THE INSTITUTE OF CHARTERED ACCOUNTANTS OF SRI LANKA

KB1 – Business Financial Reporting

December 2016

Examiner's Comments

Question-wise comments

General

It was noted that the performance of the candidates was very poor and below the required standard for this level.

It was a concern that many candidates did not have a basic understanding of the accounting standards and also on how to approach the examination.

Lack of technical knowledge, errors in principles, producing irrelevant answers sometimes with unnecessary detail (wasting time that should have been spent on another question), illegible hand writing and not paying attention to the action verbs in the questions was very evident in almost all the questions.

Poor knowledge demonstrated on accounting standards is a serious concern, as most (95%) of the standards are taught at this level. Even the candidates who passed the exam, a majority just managed to reach the pass mark. This will definitely have an impact at the KC 1 level in the following examination.

The overall pass rate was very poor and general performance was as follows.

Question No	Average Marks	Topic tested
1 (10 marks)	4 - 5 ½	(a)Revenue recognition - application of recognition criteria in Conceptual frame work and LKAS 18 (b)Knowledge on application of measurement bases referred to in the conceptual framework
2 (10 marks)	2 - 3	(a)Cash flow statements- preparation of extracts showing "cash flows from Investing activities' (b)IFRIC 1- Impact on financial statements due to change in the decommissioning liability
3 (10 marks)	3 - 5	(a)Measurement of a financial asset that has been impaired and how it should be reflected in the FS (b) Related Party disclosures

4 (10 marks)	2 ½ - 4	Leasing – (a & b) Assess the appropriateness of the lease classification, preparation of FS extracts of lessee and lessor – Income statement, SOFP and cash flow (c)Effects on the profitability and the cash flow of the lessee had the lease been accounted as an operating lease.
5 (10 marks)	2- 3	Ratio Analysis- (a) Interpret given ratios using given industry averages (b) Recommend measures to improve each ratio category
6 (25 marks)	11- 16	Preparation of Consolidated FS - (SOFP only)
7 (25 marks)	5 – 8 ½	Tested several scenarios from multiple standards (a)Evaluate the appropriateness of determined FV of equity investment – SLFRS 13 (b) Accounting for impairment (LKAS 36)of NCA of a subsidiary company (Separate CGU) in the Consolidated FS (c)Knowledge on classification of transactions/ Items - (LKAS 2, LKAS 39 & LKAS 1) (d) Accounting treatment of a restructuring operation (LKAS 37) (e) Assessment of the amortization charge of two separate intangible assets (LKAS 38)

- Knowledge on the application of standards is very poor. However, it was noted that in Q6, the preparation of the Consolidated Statement of Financial Position was attempted well by the candidates. This shows that students know how to deal with the numeric aspects but lack in technical knowledge.

- The students lack the knowledge on interpretation of ratios (Q 5). In the previous examinations, it was required to compute the ratios and then to interpret it. The students used to score 30%- 40% marks for the computations. However this time the examiner has given the ratios with the industry averages and the requirement was to comment on it. Thus the gap in knowledge is very much evident.

- It was alarming to note that candidates did not know how to identify cash flows from investing activities from a given set of information which had financing activities as well. Also some of those students did not indicate whether it is an outflow or an inflow and thereby lost marks even when the correct figures were arrived at.

- Quite a number of candidates provided irrelevant answers for Q 4 on Leasing. The question required the students to show the extracts of the FS, whereas the answer was given as transactions in the “T” accounts.

- It was noted that some candidates were confused on how to compute interest – (Payment in arrears and payment in advance) and made mistakes in the computation.

- About 60% of the candidates did not attempt the question on decommissioning cost (IFRIC 1)

KB2 – Business Management Accounting

December 2016

Examiner's Comments

Question-wise comments

General comments about submission of workings

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

General comment about candidates' handwriting

There were a number of instances, where the marking examiners 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

<u>Part (a)</u>

The overall performance of the candidates ***on average was somewhat satisfactory***. Majority of the candidates (about 50%) had scored 2 marks to 3 marks out of 4 marks allocated to the part. The question tests the ability of the candidates to ***understand and demonstrate limitation associated with absorption costing***. Although the question seems simple and straightforward, the candidates had failed to point out the key ***shortcomings of absorption costing when compared with the ABC method***. Many candidates had failed to relate the answer to the setting in which the production is carried out (***i.e. the semi-automated production system***). About 70% of the candidates who attempted the question ***had failed to incorporate*** this fact in developing the answer. ***None of the candidates*** had pointed out that ***machine hours utilized is highly sensitive to cyclical variations,*** for example, seasonal fluctuations ***which might undermine the cost relevant to other activities***, for example material handling, when the number of units produced by the Company varies over time. Surprisingly, majority of the candidates (about 70%) had identified the fact that ***absorption costing uses a flat rate for allocating indirect overhead to the product***. Weak answer scripts (about 50%) contained ***no discussion*** of the ***rational basis of allocation of cost over different activities of the organization*** as opposed to machine time.

However, some answer scripts (about 30%) had ***carried very good arguments against absorption costing***, hence scored full marks. A handful of candidates (about 5%) had provided ***detailed calculations*** taking examples of ***their own which was clearly not expected by the Examiner***. All candidates who mentioned ABC method in their answers ***had correctly interpreted the basis of ABC system***.

Part (b)

The overall performance of the candidates ***was very satisfactory***. The average marks obtained by candidates ***ranged from 3 ½ marks to 4 ½ out of 6 marks allocated*** to this part of the question. Majority of the candidates (60%) had computed the unit cost based on ***ABC method accurately*** whereas some (about 40%) who attempted to compute unit costs based on ABC method and absorption costing method had failed to calculate the ***unit cost based on absorption costing system correctly***.

The common weaknesses observed in the answer scripts include but are not limited to the following;

1. Taking utilizations of both HDD and total for the plant when ascertaining the applicable hours/orders, for example, machine hours Rs. 6 mn/(100+500)
2. Some candidates (about 40%) had failed to identify the composition of indirect cost applicable to each driver, for example Rs. 30mn x 40% for machines.
3. Some candidates had divided Rs. 30mn by the utilizations of both HDD and total for the plant, for example as in 1 above and then divided such by 10,000 units to arrive at the unit cost applicable (i.e. (Rs.30mn/(100+500))/10,000) to the plant.
4. Considerable amount of candidates (about 40%) had taken Rs. 3,000 as indirect cost allocation under absorption costing without regard to the machine time for example, Rs. 30mn/10,000.
5. A handful of candidates (about 10%) had taken Rs. 30mn/20,000 hours as unit indirect cost allocation under absorption costing.
6. Only a negligible amount of candidates (about 2%) had been able to demonstrate the applicable machine time for a unit, for example, 100/10,000 = 0.01 and the correct apportionment as Rs. 60,000 x 0.01 = 600 where Rs. 60,000 is arrived at by dividing Rs. 30mn by 500 machine hours for the plant.
7. About 20% - 30% of the candidates had failed to support the answer (a) by using the assessment results of part (b).

