OBJECTIVES OF THIS REPORT

This report has been compiled from the analysis of examiners on candidates’ performance in Part I of the Qualifying Examination, which was written in January 2010. Its objectives are to –

- assist unsuccessful candidates in identifying those areas in which they lost marks and need to improve their knowledge and/or presentation; and
- assist future exam candidates, by providing a commentary for them to use when working through past papers.

To accomplish these objectives, the report provides background information on how the examination questions are chosen, marked and adjudicated, comments on general shortcomings in answers and specific comments on each question of the two examination papers.

The purpose of Part I of the Qualifying Examination is to test the integrated application of cognitive knowledge, preferably as soon as possible after the prescribed academic requirements have been met.

The remainder of this report is discussed under the following headings:

- Statistics for Part I of the Qualifying Examination 2010
- Background information on the setting, marking and adjudication of SAICA examinations
- General comments on Part I of the Qualifying Examination 2010
- Professional paper 1 – detailed comments by question
- Professional paper 2 – detailed comments by question
STATISTICS FOR PART I OF THE QUALIFYING EXAMINATION 2010

<table>
<thead>
<tr>
<th></th>
<th>% Pass</th>
<th>Passed</th>
<th>Failed</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>First attempt</td>
<td>73%</td>
<td>1 239</td>
<td>450</td>
<td>1 689</td>
</tr>
<tr>
<td>Repeat candidates</td>
<td>21%</td>
<td>253</td>
<td>979</td>
<td>1 232</td>
</tr>
<tr>
<td>All candidates</td>
<td>51%</td>
<td>1 492</td>
<td>1 429</td>
<td>2 921</td>
</tr>
</tbody>
</table>

Average marks per question

<table>
<thead>
<tr>
<th></th>
<th>Question 1</th>
<th>Question 2</th>
<th>Question 3 Part A</th>
<th>Question 3 Part B</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Paper 1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total marks</td>
<td>60</td>
<td>75</td>
<td>25</td>
<td>40</td>
<td>200</td>
</tr>
<tr>
<td>Average marks</td>
<td>33,88</td>
<td>31,53</td>
<td>13,07</td>
<td>22,76</td>
<td>101,24</td>
</tr>
<tr>
<td>Paper 2</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total marks</td>
<td>60</td>
<td>40</td>
<td>40</td>
<td>60</td>
<td>200</td>
</tr>
<tr>
<td>Average marks</td>
<td>30,85</td>
<td>17,78</td>
<td>19,15</td>
<td>27,70</td>
<td>95,48</td>
</tr>
</tbody>
</table>

More detailed statistics can be found on the SAICA website at [www.saica.co.za](http://www.saica.co.za).
BACKGROUND INFORMATION ON THE SETTING, MARKING AND ADJUDICATION OF SAICA EXAMINATIONS

The Examinations Committee constantly strives to improve its ability to determine whether candidates demonstrate a readiness to continue with their accounting education and training. This is done by means of an ongoing process of evaluation and improvement of the way in which it selects questions for inclusion in the examination and decides on the final mark plans.

1 Source of the questions

The Examinations Committee, a sub-committee of the SAICA Initial Professional Development Committee (Education Committee), takes overall responsibility for the setting of the examination paper. Examination questions could be drawn from different sources:

- Questions may be submitted by practitioners, accountants in commerce and industry, as well as academics. These questions are added to a question pool that has been built up over the years and from which questions may be selected; or
- Questions on a particular subject may be commissioned from persons in commerce and industry or public practice or from academics.

Academics or former academics are also involved in reviewing exam questions in each of the core subject areas. Academics who have any involvement whatsoever in the presentation or otherwise of Board courses may NOT act as reviewers. These academics or former academics are appointed by core subject area and their role is to –

- review questions for conceptual problems and consistency in use of terminology;
- give an indication as to whether the relevant examination questions are set at an appropriate level;
- provide comments on whether the number of marks and time limit are appropriate; and
- provide comments on the validity and reliability of such assessment.

