to interpret the positive and negative co-efficients of the AED. Effectiveness of advertising expenditure goes up when AED increases. Only a few stated that the impact an increase in advertising expenditures has on sales varies by industry.
- 2.4 Most of the students stated benefits such as possibility of providing quality products, providing at cheaper rates and effective implementation of contingency plan. Some stated that loyalty of suppliers could be won when the firm has more suppliers, without elaborating as to how it happens.
- 2.5 Most of the students mentioned interest rates, taxation rates, exchange rate, inflation rates etc. as items which affect business operations. A few stated “Money supply” which earned no marks.
- 2.6 Increasing tax, reducing govt. expenditure, surplus budget under fiscal policy measures and raising interest rates, selling securities in the open market etc. under monetary policy measures and increasing aggregate supply and decreasing aggregate demand etc. under other measures, need to be stated. Some just mentioned policies like fiscal policy, monetary policies, foreign investment policy sans appropriate measures being stated.
- 2.7 Some correctly listed steps such as assigning the required authority and resources, allowing the subordinates to perform the task, reviewing the progress made and giving performance feedback. Some were unable to list the steps in the correct sequence. Some were unable to state “reviewing the progress made”.
- 2.8 Some have correctly explained the “Economies of scale” as “Advantages in terms of cost, level of output, with cost per unit decreasing with increase of scale. Diseconomies of scale occur when a percentage increase in all factors of production results in a lower percent increase in output”. Most of the students did not mention the circumstances under which diseconomies of scale can occur, i.e. when a firm becomes too big.
- 2.9 Job analysis, job designing, recruitment, retention, assessing future needs, training etc. have been correctly identified by some students. Some mentioned HRM planning, human resource analysis rather than job analysis, which earned no marks.
- 2.10 Mgt. Information System, Executive Information System, Decision Support System, Office Automation System, Transaction Processing System etc. were identified by some students. Some stated “Narrow Information System, Horizontal & Vertical Information Systems” for which no marks were allotted. Some just mentioned only abbreviations E.g. MIS, EIS, DSS, OAS, TPS etc.

Section 2

Question 03

General comments

Question no. 3 carries 10 marks and overall performance was satisfactory.

Part (a) requires 3 components of the Transformation Process Model to be identified.

- Part (b) requires normal, inferior and Veblen goods to be defined.
- Part (c) requires an explanation of how total quantity demanded goes up when the price falls using income effect and substitution effect.
- Part (d) requires explanation of action steps that a producer could take to increase sales revenue when price elasticity of demand coefficients are 1.5 and 0.5.

Specific comments

- Part (a) The 3 words (in sequential order) input, process and output were expected by the examiner. Most of the students answered as expected. A few mentioned “planning, organizing and directing” which earned no marks.
- Part (b) Consumer income and demand are the two variables based on which normal goods and inferior goods are categorized. Some students incorrectly defined normal goods as a good when the price of which falls, the quantity demanded goes up. A fair number of students defined correctly Veblen good as a good when the price of which increases, demand also increases, e.g.: luxury cars, Some had the wrong view that a Veblen good is characterized by a relationship between consumer income and quantity demanded.
- Part (c) Most of the students correctly explained the income effect as “the change in consumption resulting from a change in real income”. A few just mentioned income effect is due to change in income without specifying “real income”. Some students stated that consumers will buy substitute goods when price of a good falls. They have not mentioned that consumers will replace more expensive items with less costly alternatives due to substitution effect.
- Part (d) When PED is 1.5 and 0.5, action step to increase sales revenue should have been reduction of price and increase of price respectively. Nevertheless some answered the other way round which earned no marks.

Question 04

General comments

Question no. 4 carries 10 marks and overall performance was satisfactory.

- Part (a) requires discussion of how depreciation of SLR can affect FPL (i.e. in the scenario provided in the question).
- Part (b) requires the measures to mitigate/avoid risks of making losses on foreign trade transactions to be explained.

Specific comments

- Part (a) Most of the students mentioned imported shoes become more expensive and export garments become cheaper to foreigners when the rupee depreciates. Only a few students mentioned the elasticity of demand for imports and exports in discussing the effects of the depreciation on FPL. If the demand for ladies shoes is price elastic, rise in the import price will lead to a substantial decrease in quantity sold.

- Part (b) Entering into forward contracts, buying locally manufactured raw materials, pricing both export & import items in US\$ would be risk mitigating measures. According to some students, Rupee should not be allowed to depreciate so that the losses under reference could be minimized. Some stated imports need to be curtailed, but no alternative was suggested to mitigate the possible loss of business.