Question 02

General Comments

Question consists of two parts. Part (a) tested the knowledge of assumptions used in ROL and EOQ and restricted application of these two formulae in a real-life situation, where it failed to produce desired results. Part (b) examined the knowledge of MRP, its important features and its application to overcome issues faced by production manager in using ROL and EOQ in inventory control.

Part (a)

About 40% of candidates failed to appreciate the requirements of the question, which is to examine problems faced by production manager in controlling the inventory, utilizing EOQ and ROL with special emphasis on assumptions upon which these two models have been founded.

Some students stated all assumptions used in formulation of EOQ and ROL, but failed to examine reasons for their failure and as to why assumptions referred to above did not produce results.

Part (b)

Large number of students failed to appreciate the gradual evolution of MRP to MRP2 and then to ERP. This evolution resulting in improvements at every succeeding stage will indicate which model suits the complexities of business entity PQR.

Question expects only MRP (not MRP2 or ERP) to be used in this situation to indicate how problems faced by manager in (a) could be rectified with the help of special features witnessed in MRP.

Students simply stated the benefits of MRP but did not attempt to indicate practical application of it to overcome issues with the help of features not witnessed in ROL and EOQ.

Question 03

General comments

This is a two part question. Part (a) tests the candidates' understanding of the effect on contribution due to changes in the price and volume. Part (b), tests the ability of the candidate to price products to achieve a given profit. Performance of the candidates was poor with the question having the second lowest average marks for the paper. Though the costing concepts tested in this question does not go beyond what is learnt at the Executive Level, poor application of these concepts and poor analytical ability had prevented the candidates from successfully tackling a problem of this nature.

Specific comments

Part (a) Common mistakes made by the candidates were;

- (i) Being unaware of the nature of fixed costs (i.e.) adjusting it with the change in production volume.
- (ii) Not calculating the incremental profit, but instead calculating the total profit from following each strategy.
- (iii) Not identifying all the possible strategies (i.e.) strategy A, B and strategies A & B both.
- (iv) Calculating the profit from combined strategy (A and B) by adding the individual profits of strategy A and strategy B.
- (v) Taking the incremental sales as incremental profits.
- (vi) The present total production cost (Rs. 36,500) taken as the production cost for all the strategies.

Part (b) Majority of the candidates have not understood how the strategy C can be combined with existing strategies. The approach to pricing of export order in strategy C was not bottom up. Instead, candidates have decided on a selling price (usually Rs. 5,000) and arrived at a profit which is then compared with the target profit of Rs. 4 million. The performance of the candidates in this part was very poor.

Question 04

General comments

This is a three part question which tested the candidates' knowledge on transfer pricing. Part (a) requires the candidates to calculate the transfer prices under the existing and proposed methods. Part (b) involves determining the effect on the profit of the purchasing company and the group as a whole if the purchasing company is free to decide on the source of purchase (i.e.) whether external or internal. Part (c) tests the candidates' knowledge on dual rate transfer pricing policy.

Specific comments

Part (a) Performance of the candidates satisfactory. However, some candidates had made mistakes in the calculation of fixed overhead by taking the variable production cost to include delivery charges while some others had confused it with variable production overheads.

Part (b) Some had computed the profit/loss on TPL making its own purchasing decisions by computing the difference between the present and proposed transfer prices, not realising that the external market price is lower and TPL will purchase externally. Some had computed the loss to the DPP group by only computing the loss to Qtech (without adding the TPL profit). Some had assumed that in the event of TPL purchasing externally (at Rs. 11,500 per motherboard), Qtech could sell the 20,000 motherboards per month to external market, and proceeded to work out Qtech's loss at Rs. (11,960-11,500) per motherboard. However, this is not possible as the question clearly states that the external market demand for motherboards cannot be increased in the short term. This shows the importance of reading the question carefully and noting all the relevant information before answering a question.

Part (c) Some candidates were unaware of what dual rate transfer pricing is and tended to guess the answer by explaining the meaning of the word 'dual' while there were others who thought dual rate transfer price is the two prices a company charges, one for external sales and the other for internal sales.

Question 05

General comments

This is a three part question on debt factoring. Candidates were required to determine the cost/return on debt factoring from the point of view of the factoree/factoror. Performance of the candidates very poor with the question having the lowest average marks for the paper. It is apparent that the candidates have not sufficiently covered this area/attempted similar problems within studies.

Specific comments

Candidates could not appreciate that this is a problem involving the time-value of funds and the need to draw-up an appropriate cash flow which will have the amount offered for lease receivables upfront as year zero cash inflow or outflow as the case may be from the points of view of the factoree and factoror. This needs to be compared with the discounted cash flow of the monthly lease receivables. Many who attempted this question had tried to approach the problem by calculating the interest element on the lease receivables and failed miserably.

Question 06

General comments

The question consisted of two parts which tested the candidates' knowledge on variance analysis and controllability of variances.

Part (a) for which the allocation was fifteen, required the candidates to prepare detailed variance analysis that would enable a critical evaluation of the performance of the stitching department of an apparel manufacturing company. In part (b), the candidates were required to demonstrate the extent to which the performance is attributable to and controllable by the stitching dept. in the context of the operation manager's comments that "the stitching department had been inefficient in controlling costs and as a result the actual unit cost has increased by 18% compared to what it should have been". Ten marks were allocated to part (b);

Specific comments

Many candidates had provided good answers to part (a). Some candidates had calculated DM total variance, DL total variance etc. instead of calculating the DM price variances and DM usage variances separately for transfers from the cutting department and accessories bought from outside, although the question required the preparation of a detailed variance analysis. Similarly, FOH total variance was calculated instead of calculating the FPOH expenditure variance and FPOH volume variance for FPOH directly incurred by the stitching department as well as allocation from the general pool.

Some candidates had calculated the FPOH volume efficiency and FPOH volume capacity variances using the standard absorption rate per unit, instead of the standard absorption rate per hour. Many candidates hadn't reconciled the stitching department standard cost for actual production and the actual cost of production. Some candidates had used the budgeted production cost of Rs. 800,000 instead of the standard cost of actual production amounting to Rs. 1,000,000 in the reconciliation.

Some of the other mistakes made were calculating FPOH total variance for FPOH expenditure variance, calculating FPOH volume variance only for allocated FPOH and using standard DL hours required for actual units produced (7,000 hours) instead of the actual DL hours, in calculating VOH expenditure variance. Further, some candidates hadn't calculated the FPOH volume variance.

Many candidates hadn't provided good answers to part (b) and some hadn't made an attempt to answer the part.