In addition two external examination sitters, who are independent of the exam setting process, are appointed to review the entire set of questions after the review from the academics has taken place. The examination sitters provide independent comments on the examination paper, suggestion solutions or mark plans and report back to the Examinations Committee.

SAICA would like to acknowledge and thank all the people involved in the examination setting process. An alphabetical list of all the people involved in various roles, including members of the Examinations Committee, question composers, subject specific reviewers and external examination sitters, is as follows:

- Greg Beech
- Mike Benetello
- Graeme Berry
- Kim Bromfield
- Helouise Burger
- Melanie Cope
- Fred de Hart
- Dewald Joubert
- Chauke Khongelani
- Ben Marx
- Lindsay Mitchell
- Chantyl Mulder
2 Security and confidentiality of examination papers

The examination papers for each year are compiled, printed and sent to each examination centre under very stringent conditions of security. The only persons who know the contents of a particular paper are the members of the Examinations Committee. They are all selected with great care regarding their integrity and professional standing and are sworn to secrecy.

2.1 Marking of the scripts

The Initial Professional Development Committee (Education Committee) devotes a great deal of time to the review and refinement of mark plans to ensure that the plans are consistent with its expectations for each question.

Before marking of the scripts commences, copies of the examination papers and suggested solutions are forwarded to all participating universities for comment. The markers and umpires decide on a suggested solution and mark plan once all these comments have been considered and a test batch of scripts has been marked. The suggested solutions, mark plans and test batch results are then reviewed by the Initial Professional Development Committee (Education Committee), which authorises the final suggested solutions and the mark plans that will be used in the marking process.

All markers and umpires have to sign a declaration of secrecy regarding the handling of scripts, questions, solutions and mark plans. SAICA holds the copyright of the solutions and mark plans, and they are returned to SAICA together with the mark lists once the marking has been completed.

Each marking team consists of a number of individuals (comprising academics, practitioners and representatives from commerce and industry) and an umpire, who are on the whole fully bilingual and equally capable of marking both English and Afrikaans scripts.

Each script is marked independently by two different persons who record their marks on separate mark sheets. Once the marking has been completed, the markers confer and jointly decide on the final mark to be awarded. Then each marker's mark, as well as the compromise mark, is noted down on the cover of the script. In the event of the markers being unable to agree upon the number of marks to be awarded for a particular answer, the script is referred to the umpire, who then awards the final mark.

In view of the above stringent marking process no request for re-marks will be entertained.
2.2 Adjudication

Adjudication is done by the full Initial Professional Development Committee (Education Committee) as soon as possible after the mark lists have been received and checked by the SAICA secretariat.

The members of the Committee do not know the candidate names at the time the adjudication process takes place.

During the adjudication process, the Initial Professional Development Committee (Education Committee) considers all relevant evidence, including the following:

- Whether there were any time constraints encountered by candidates;
- The level of difficulty for each question;
- Possible ambiguity in the wording or translation; and
- Any other problems that may have been encountered relating to the examination.

It is important to note that no person from the academe who is a member of SAICA’s (Initial Professional Development Committee (Education Committee) is allowed to serve on the Examinations Committee, and that candidates’ anonymity is preserved until the final adjudication has been completed.

In order to ensure that the whole marking and adjudication process remain anonymous, the instructions to candidates clearly state that their names should not appear anywhere on their scripts.
GENERAL COMMENTS ON PART I OF THE QUALIFYING EXAMINATION 2010

1 Objective

In view of the primary objective of Part I of the Qualifying Examination, namely to test the integrated application of cognitive knowledge, candidates are tested on their ability to –

- apply the knowledge specified in the subject areas set out in the prescribed syllabus;
- identify, define and rank problems and issues;
- analyse information;
- address problems in an integrative manner;
- exercise professional judgement;
- evaluate alternatives and propose practical solutions that respond to the users’ needs; and
- communicate clearly and effectively.

2 Overall comments on the papers

Overall comments received from universities indicated that the papers were of an appropriate standard for Part I of the Qualifying Examination.