Question 05

General comments

Question no. 5 carries 10 marks and overall performance was satisfactory.

- Part (a) requires summarisation the steps involved in a formal planning process.
- Part (b) requires the advantages to Sunil i.e. in relation to given scenario, of a systematic approach to planning to be explained.

Specific comments

- Part (a) Setting out the goals, identifying strategies, evaluating them, choosing the best strategy, implementing the strategy and controlling and reviewing are the essential steps of a planning process. Some have written all these steps. But a few have not identified the logical steps. Some students came out with "Division of labour," specialization, employee welfare as steps of planning process which earned no marks.
- Part (b) Direction towards goals, achieving goal congruence, adopting long term view, allocation of resources on rational basis, facilitating performance evaluation are some of the main advantages of planning which some students explained correctly. Some explained the advantages of planning in a general manner in that profit, goodwill etc. of the organization could be enhanced, which earned no marks. A few stated time could be saved because of proper planning.

Question 06

General comments

Question no. 6 carries 10 marks and overall performance was not that satisfactory.

- Part (a) requires to be explained the terms market segmentation, targeting and positioning.
- Part (b) requires the different bases of segmentation to be explained.

Specific comments

- Part (a) Most of the students were not able to explain the term "Market positioning". Market positioning is the way customers perceive a brand/product relative to other brands/products. According to some students, positioning is sales promotions made in respect of target groups which was not elaborate enough to award marks. Some provided incomplete definitions for market targeting and positioning is producing items for the target group according to them.

Part (b) “Geographic, Demographic, Psychographic and Behavioural” are the bases of segmentation expected by the examiner. Some of the students were able to name the bases correctly. Nevertheless they were unable to explain the bases. Some explained that as per age groups, employment social status etc. shirts could be produced without broad bases like geographic, demographic etc. being identified.

Section 3

Question 07

General comments

Question no. 7 carries 20 marks and overall performance was satisfactory.

Part (a) requires calculation of equilibrium price and quantity based on the information given in the question.

Part (b) I requires computation of the point price Elasticity of Demand (ED)
II requires identification of the nature of the point price ED.

Part (c) requires explanation of 3 of the determinants of ED.

Part (d) requires explanation of the likely impact on the market of branded PCS and the foreign exchange outflow on account of subsidy given.

Part (e) requires discussion of how the benefits of the subsidy is shared between the company and the consumer, using an appropriate diagram.

Part (f) requires to listing of two endogenous variables that could have had an impact on the demand & supply.

Part (g) requires to explanation of the possible reasons as to why the company i.e. PCV was unable to achieve monthly profit targets.

Specific comments

Part (a) Almost all have arrived at 200,000 units and Rs. 90,000/- as equilibrium quantity and price respectively. A few students could not ascertain the correct answers due to calculation errors. Some have just indicated 200 and 90 as equilibrium quantity and price instead of 200,000 units and Rs. 90,000/-.

Part (b)I & II Some have arrived at 1.29 correctly as Price Elasticity of Demand (PED) and concluded the product has elastic demand. However some other students applied the new price of Rs. 97,000/- to supply equation instead of demand equation which resulted in incorrect quantity and incorrect PED. A few arrived at 1.29 as PED but concluded that the product had inelastic demand.

Part (c) Percentage of income spent on the good, availability of substitutes and necessity for the good are main determinants of the PED of the branded PCs. Some stated that demand becomes elastic in the long-run of the business without the required explanation.

- Part (d) Only a few arrived at 218,000 units and Rs. 83,700/- as new equilibrium quantity and price respectively to explain the impact. They further concluded that foreign exchange outflow would get increased. Some incorrectly concluded foreign exchange outflow would be less and they have not calculated new equilibrium price and quantity in arriving at the conclusion.
- Part (e) Only a few have drawn the diagram correctly showing the outcome before and after subsidy of Rs. 9,000/- was granted to suppliers and concluded that users of computers would get a price advantage of Rs. 6,300/- per unit. Some have concluded more benefits would be received by consumers by incorrectly drawing the new demand and supply diagram, without the benefits being quantified.
- Part (f) Some correctly listed "Advertising, sales promotions, after sales services, warranties, cost reductions etc. as endogenous variables. Some came out that global market price, per capita income are endogenous variables which earned no marks.
- Part (g) Only a few explained correctly "under-pricing" is the main reasons as to why PCV was unable to achieve its monthly profit targets. Some stated that due to non-conducting sales promotional activities, exchange rate depreciations etc. contributed to the non-achievement of profit targets.