Many candidates hadn't indicated the variances that are uncontrollable by the stitching department with the reasons for uncontrollability. Similarly, the controllable variances were not identified and a conclusion reached whether the stitching department had controlled costs efficiently or not. Only a few candidates recognized that the FPOH allocated from the general pool is uncontrollable by the stitching department.

Some candidates had only calculated the % increase in unit cost and not stated whether the operation manager's comment regarding the 18% increase in the unit cost was correct or not, although 10 marks were allocated for the part.

Question 07

General comments

This is a three part question set on decision making under risk and uncertainty. Part (a) requires the candidates to calculate the unit prices for each design under each of the possible demand levels. Part (b) requires the candidate to determine which design would be chosen by (i) a risk seeking (ii) a risk averse (iii) a risk neutral decision maker. Part (c) requires the candidates to assess the impact of an increase in material prices on the expected profits.

Specific comments

Common mistakes made by the candidates were;

Part (a)

(i) Taking Rs. 100,000 material costs included in Rs. 180,000 variable costs per unit as Rs. 180,000 other variable costs and Rs. 100,000 as material costs.

(ii) Instead of working out the unit prices for each design at each demand level, many had worked out the expected demand level (using the given probabilities) and calculated one price for each design.

(iii) Variable cost per unit added to total fixed costs to arrive at the cost per unit.

(iv) Calculating revenue per unit instead of profit per unit.

(v) Not considering the price cap of Rs. 273,000 per unit

(vi) Calculating the total sales volume instead of the selling price per unit.

Part (b)

(i) Instead of the required total profit for each possible outcome many had worked out the answer based on the profit per unit.

(ii) Some had based their answers on total sales (i.e.) not the total profits.

(iii) Some had based their answers (for risk seeking & risk averse) on expected profits.

(iv) Some had selected the highest value for risk seeking, lowest value for risk averse and middle value for risk neutral.

Part (c) Candidates were required to assess the impact of the change in material prices on the expected profit. However, many had calculated only the increase per unit cost. (i.e.) Rs. 100,000 x 10% = 10,000.

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KB3 – Business Law and Tax

December 2016

Examiner's Comments

Business Law

Question 01

(a) Fair percentage of candidates had understood that corporate veil or veil of incorporation refers to the legal concept that separates corporate personality from its owners the shareholders. The corporate veil or the curtain separates the shareholders from the company and protects them from being personally liable for the debts and other obligations of the company since it is a separate statutory body. Also they are well aware that this legal concept was established in the landmark case decision given in Salomon vs. A Salomon & Co. Ltd.

Further they are familiar with instances under which court has lifted the corporate veil in the past and had furnished even more than 3 instances though the question required only 3 such instances.

Similar percentage of candidates had tried to interpret this concept in a different manner and had stated that 'corporate veil' means a company is a separate entity from promoters and directors (management of the company). As a result the company can purchase assets, file legal cases in the name of the company irrespective of the losses suffered by outsiders due to company related activity of the directors/promoters who are not liable but the company itself is liable for such situations. Some had cited irrelevant statutory provisions and case law.

(b) Large no. of candidates had recognized that Dunstan (Pvt) Ltd has suspended its business for more than a year i.e. from 30.06.2014 to date. On that ground a creditor/contributory (shareholder) can petition to the court under section 272 of Companies Act for winding up of the company on the ground of suspension of its business for more than a year. As per section 270 (b) a company may be wound up by the court if it does not commence its business within a year from its incorporation or suspends its business for one year. They have clearly recognised that it is a valid ground under the Act to petition to court for winding up the company.

Also there were some others who had in addition dealt with section 271(a) and had discussed the possibilities to petition to the courts on the ground that the company is unable to pay its debts and had explained following areas.

Company owes Rs. 60,000 to Zimbo which exceeds the prescribed limit of Rs. 50,000. Therefore, first he must serve a notice on the company at its registered office demanding that the company settle the amount due to him.

If the company does not settle the amount within 3 weeks from such notice then the company is deemed to be unable to pay its debts and Zimbo can submit a petition to wind up the company. Similar no. of candidates had missed this important point and had only dealt with the other point that Dunstan (Pvt) Ltd owes Rs. 60,000 to Zimbo from 1 June 2014 and as a creditor he can petition to court to wind up the company on the ground that the company is unable to pay its debts (section 271 (a)).

They have failed to realise that first Zimbo has to serve a notice on the company at its registered office demanding the company settles his dues. Only if the company does not settle within 3 weeks from the date of Zimbo serving such notice the company is deemed to be unable to pay its debts and petition for winding up on that ground may be made.

They all have totally missed the main point that the company has suspended its business for more than 1 year and a creditor can petition to court to wind up the company on that ground.

Question 02

(a) Large no. of candidates had explained the procedure that should be followed in adopting the Model Articles as the company's own articles as has been laid down in the Companies Act No. 07 of 2007. As per section 15 of the Act they had dealt with areas like calling for the EGM with due notice, and passing of special resolution for the purpose and thereafter giving notice to registrar of companies within 10 working days with the full facts of the special resolution and newly adopted model articles or amended articles, as they are familiar with the subject area.

But a similar no. or even a higher no. who had failed to understand the question properly had explained various irrelevant areas like;

(i) Explaining Memorandum and Articles of Association as detailed in previous Companies Act.
(ii) Content of articles such as object clause and rules applicable for day today management of the company.
(iii) Ultra virus doctrine.
(iv) Effect of articles of association of a company and obligations of directors and employees of the company.
(v) Procedure to be followed in passing a special resolution or passing of circular resolution and so on.

(b) Many candidates are familiar with pre-incorporation contracts and the effects on them before and after new Companies Act No. 07 of 2007. They had correctly quoted the correct case law Kelner vs. Baxter clearly explaining the ruling laid down under it that if the company did not exist at the time of entering in to the contract it would be totally inoperative unless the contract is binding on promoters personally and a stranger cannot by subsequent ratification relieve them from responsibility. Accordingly before the new Act the promoters were personally liable on those contracts.

However under new Companies Act not only are pre-incorporate contracts recognized it has introduced 2 implied warranties for pre-incorporation contracts. In terms of section 24 of the Act when a person enters into a pre-incorporate contract for and on behalf of a company that person is deemed to give implied warranties to say;

" The company will be incorporated within the period as may be specified in the contract or if no period is specified within a reasonable time after making the contract and that the company will ratify the contract within such period as has been specified or if no period is specified within a reasonable time after the incorporation of the company."

However, there were others who had failed to understand the question properly and had focused their answers in incorrect/irrelevant directions such as;

- explaining what is a pre-incorporation contract in general and who enters into pre-incorporation contracts.
- duties and responsibilities of promoters and they should not earn secret profit.
- who is responsible for such contract in the event the company fails to ratify them and so on.