- The accounting questions were of a good standard, as can be expected for Part I of the Qualifying Examination. The accounting questions were adequately integrated between accounting topics and also incorporated knowledge relating to taxation and management accounting. The questions required candidates to have a good knowledge of and solid foundation regarding the basic principles underlying the topics. Topics examined were relevant and of importance both in practice and in the academic syllabus. Part I of the Qualifying Examination is known for testing knowledge and principles by way of pro-forma journal entries, and the importance of pro-forma journal entries is also stressed in the list of examinable accounting pronouncements issued annually by SAICA. However, many candidates still performed poorly in this question.

The integrated question in Paper 2 dealt with issues that are commonly encountered in practice. The question tested the candidates’ ability to integrate their knowledge across topics and subjects and to plan their answers within the time allocated to each section of the question. The question was generally viewed as being at an appropriate level of difficulty by all the major universities. Despite this, the question was answered poorly by majority of the candidates, it would seem as a result of a lack of basic knowledge and poor examination technique.

- The tax questions were of an appropriate to high standard with most of the candidates passing the tax question in Paper 1. The overall question comprehensively covered a number of general taxation issues from the academic syllabus. Despite this, candidates did not score as well as expected and markers continue to comment on the lack of candidates’ basic and current tax knowledge.

- The management accounting and financial management questions were adequately integrated with financial accounting topics. The standard of the questions was considered moderate to easy and appropriate for the questions in Paper 1 and 2. The quality of answers was better than in previous years, but despite this, the questions were not answered to the standard required of a candidate writing Part I of the Qualifying Examination. Again, it seems as if the poor performance may be ascribed to a lack of basic knowledge and poor examination technique. Presentation in general was poor, both with regard to commentary and calculations. Candidates did not structure their solutions in a coherent manner that showed a logical thought
path. Linking of theoretical points to the scenario was poor and discussion of the questions in the context of the current economic climate was poorly handled by most candidates.

- The **audit question** was challenging but of a fair and appropriate standard for Part I of the Qualifying Examination. The question tested a wide variety of auditing and governance aspects of the syllabus in a practical situation. The question addressed the important phases of the audit process, namely planning, internal controls, substantive procedures and reporting. The question was reasonably well answered by the candidates who attempted it and applied themselves to the information of the question and the requirements thereof.

The sections on ethics and corporate governance as well as on the Companies Act were well answered. Candidates battled to identify key controls, or failed to provide proper explanations why such controls would reduce the risk of material misstatement. Similarly, the section dealing with the impact of the penalty on the audit report was poorly answered. Candidates who regurgitated “shopping lists” of information did not score marks.

3 Specific comments

From a review of candidates’ answers to the six examination questions for the January 2010 examination the general deficiencies set out below were identified. These problems affected the overall performance of candidates, and it is a matter of concern that candidates make the same mistakes every year. Although these aspects seem like common sense, candidates who pay attention to them are likely to obtain better marks, and it may even turn a low mark into a pass.

3.1 Application of knowledge

A serious problem experienced throughout the examination was that candidates were unable to apply their knowledge to the scenarios described in the questions. Many responses by candidates were a “shopping list” of items – this being a pure regurgitation of what candidates may have learnt about the theory at university, but of no real relevance to the question in hand. Candidates also do not appear to identify the correct issues in the scenario provided.

This is a major concern, because by the time candidates qualify for entry to these examinations, one would expect them to have assimilated the knowledge, at least to the extent of being able to apply it to simplified facts as set out in an examination question. Obviously, candidates who are unable to identify the correct issues do not do well in the examination.

3.2 Workings

It is essential that candidates show their workings and supply detailed computations to support the figures in their answers. Marks are reserved for methodology, but can only be awarded for what is shown. In many instances workings were performed by candidates but not cross referenced to the final solution. Once again, markers could not award marks as they were unable to follow which working related to which part of the final solution. Candidates must ensure they show their workings and that these are properly and neatly cross referenced to the final solution.
3.3 Communication

Candidates fared better in questions requiring calculations than in discursive questions. It is important that candidates note that written answers are a large component of the Qualifying Examination, because written communication is a key competency required in the workplace. Candidates should learn to answer discursive questions properly. This can be done by practicing exam-type answers under exam conditions in preparation for the examination.