Question 03

(a) Good no. of candidates are familiar with the procedure to be followed in paying of dividend by a Plc as laid down in the model articles attached to the Companies Act. Some of them had recognised that the dividend falls within the meaning of distribution out of profit under section 56 of the Companies Act although majority of them had ignored that important point.

In their answers they had explained the following procedure that should be followed in distributing of profits as has been laid down in the model articles. Accordingly distribution of dividend by a company must be first recommended by the Board of Directors of the company and thereafter should be approved by the shareholders by passing an ordinary resolution. Further the directors must be satisfied that the company will satisfy the solvency test immediately after distribution of dividend and directors who vote for the distribution must sign a certificate of their opinion to that effect.

Majority of the others had failed to realise the correct procedure to be followed in paying of dividends as explained in model articles and had explained irrelevant areas as the procedure that should be followed for payment of dividend.

Mr. Kaluarachchi is the major shareholder of Heal Me. PLC. Therefore, first he should communicate his requirement to the Board of Directors of the company as he holds voting shares. Then the board will act on his request. However the proper quantum is to be ascertained through the meeting of shareholders. If the directors fail to comply with the requirements laid down under 1st schedule and under section 56 they will be guilty of offence and be liable to a fine not exceeding Rs. 200,000.

Further board should determine the appropriate amount to be distributed considering the solvency of the company immediately after distribution is done and is required to obtain a certificate of solvency from the auditors along with the statement of directors.

Before declaration of dividend it should be authorized by the board of directors of the company considering such time and such amounts as they think appropriate/reasonable as per the profit earned by the company.

(b) Candidates were required to explain the terms Executive, Managing and Shadow Directors. Good no. of candidates are familiar with all 3 types of directors and had furnished acceptable answers which deserved good marks. The following details were furnished in their answers.

- Executive director plays a dual role in a company's management in the capacity of a director as well as an employee of the company.
- Managing director is an executive director appointed by Board of Directors of the company. Generally MD is a full time employee of the company i.e. he is in charge of day to day management of the company subject to any special provisions contained in the articles of the company in that regard.

Shadow director is a person who provides instruction and guidance for the operation of the company although he/she is not regarded as a director of the company.

But there were other candidates who were not competent to understand the 3 types of directors and had focused their answers in some irrelevant/incorrect directions such as;

Executive directors are of 2 types namely executive directors and nonexecutive directors. Executive director does not attend board meetings but advises in the day to day management of the organization. They owe their duty to the company and not to the shareholders Executive director is a "controlling part of the co". MD is a member of the company's board of directors who is not part of the executive team. They usually do not engage in the day to day management of the organization. MD works for the company and participates in the functions of the company. He holds a key position in the company and he has a useful role regarding the company management.

Executive directors act according to some instructions. If a person instruct the board of directors as to how he should act and board of directors has the habit of acting in accordance with such instructions, such a person will be treated as MD. Shadow director is something similar to a validly appointed director as far as the duties and obligations are concerned.

Question 04

(a) Very easy straightforward question which requires to state 5 documents that have to be kept at the registered office of a company as stated in Companies Act under section 116. Very high percentage of candidates had correctly copied even more than 5 such documents including the following which deserve full marks.

i. The certificate of incorporation and articles of association of the company.
ii. Register of directors and secretaries as specified in section 223.
iii. Share register required to be maintained under section 123.
iv. Certificates required to be given by directors under the Act within the proceeding 10 years.
v. An interest register unless it is a private company which can dispense with the need to maintain such register.
vi. Minutes of all meetings held and resolutions passed by the board of directors and directors' committees held within last 10 years and various other documents laid down under section 116 of the Act.

However there were a handful of others who are not even competent to refer to said section 116 of the Act but just stated a few names of documents of their own choice such as;

i. Comprehensive income statement/statement of financial position statement of changes in equity/cash flow statement and required notes.

ii. Annual reports of the co./current year audited financial statements.
iii. Certificates of registration for VAT and NBT.
iv. Registered address of the company.
v. Copies of form nos. 01, 13, 18, 19 & 22 and wasted time.

(b) Majority knew how to analyse a transaction determine whether it is a transaction as laid down under section 185 of the Act, since at this level they are conversant with such subject areas. To candidates at this business level it is a simple exercise to analyse what a major transaction is when the value of any proposed liability is given. If the value of such a transaction exceeds half of the value of total assets it falls into the category of a major transaction as stipulated under section 185 (2) (c). Further section 185 (1) deals with how a company can validly enter into a major transaction. Accordingly they had stated that Tasty Tea (Pvt) Ltd must follow the necessary steps to proceed with the transaction.

- Pass a special resolution for entering into a major transaction with Colombo Bank PLC;
- Contingent approval by a special resolution;
- Obtain the consent of all its shareholders to enter into this transaction;
- Make sure articles of the company has expressly authorized the company to enter into a transaction of this nature and so on.

However there were some others who are not quite familiar with major transactions as dealt within the Companies Act under section 185 and explained some other irrelevant areas disclosing their poor knowledge and had dealt with areas including the following;

- Before the transaction company must satisfy the solvency test. Once it is done the company must take note of the new total assets of the company and total liability of the company and also the new shareholding of the company.
- The transaction can be treated as a major transaction because the current assets of the company are Rs. 100,000 but non-current assets are Rs. 200,000.
- The directors should delegate to a committee directly their voting shareholding regarding this major transaction.
- The loan amount is Rs. 175,000. Therefore, this transaction exceeds current assets hence it cannot be treated as a major transaction.
- The amount of bank loan is only Rs. 175,000 which is not a significant amount and does not come under major transaction and so on.

Question 05

(a) Some of the candidates had reproduced the statement as it appears in study text and earned full marks. In their answers they had started by saying;

The objectives of regulating the securities market are as follows
- to help stock market and so on and ended up with ………… in the securities market (page 135 of study text).

It appears that the said statement had been copied in to the Companies Act in advance and taken to examination hall and reproduced in their answer books since candidates are allowed to take the Companies Act to the examination hall under open book examination, i.e. candidates are allowed to take the Companies Act containing highlighted, short notes/other notes for their reference purpose in the examination.

There were others who had confused the objectives of regulating the securities market with the role of the CSE or its objectives, powers, duties and functions and had described these as objectives of regulating the securities market. In some of their answers they had dealt with creation and maintenance of a market in which securities can be issued and traded in an orderly manner, protection of the interest of the investors, the operation of a compensation fund, granting of license to a body corporate to operate as a stock broker etc.

There were some others who had furnished their own assumptions as the objectives of regulating the securities marked including the following;

- "Preventing any misdirecting transactions and observing any unusual transaction in the market and composing some legal actions and controls to prevent any misleading transactions.
- Establishing business friendly environment for investors.
- To prevent any unethical transactions and secure the interest of the investors
- Promote investment opportunities and establish a good environment for investors.
- To prevent any wrong or misunderstanding transaction in security market and so on."