In addition markers found that candidates used their own abbreviations (SMS messaging style) in their answers. Marks could not be awarded here as it is not up to the markers to interpret abbreviations that are not commonly used. The increased use of an SMS style of writing in a professional examination it is a major concern. Candidates should pay specific attention to the way in which they write their answers, and bear in mind that this is a professional examination.

3.4 Journal entries

A fundamental part of financial accounting is an understanding of debits and credits. A means of assessing whether a candidate understands the fundamental principles is to require the candidate to prepare the relevant journal entries. Candidates increasingly do not understand what journal entries they need to process. In many instances basic journal entries were processed the wrong way around. In addition, account descriptions were poor and abbreviations were used.

This is inexcusable and candidates must ensure that they understand what impact transactions would have on specific account balances, by showing that they know which account in the income statement or balance sheet has to be debited or credited. It is not sufficient for a candidate with Accounts IV to be a technocrat – understanding of the fundamental principles of accounting is critical to the success of a candidate at a Part I level.

3.5 Time management

Candidates are advised to use their time wisely and budget time for each question. The marks allocated to each question are an indication of the relevant importance the examiners attach to that question and thus the time that should be spent on it. Candidates should beware of the tendency to spend too much time on the first question attempted and too little time on the last. They should never overrun on time on any question, but rather return to it after attempting all other questions.

3.6 Layout and presentation

Candidates should allocate time to planning the layout and presentation of their answers before committing thought to paper. Very often, candidates start to write without having read the question properly, which invariably leads to, for example, parts of the same question being answered in several places or restatement of facts in different parts. Marks are awarded for appropriate presentation and candidates should answer questions in the required format, that is, in the form of a letter, memorandum or a report, if this is what is required.

The quality of handwriting is also an ongoing problem and was of particular concern in this year’s examination. The onus is on the candidate to produce legible answers.

Separate books are used to answer each question of the Qualifying Examination. Each book is clearly marked and colour coded. Candidates are given explicit instructions to write the correct answer in the correct book. Despite this some candidates did not write the correct answer in the correct book which resulted in delays in the marking as the correct question had to be found and
then sent to the correct mark team. However, despite the extra work involved, the secretariat has made quite sure that candidates who wrote answers in the incorrect book were nevertheless marked.

3.7 Irrelevancy

Marks are awarded for quality, not quantity. Verbosity is no substitute for clear, concise, logical thinking and good presentation. Candidates should bear in mind that a display of irrelevant knowledge, however sound, will gain no marks.

3.8 Recommendations / interpretations

Responses to these requirements are generally poor, either because candidates are unable to explain principles that they can apply numerically or because they are reluctant to commit themselves to one course of action. It is essential to make a recommendation when a question calls for it, and to support it with reasons. Not only the direction of the recommendation (i.e. to do or not to do something) is important, but particularly the quality of the arguments – in other words, whether they are relevant to the actual case and whether the final recommendation is consistent with those arguments. Unnecessary time is wasted by stating all the alternatives.

3.9 Examination technique

Examination technique remains the key distinguishing feature between candidates who pass and those that fail. Many candidates did not address what was required by the questions and, for example, answered questions in words where calculations were required or presented financial statements where a discussion of the appropriate disclosure was required.

3.10 Open-book examination

Candidates are reminded that they MUST familiarise themselves with SAICA’s open book policy and be aware that this may differ from that of their CTA university. Candidates are also reminded that only SAICA has the authority to interpret its own open book policy. To this end candidates are advised of the following:

- **No loose pages** (of any kind) may be brought into the exam. This includes index pages which were seen by some candidates in this year’s exam not to “supplement texts” and therefore considered acceptable; and
- Candidates are advised to familiarise themselves with SAICA exam rules prior to writing the examination.