(b) Candidates were required to explain the procedure followed in enforcing an arbitral award as laid down in the Arbitration Act No. 11 of 1995. The answers furnished to this question too by the some candidates are a reproduction of what is given in KB 03 (Law) study text indicating again that some candidates would have copied what is contained in the study text covering the said procedure into the Companies Act and taken to the examination hall and subsequently reproduced in their answer books. It could be observed that this is a regular practice followed by some candidates under open book examination.

In their answer they had covered the following relevant areas to earn good marks.

To enforce an arbitral award an application has to be made to the high court within 1 year after expiration of 14 days of the award being given. High court shall on a date noticed to the parties proceed to file the award and its judgment will be made available in accordance with the award given. After the judgment of the high court a decision shall be made which will be enforceable like any other decision of a civil action.

Many others had furnished irrelevant answers as they are not familiar with the procedure to be followed in enforcing an award delivered by an arbitrator, covering subject areas like;

i. An arbitrator's award is final and Rosa Shipping (Pvt) Ltd cannot challenge it.
ii. No party can reject the award given by the arbitrator and they are bound by an award given by him.
iii. To enforce arbitrator's award, a formal award on the agreed terms to a settlement has to be prepared and signed by the arbitrator.
iv. An arbitration is an alternative dispute solution method and at the end of it an "Arbitrated award" is issued by the arbitrator.
v. The affected party has to file a petition against the award made in writing in the high court before expiration of 20 days of awarding of such award by the arbitrator. The court will proceed thereafter and so on and had wasted their time.

Business Taxation

General Comments (applicable to both questions)

1. Taxation part of the paper consisted of two (02) questions each carrying 25 marks.
2. The subject matter covered in both questions was within the syllabus and adequately covered in the study pack published by CA Sri Lanka.
3. Overall performance can be considered as quite satisfactory with around 15% to 70% of the candidates scoring 50% or more of the total allocated marks.

Question 06

The question required candidates to:

(a) Assess the total income tax liability and the balance tax payable by a resident company which was formed by the conversion of a sole proprietorship.

(b) Explain whether there is any liability to deemed dividend tax for the year of assessment 2015/16.

General comments

Majority of the candidates made a good attempt at the question and the overall performance can be considered as quite satisfactory. About 55% of the candidates scored over 50% of the allocated marks. There were some excellent answers and a few (about 5%) candidates scored 20 or more marks out of the allocated 25 marks.

The question had a reasonable coverage of commonly applied sections of the Inland Revenue Act in this corporate income tax computation. The inclusion of section 25 (7) (f) (iii) and section 25 (1) (i) which are not so commonly applied, is commendable.

Specific comments

Part (a) Most candidates made a good attempt at this part of the question displaying excellent application skills in the construction of the structure and in identifying the statutory contents of an income tax computation of a corporate entity.

Majority of the candidates demonstrated sound knowledge in the application of the provisions of the Inland Revenue Act in relation to:-

- Sections 25 and 26 – allowable and disallowable expenses and charges including limitations thereon.
- Identifying statutory/assessable/taxable income.
- Identifying available tax credits.

Where mistakes were made, those generally related to:

1. Improper reading of the question, e.g. Research & Development – the question had clear indications that the lab equipment was capitalised and included in fixed assets.

   However, a good number of candidates assumed that this cost was included in research and development expenditure and written off as an expense.

Shortcomings in technical knowledge.

Part (a)

(i) trade/business income –

- Rent income – a good number of students treated this as income under section 3 (g). Students are advised to read section 217 which defines 'business' to include 'letting of premises by a company'.
- Research and development.
  - Market survey – a good number of candidates claimed double deduction in respect of market survey expenses under section 25 (1) (i). Market research which includes market survey is expressly excluded from the expenditure eligible for double deductions.
  - Laboratory equipment – A good number of candidates did not know that double deduction can be claimed in respect of capital expenditure as well under section 25 (1) (i).
  - Expenses relating to buildings let on rent – a good number of candidates made mistakes in identifying the allowable report expenditure on rented out buildings.

E.g. (a student's answer)

Gross rent	Rs. 6,000
Less rates	40
	5,960
Less 25% repair allowance	1,490
	Rs. 4,470
	=======

Allowable – Rs. 1,490

- capital allowances –
- Laboratory equipment – A few candidates claimed the allowance in addition to the 200% deduction under section 25 (1) (ii). Where an expense is eligible for deduction under two or more paragraphs, section 25 (2) restricts the deduction to only under one such paragraph.
- Majority of the students did not know provisions under section 25 (7) (f) (iii) relating to the cost of acquisition of fixed assets at the time of conversion of a proprietorship into a company.
-
- A good number of candidates claimed capital allowance in respect of buildings which are not 'qualified buildings' for the purposes of the Inland Revenue Act.

- lease
- A good number of candidates made mistakes in computing the allowable lease rental in terms of section 26 (1) (f) (i).

E.g. (student's answer)

Total lease value	xxx
Less 1/5th thereof	xxx
Allowed	xxx

(ii) Interest income – a few candidates mentioned that this does not form part of the statutory income since withholding tax has been deducted.

(iii) qualifying payments – majority of the candidates correctly identified payments that are eligible to claim the relief. However, they failed to mention the limitation on such claims.

(iv) dividend tax – a few students did not know that a company's tax liability includes tax on dividend distributed.

(v) tax credits – a few candidates claimed tax credits either as a deduction from assessable income in ascertaining taxable income or as a deduction from <u>taxable income</u>. Such shortcomings are serious in nature being errors of principle.

Part (b) Overall performance in this part of the question was fairly satisfactory.

The undermentioned shortcomings are noteworthy;

- taking the profit adjusted for tax purposes.
- taking depreciation on fixed assets purchased in prior years.
- taking capital allowances instead of accounting depreciation.
- taking fixed assets purchased in prior years.
- calculating deemed dividend tax without considering dividends already distributed.

Common mistakes made by the students

Part (a)

- Rent income – a good number of candidates appear to be ignorant of section 217 which defines 'business' to include 'letting of premises by a company'. Such students computed net income in terms of section 3 (g). On the other hand, a good number of candidates who correctly assessed this income under section 3 (a), made mistakes in calculating the deductibility of repair expenses in respect of rented buildings.

- Capital allowance - only the buildings transferred at the time of conversion to a company is eligible for capital allowance claim. However, a significant number of candidates claimed capital allowance on the buildings acquired after conversion. None of those buildings are eligible for the allowance. With a few exceptions, acquired buildings do not qualify for capital allowance. The buildings mentioned in the question do not fall within the exceptions.

Question 07

The question required candidates to:

(a) (i) advise the management of a company regarding NBT liability.
(ii) compute the NBT liability for the quarter ended 31st December, 2015.
(iii) explain whether the company is chargeable to ESC for the quarter ended 31 December 2015 where the company had incurred a tax loss for the previous year of assessment.

(b) (i) assess the income tax liability of a partnership for the year of assessment 2015/16.
(ii) advise the precedent partner's responsibilities in furnishing income tax returns to the Inland Revenue Department.

General comments

Majority of the candidates scored good marks in computational parts of the question. As mentioned in any earlier comments candidates performed poorly in theoretical aspects of the question. However, average performance can be considered as satisfactory. About 60% to 70% of the candidates scored 50% or more of the allocated marks.

Computation of partnership tax had been frequently tested in past examinations and majority of the candidates scored almost full marks (11 marks).

The reason for such high marks could be due to repetition of similar adjustments in successive exams.

Specific comments

Part (a) This part of the question tested mainly the theoretical aspects of taxation. Overall performance was disappointing. There were only a very few good answers earning good marks.

Part (b) Overall performance in part (b) (i) was excellent with a few candidates scoring full marks (11 marks). However, performance in part (b) (ii) was extremely poor.

The undermentioned shortcomings in candidates' answers are noteworthy.

Shortcomings in technical knowledge

Part (a) (i) Advice to management – Majority of the candidates simply answered that the company has to pay NBT on turnover. This type of advice is inadequate and layman style. Professional advice should include a reference to statutory provisions relating to chargeability to NBT.

(ii) Liable turnover - a few students computed NBT on 50% of turnover. This is appropriate for wholesalers and retailers. PK Ltd is a manufacturer and 100% of its turnover is liable to NBT.

(iii) ESC – Majority of the candidates are ignorant of the applicable provisions relating to chargeability to ESC. A good number of candidates mentioned that the company is chargeable to ESC although it has incurred a loss in the previous year while some mentioned that the ESC is chargeable if the quarterly turnover exceeds Rs. 50 million.

A few candidates deducted the tax loss of the previous year of assessment from the turnover and calculated NBT on the net figure.

Part (b) (i) Divisible profits –

- A good number of candidates appeared to be ignorant of section 76 (2) which stipulates the basis of ascertaining the divisible profits of a partnership.
- Partnership tax computation – A good number of candidates presented computations which would be appropriate to a person or body of persons. Students should know that a partnership is not a "person" for the purpose of section 2 and therefore normally not chargeable with tax. However, partnerships are chargeable to tax under section 78 (i) which also specifies the basis of taxing partnerships.

(ii) Income tax return - majority of the candidates mentioned only one aspect of the responsibility of the precedent partner, namely, the furnishing of the income tax return.

Improper reading of the question

Part (a) (ii) A good number of students applied the proportion 2/102 to the turnover figure in calculating NBT assuming that the turnover is inclusive of NBT. Such assumption is inappropriate as the question clearly states that the company has not paid NBT on its turnover.

Irrelevant answers

Part (b) (ii) A few candidates computed the distribution of divisible profits and other income among the partners. This was not required in the question. This is a waste of valuable exam time earning no extra marks.

Common mistakes made by candidates

Part (a) (i) Professional advice – not making reference to statutory provisions relating to chargeability to NBT.

(iii) Economic service charge (ESC) –

- Not identifying the period whether quarter or annual when making reference to turnover threshold.
- Ignorance of when a business becomes chargeable to ESC.

Part (b) (i) Identification of divisible profits.

Any other comments to students

General (applicable to both questions)

1. Read each question at least twice before attempting to answer. This will help to plan your answer through better understanding of the question. You are given additional 15 minutes to read and plan your answer.
2. Good planning will help to avoid irrelevant answers. It was observed that a good number of candidates wasted valuable exam time writing irrelevant answers earning no extra marks.
3. In building up answers, give relevant workings to support your answers. In taxation, arithmetical accuracy and final answer do not score marks.
4. Improve on your handwriting and communication skills. Examiners cannot award marks if the candidate's handwriting is illegible or they cannot understand what is written.

KB4 – Business Assurance & Ethics

December 2016

Examiner's Comments

General comments

This paper consists of two sections and all questions are compulsory. The second section consists of two questions carrying 25 marks each.

All the questions in this paper are based on the study text. It is disappointing to note that overall performance in this paper is poor with it being obvious that many candidates had not properly prepared for this examination.

Specific Comments

Question 01

Part (a) The candidates were required to state the qualification that a person should possess to act as an auditor of a private limited company. Many have understood the question and wrote that, that person should be a member of CA Sri Lanka, but many have failed to write that a registered auditor also qualifies to be an auditor. There were some answers stating the persons who are disqualified from being an auditor.

Part (b)It was required to assess all possible threats to independence and objectivity in the given scenario.

1. The candidates have failed to assess the issue, most of them have written about threats without explaining. Some have identified the correct threat in obtaining the loan, but were unable to assess the materiality of that.
2. Some candidates have identified the correct threat, but many were unable to identify the threat to independence and also to assess the significance of the threat. Some candidates have written irrelevant threats such as;
   - Familiarity threat
   - Advocacy threat

Question 2

Part (a) The candidates were required to evaluate deficiencies in the board structure of the company in the given scenario. Many have written about the number of directors and the effect on independence. Writing the answer without referring to the issues in the scenario, was a common error in most of the scripts.

Part (b) It was required to outline the responsibility of the board and the operational management. It was observed that many were unable to distinguish the board from the operational management although this is illustrated in chapter 4 of the text book. Most of them lacked the practical knowledge and the technical knowledge to identify how the responsibilities of the board are delegated to the operational management.

Part (c) It was required to recommend internal controls to mitigate the issues given in the scenario.

Payroll; Most of the candidates stated segregation of duties as a recommendation. There were only a few candidates who have identified the IT controls as a recommendation.

Purchasing process; some candidates have written segregation of duties without explaining the purchasing process. As a result they got less marks.

Question 03

Part (a) The candidates were required to outline the business risks in the given scenario. Most of the candidates produced satisfactory answers.

Part (b) It was required to state the affected financial statement line items (2) relevant to the business risks outlined in (a).

Product quality issues- Many candidates have identified inventories as the line item but failed to identify revenue as a line item. Most of them were not specific in their answers. They stated that there are sales returns, but were unable to link that to revenue.

Pressure from competitors-Although the candidates have identified inventory and revenue as line items they failed to identify impairment of plant and equipment as a line item. There were some candidates who wrote the requirement to impair the plant and machinery but were unable to state this as a line item.

Part (c) The candidates were required to differentiate the business risk approach from the audit risk approach. Many candidates have explained the business risk approach and the audit risk approach in isolation and failed to explain the difference and as a result obtained less marks.