Another problem relating to the open-book examination was that candidates did not state the relevant theory and/or definitions in their answers. One cannot build a logical argument without using the theory as a base and starting point. Reference to theory and definitions is essential to create the perspective from which the question is answered and is required to enable markers to follow the argument. However, since candidates have this information at hand, marks are not awarded for stating detailed definitions only. This type of examination does affect the answer that is expected and application and demonstration of insight into the use of the definition have gained in importance.

Candidates should also remember that one has to be very well prepared for an open-book examination. There is not enough time in the examination to look up all information from the texts. In certain aspects one would be expected to offer an immediate response based on embedded
knowledge. Complex information needs to be fully understood before the examination. Candidates who enter the examination hoping to look up data that they have not processed in advance will be at a disadvantage as they are unlikely to finish the papers.

In conclusion, a message to those who were unfortunately not successful in the examination:

*Please start preparing for next years’ examination in good time.* Don’t give up - sufficient preparation and a review of the basics will stand you in good stead for next year’s exam!

*Best of luck!!*
Paper 1 consisted of three questions that dealt with the following aspects:

**Question 1**
This question was solely a taxation question, counting 60 marks in total. The question required candidates to calculate the taxable income of a company by commencing with the net profit that was given in the question.

**Question 2**
The question was a 75-mark audit question, dealing with the risk of material misstatement, audit response, key controls, substantive procedures and audit qualification and reporting. The question also included integrated aspects of ethics, corporate governance and the Companies Act.

**Question 3**
The question was a 65-mark integrated question, examining aspects from the financial accounting and management accounting core disciplines.

**Part A**
Part A consisted of 25 marks of financial accounting, testing candidates’ understanding of revenue recognition and measurement criteria. Candidates were required to discuss the application of the financial accounting principles in IAS 18 and IFRIC 13.

**Part B**
Part B consisted of 40 marks of management accounting, which covered business strategy, variable costing calculations, calculation of financial ratios and a discussion on the allocation of head office costs.

Presentation marks were available for all three questions. These marks were clearly and separately stated in the “required” sections of each question.
QUESTION 1

<table>
<thead>
<tr>
<th>Maximum mark</th>
<th>Average mark</th>
<th>Marks &gt; 50%</th>
<th>Marks &lt; 50%</th>
</tr>
</thead>
<tbody>
<tr>
<td>60</td>
<td>33.88</td>
<td>1 854 candidates</td>
<td>1 067 candidates</td>
</tr>
</tbody>
</table>

Level of difficulty

The question was adequately integrated and set at an appropriate level of difficulty for Part I of the Qualifying Examination.

Main subjects / topics examined in the question

The question required the candidates to calculate the taxable income of a company by commencing with the net profit that was given in the question. It dealt with a number of issues, as will be clear from the specific comments below.

The individual items examined were the following:

- The allowances granted on depreciable assets.
  - These assets included a second-hand plant which was acquired from a connected person. This required the candidates to determine the value to be used for purposes of the allowance in terms of section 23J.
  - It also included computer equipment that was acquired to replace damaged computer equipment, with the replacement assets having been acquired from the insurance proceeds.
- Interest incurred in terms of a suspensive sale agreement.
- Share-dealing transactions – the taxpayer held a portfolio of shares for speculative purposes, but some of these were disposed of after they had been held for more than three years. Research and development – the expense incurred could be deducted in terms of section 11D(1) at 150% of the amount and the assets were to be written off over three years (50%:30%:20%). This part included a “donation to a recognised university” in respect of which the required “section 18A” receipt was obtained. The research was abandoned during the year relevant to the examination question and candidates had to deal with the tax consequences thereof.
- Share investments – this included the treatment of exempt dividends and the denial of the interest paid in respect thereof as a deduction for tax purposes. It also dealt with interest paid to derive foreign dividends, and the interest in this case qualifies for deduction, but the deduction is limited to the foreign dividend received.
- Allowances relevant to factory buildings which were disposed of, with the proceeds being used to erect a building on leasehold land.
- Purchase of raw materials – relating to section 23F (trading stock not on hand at year end).
- Capital gains – in respect of most of the assets mentioned above there were disposals and candidates had to address the capital gain or loss consequences as well.

General comments

This question was generally well answered by the candidates and they used a logical layout in doing so. Many candidates did not show all the relevant calculations or did not do the calculations together with the answer.
Areas the candidates handled well

The question required the candidates to commence with net profit and they generally obtained the marks relevant to the principle of adding back items where the tax treatment differed from the accounting treatment. However, see the section below.

Candidates also had few problems in dealing with the allowances available to the taxpayer in respect of the cost (or value) of depreciable assets. A small number of candidates used the wrong rates for the allowances.

The section 11D allowances relating to the research and development expenses and assets were also handled well by the majority of the candidates.

The application of sections 23H and 23F was generally correct.

Areas the candidates handled poorly

Although the way in which candidates were required to present their answer (to commence with net profit) was generally handled well, candidates in many cases made mistakes later in their answers. These included deducting an amount where an addition was required and doing the calculations, but not including the result thereof in the tax calculation.

Some candidates did not know the difference between an instalment sale agreement and a finance lease.

Most candidates did not apply section 13(3) – this requires the cost of the replacement building to be reduced by the recoupment.

Quite a few candidates awarded the company the R3 500 exemption in respect of foreign dividends despite the fact that this is only available to natural persons.

While most candidates could perform the capital gain calculations, many did not know that it must be aggregated before the taxable capital gain is included in taxable income. Many candidates did not deduct the relevant recoupment from the receipt when the proceeds were calculated for purposes of the capital gains tax (CGT).

Many candidates were unsure when allowances had to be apportioned, in the case of for example section 11(f) and section 11(g), and made mistakes in doing so. Some candidates apportioned deductions where no apportionment was required.

In the case of the sale of the Bombay shares, candidates either handled the treatment very well, or applied the item completely incorrectly. From the information given in the question, it was clear that these shares had been held for longer than three years and the application of section 9C should therefore have been considered. As there was no information regarding the resident status of this company and it was not clear whether it was listed as required by the Act, candidates had to deal with this before providing the answer. The candidates had to make the assumption that Bombay was not a resident and dual listed to apply section 9C, or had to state that it was not, if they did not apply section 9C. Those candidates who applied section 9C often forgot to recoup the deduction relating to the opening stock.
Specific comments on sections of the question

The question consisted of one section only and required of the candidates to calculate the taxable income of a company by commencing with the net profit that was given in the question.
QUESTION 2

<table>
<thead>
<tr>
<th>Maximum mark</th>
<th>Average mark</th>
<th>Marks &gt; 50%</th>
<th>Marks &lt; 50%</th>
</tr>
</thead>
<tbody>
<tr>
<td>75</td>
<td>31.53</td>
<td>760 candidates</td>
<td>2 161 candidates</td>
</tr>
</tbody>
</table>

Level of difficulty

It is considered to be a well set question, with adequate topic coverage of the syllabus. The aspects examined were also of importance and relevance, integrating various topics effectively. This view is supported by the various university comments.

Main subjects / topics examined in the question

The question consisted of 75 marks of auditing, dealing with the risk of material misstatement, audit response, key controls, substantive procedures and audit qualification and reporting. It also integrated aspects of ethics, corporate governance and the Companies Act.

General comments

The question was reasonably well answered by those candidates who attempted it and applied themselves to the information in the question and the requirements thereof. It was, however, disappointing that some candidates neglected the question and did not make an asserted effort to answer it and accordingly received very low marks.

Examination technique was, as in previous years, a problem. Many candidates did not read and consider the information of the question carefully, as was evident from the fact that many candidates treated the IT rental equipment as inventory, instead of property, plant and equipment. Candidates also often made statements, rather than describing risks, audit procedures, etc.

Areas the candidates handled well

The section on ethics and corporate governance as well as on the Companies Act was well answered.