Part (d) It was required to state factors that affect the identification of an appropriate bench mark. Although some have produced satisfactory answers there were irrelevant answers such as;

- Risk of material misstatement
- Effectiveness of the internal control

Question 04

Part (a) The candidates were required to explain the relationship between the sample size and the audit risk. The candidates demonstrated poor technical knowledge on sampling. They explained what an audit risk is, without linking that to the question requirement. Some were unable to assess the purpose of audit procedure when designing the sample. They lacked the technical knowledge to understand that if the auditor expects to lower the audit risk he should increase the sample size. Most of the answers stated "when the audit risk is high the sample should be high". The candidates should be trained to use the words appropriately as this is a professional exam. The candidates should have written "if the auditor expects a high risk he should increase the sample size in order to lower the risk".

Part (b) It was required to discuss the most appropriate way to select the sample from the given scenario.

Revenue in construction project

Many candidates have not understood that it has a small number of population with high values. They produced irrelevant answers such as;

- Block sampling
- Cutoff procedure

Super outlets

Many candidates have understood that when there is a larger population with small values sample should be selected on random basis but were unable to mention about statistical sampling. Some have written irrelevant answers such as;

- Ensure all records are complete
- Get confirmation from the customers

Question 05

Part 1 This question was based on audit opinions.

(a) It was required to outline types of modified opinions in relation to the circumstances given in the scenario. Most of the candidates have produced satisfactory answers.

(b) It was required to evaluate whether a modified opinion is required for the circumstances stated in the given scenario. Some have written;

- When the financial statements as a whole are not free from material misstatements
- When the auditors are unable to obtain sufficient and appropriate audit evidence to conclude that the financial statements are free from material misstatements
- Not likely to be pervasive

Although the above statements are 'qualifications' they are not linked to the scenario. As a result they have not obtained full marks .They should understand the question requirement. Some have written irrelevant answers such as;

- the company has used the equity method for accounting for the investment
- restrictions imposed by management
- circumstances beyond the control of entity

(c) It was required to discuss the actions that should be taken by the company with regard to the circumstances given in the scenario. There were relevant answers, may be that they have studied the text book. Majority was not able to understand the issue that the management has refused to correct the financial statements and wrote irrelevant answers such as;

- decide the selection of the sample size
- qualify as except for

Question 06

This question is on IT controls and the auditor's responsibilities.

Part (a) It was required to identify two IT general controls and two application controls. There had been similar questions in the past exams. It was disappointing to note that the general performance was not satisfactory. The only relevant answer that the candidates produced for IT controls is the password protection. There were irrelevant answers such as;

- Unit price is updated automatically
- GRN is raised automatically

Some candidates have written following irrelevant answers as application controls

- Use password
- Use ERP system
- Branches are connected to HO

Part (b) It was required to discuss the importance of coordination between IT specialists and the audit team. Many candidates have not discussed the importance of interdependence of IT general controls and application controls. Most of them wrote the importance of having IT specialists as the auditor has no expertise.

Part (c) It was required to analyze fraud risk factors when planning the audit. Most of the candidates produced irrelevant answers such as;

- Check current year details with previous year
- Check subsequent events
- Obtain letter of representation

Part (d) it was required to demonstrate how the auditor responds to the assessed risks of fraudulent financial reporting on inventory and revenue. Many candidates have written irrelevant answers such as;
Inventory
Check valuation
Discuss with management
Revenue
Obtain confirmation from debtors
Inquire from management

Part (e) it was required to prepare an illustration of the audit working papers. There were fairly good answers.

Question 07

Part (a) It was required to assess the potential impact on the audit report arising from the issues in the given scenario. Almost all have identified the issue as going concern assumption but not assessed. Some have written irrelevant answers such as;

- The auditor should modify as an adverse opinion.
- Give an appropriate opinion
- Disqualify the opinion-

Candidates wrote the following ignoring the question requirement

- Recommend suspension of the factory
- As the incident happened after the balance sheet date substantive procedure should be carried out
- Assuming there is capacity in the other factories Ruwanwella operation should be transferred to other factories

Part (b) It was required to outline evidence that the audit team should obtain in determining the material uncertainty. Some candidates have written that the auditor should discuss with the management and evaluate the information in order to assess the ability to continue as a going concern. There were irrelevant answers such as;

- Review subsequent position
- Obtain confirmation from debtors
- Close down the factory

It was observed that the candidates have been prejudiced regarding an actual incidents that happened in Sri Lanka and wrote ignoring the fact that they are answering a question on auditing.

Part (c) It was required to identify audit procedure that the audit team could apply in performing going concern reviews. This part was answered well by some candidates, but most of the candidates have written that the auditor should obtain a written representation stating that all the information relating to going concern has been included in the financial statements. It was observed that such candidates lack the technical knowledge to understand that the letter of representation is obtained in order to support the audit evidence.

Part (d) It was required to outline factors the audit team should consider when assessing representation by management as relevant and reliable audit evidence. Some candidates have explained what the representations are and explained relevance and reliability separately. It reflected that the candidates have misunderstood the question. Some have produced irrelevant answers such as;

- Inquire from management
- Check the integrity of management
- Inspect board minutes
- Get industry norms
- Discuss with local government authorities

Part (e) It was required to outline the actions that the auditor should take when management does not provide written representation. Most of the candidates wrote to

- Modify the opinion.
- Take legal action

It reflected that they lack the technical knowledge.

Part (f) It was required to explain the difference between a positive confirmation request and a negative confirmation request. This part was poorly answered. Candidates produced irrelevant answers such as;

Positive-

- Confirm existence
- Confirm if correct only
- Financial statements are free from material misstatements

Negative
To obtain details
If the balance is negative
Financial statements do not comply with reporting framework

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KB5 – Business Value Creation

December 2016

Examiner's Comments

Question-wise comments

General comments

Overall performance of the candidates was good. This question carries 10 marks and requires;

(a) to assess the power and interest of stakeholder groups of 'REL' using stakeholder mapping.
(b) to discuss how the management could react to the concerns of the stakeholder groups.

Specific comments

Question 01

(a) Some correctly have understood that stakeholder mapping is a method of understanding the interest and power of different stakeholders in order to respond to the concerns of each group of stakeholders. Nevertheless some identified "government" as a "high-powered and low interested" stakeholder group. They did not mention that based on the magnitude of the protest under reference that the government might become interested in the project. Most of the students were unable to group "Green friends" as a "high-powered" stakeholder.

(b) Some students correctly stated that the management needs to consider the views of major shareholders and "*Green friends*" and citizens of Lakeside district are to be provided with relevant information taking into consideration the level of interest and the power wielded. Some mentioned that stakeholders are to be handled carefully rather than specific ways of handling being stated.

Question 02

General Comments

Overall performance of the candidates was good. This question carries 10 marks and requires;

(a) to outline the costs of the current approach to inventory management.
(b) to demonstrate how a JIT system and a Warehouse Management System (WMS) could assist in overcoming the current issues.

Specific comments

(a) Some students stated correctly that high working capital investment, high cost of inventory maintenance, customer dissatisfaction etc. as costs of the current approach. Nevertheless some stated that "Cost of labour", 'Cost of depreciation' etc. without elaborating as to how such costs emanate. A few mentioned "Cost of maintaining high inventory" without examples being cited, which earned only a few marks.

(b) A fair number of students demonstrated that JIT system could help to reduce inventory holding cost and non-moving inventory. They also mentioned JIT could lower warehousing cost if properly applied. But a few students just mentioned JIT will eliminate customer complaints etc. which earned a few marks only.

Best use of storage space, efficiency in storing, use of RFID/bar coding to track the products in the warehouse are some benefits derived from WMS to address the concerns in question, as per some students who earned full marks. But some did not cite ways and means of automation that is used in the WMS and as to how efficient storing takes place in a WMS.

Question 03

General Comments

Overall performance of the candidates was good. This question carries 10 marks and requires students;

(a) to explain 3 advantages, if Cooler Ltd. moves from leader strategy to follower strategy.
(b) to outline the stages when introducing next innovation by Cooler Ltd.

Specific comments

(a) Followers could lower product design & development cost, research and development cost and could reduce uncertainty about sales demand and market size. Some have pointed out the advantages of follower-strategy without relating these to the scenario given. Some stated advantages of leader-strategy instead of that of follower-strategy.

(b) Idea generation and screening, Concept development and testing, Business analysis, Beta testing and Market testing, Technical implementation, Launching the product and Post review are the stages of new product development. Some listed out the stages without a summary of significant features being outlined. Some students dropped certain stages while some did not provide the stages in the correct order. A few listed only some stages.

Question 04

General Comments

Overall performance of the candidates was satisfactory. This question carries 10 marks and requires students;

(a) to explain how to improve the value chain of "Bestsellers" using information technology.
(b) to outline the information technology infrastructure needed at "Bestsellers".

Specific comments

(a) IT systems like ERP, RFID, EPOS, CRM etc. could be used by "Bestsellers" in the primary activities namely inbound logistics, operations, outbound logistics, marketing, sales & services. Intranet, E-procurement could be used in the secondary activities namely firm's infrastructures, HRM, Technology development & Procurement. Some have just explained the value chain activities without reference being made to the requirement of use of IT by "Bestsellers".

(b) Standalone Computers, Networks, Connected devices, Internet, Intranets & Extranets centralized or decentralized processing are IT infrastructures that will be needed by "Bestsellers". Some incorrectly outlined computers, printers, software, data server etc. as IT infrastructure.

Question 05

General Comments

Overall performance of the candidates was satisfactory. This question carries 10 marks and requires students;

(a) to outline the advantages and disadvantages for Perera & Co. in using interviews as a selection method.
(b) to explain hygiene factors and motivator factors in relation to staff of Perera & Co.

Specific Comments

(a) Ability to test culture/discipline & proficiency, allowing two way communication and adaptability are some of the advantages. Artificial situation & inexperienced interviewers, halo effect & contagious bias are some disadvantages of interviews. Some were of the wrong view that interviews are costly. Some stated that interviews are a good method to select the best without providing justifications.

(b) Working conditions, job security, company policy and salaries are some hygiene factors and challenging work, career advancement, sense of achievement and additional pay are some motivator factors. Most of the students did not mention that hygiene factors cause dissatisfaction if individual needs are not met and then employees need to be motivated with motivator factors. Some wrongly identified payment of salaries as a motivator factor.

Question 06

General comments

Overall performance of the candidates was poor. This question carries 25 marks and requires students;

(a) to discuss whether 'SPL' should position the new product line under the Sunshine brand or a new brand name providing justification
(b) to explain the requirements for successful brand positioning
(c) to demonstrate the possible application of the promotional mix
(d) to recommend appropriate pricing strategy and method of distribution.

Specific comments

(a) Declining trend of present brand in urban areas is observed. Health and safety standards of the existing products are not environmental friendly which is a concern of urban community. Therefore, Sunshine can hold their present customer base in rural areas and attract urban customers to a new brand. Some argued that SPL should position the new product line under the existing Sunshine brand, since it has a good market share and people are well aware of the existing brand. But those students have ignored the fact that requirements and concerns of urban people are different from those of rural areas.

(b) Some have correctly explained relevance, clarity, coherence and patience as requirements for successful brand positioning. Some just listed out the requirements without any explanations. Some stated that a successful brand should be easy to understand and pronounce, to be widely made known etc. which earned only a few marks.

(c) Advertising, sales promotion, public relations, direct marketing, personal selling are some of the promotional mix, Sunshine Ltd. could apply to promote new product line. Some have given only examples of promotion mix of advertising i.e. television, cinema, radio, newspapers, and other elements in the promotional mix were not demonstrated by them. Some have listed out elements of promotional mix but not given examples.

(d) More suitable pricing strategy would be price skimming strategy and a selective distribution method using leading supermarket chains which will reach professional categories in urban areas would be more appropriate. Some argued charging lower price than competitors would be better and also extensive distribution was recommended which earned no marks.

Question 07

General comments

Overall performance of the students was poor. The question carries 25 marks and requests students;

(a) to discuss how to overcome the resistance to change when implementing new strategy.
(b) to explain how the "Four actions framework" can be used in developing the proposed blue ocean strategy.
(c) to discuss the importance of measuring both financial and non-financial performance.
(d) to outline indicators for both financial and non-financial performance that can be adopted by 'Plastex' in the future.

Specific comments

(a) Most of the students discussed the Lewin's three stage model but some were unable to discuss it in relation to the given scenario. Some were unable to state the fact that staff should understand the negative consequences if intended change does not take place.

(b) Some listed out four action framework namely, Reduce, Create, Raise & Eliminate. But most of them could not explain them in relation to the given scenario. For e.g. most of the students did not mention that recycled products could be a new feature added by 'Plastex' under "Create".

(c) Financial performance is a measure of what has happened in the past and used to compare with that of budget. Non-financial performance deals with customer satisfaction, quality, product innovation etc. which is a guide to the future and long-term objective. Only a few could indicate that financial indicators are not necessarily a good guide to achieve long term objectives. Some wasted their valuable time by calculating and comparing among the years provided in the scenario, the cost of sales ratio, SP, NP ratios etc. under this part of the question. Some cited Goodwill, Brand name, Market share etc. as non-financial indicators which were not to the expectations of the examiner.

(d) Cost of sales as a percentage of sales, sales & distribution OH as a percentage of sales, SP margin & NP margin are main financial performance indicators. Recycled products as a percentage of total products, amount of new products introduced during the year are some important indicators of non-financial performance. Some stated employee satisfaction, customer awareness as non-financial indicators which earned no marks. A few identified annual preparation of financial statements, annual budgets as financial indicators which earned no marks.