Areas the candidates handled poorly

Many candidates battled to identify the key controls, or failed to provide proper explanations for why such controls would reduce the risk of material misstatement. Similarly, the section on the impact of the penalty on the audit report was poorly answered.

Specific comments on sections of the question

Part (a)

Part (a) of the question counted 14 marks and dealt with (i) the identification and discussion of the risks of material misstatement at the financial statement level (7 marks), and (ii) the overall audit response to address these risks (8 marks).

This section was reasonably well answered although it was evident that many candidates do not understand the difference between financial statement and assertion level risk. Candidates also did not always focus on the overall response to the risks, but rather provided audit procedures for the risks.
Part (b)
This part of the question counted 7 marks and dealt with the risks of material misstatement of the valuation and allocation assertion of IT rental equipment.

Although candidates did reasonably well in the section, some did not address only the valuation assertion as was requested, but also other assertions. Very general risks were also often given, without motivating why it would be applicable to the scenario, for example stating there is a risk of obsolescence, without linking it to the information given in the scenario that it is IT equipment, which has a technical nature.

Part (c)
Part (c) of the question counted 12 marks and required of candidates to identify the key controls that were in place to address the existence assertion applicable to IT rental equipment, and to explain why each of these controls would reduce the risk.

Candidates battled with this section and had difficulty in identifying and explaining the key controls.

Part (d)
Part (d) counted 12 marks and required of the candidates to discuss the audit procedures to reduce the risk of material misstatement for the completeness assertion of the IT rental equipment.

This section was answered poorly. Candidates did not apply themselves to the information of the question by providing relevant audit procedures (test of controls and substantive tests) to address the completeness assertion. Candidates often also failed to provide audit procedures, and merely made statements regarding aspects to audit.

Part (e)
Part (e) of the question counted 10 marks and required that candidates discuss the impact of the R100 million penalty on (i) the financial statements and (ii) the audit report. This should have been presented in the form of a memorandum addressed to the partner.

Although candidates did well in discussing the impact on the financial statements, they did poorly in the section dealing with the impact on the audit report. Candidates appear to have a basic understanding of audit qualification aspects, but failed to apply it logically to the information of the scenario.

Part (f)
Part (f) counted 4 marks and required a discussion of the corporate governance and ethical considerations regarding the conduct of the financial director. This section was well answered.

Part (g)
Part (g) counted 11 marks and required an identification and discussion of the areas of non-compliance by New Era in terms of the Companies Act. This section was well answered.

Presentation
This counted 5 marks, which were awarded for the memorandum format (2), logic and language use (1), layout and presentation (1) and handwriting (1).
QUESTION 3 PART A

<table>
<thead>
<tr>
<th>Maximum mark</th>
<th>Average mark</th>
<th>Marks &gt; 50%</th>
<th>Marks &lt; 50%</th>
</tr>
</thead>
<tbody>
<tr>
<td>25</td>
<td>13.07</td>
<td>2 096 candidates</td>
<td>825 candidates</td>
</tr>
</tbody>
</table>

Level of difficulty

This was a 25-mark question. The level of difficulty of the question has been assessed per section:

**Part (a) – 13 marks**

This is a level 1 question and the standard was considered to be appropriate. The candidates should have obtained high marks as the majority of marks were awarded for discussion and application of basic IAS 18 theory and principles.

**Part (b) – 10 marks**

The question was fair and set at the appropriate level of difficulty. The majority of the marks could be obtained through quoting from the applicable standard as marks were awarded for explanation of the theory in IFRIC 13 with limited marks for high level application. As such candidates could have earned 6 out of the 10 marks simply for quoting paragraphs 5–7 of IFRIC 13.

The question was straight forward, well structured with no identified ambiguities, and was considered easy to moderate in terms of the overall level of difficulty.

**Main subjects / topics examined in the question**

The question integrated financial reporting and management accounting, and tested the candidates’ understanding of revenue recognition and measurement criteria. The financial accounting principles in IAS 18 and IFRIC 13 were tested by requiring candidates to discuss the application thereof.

**General comments on the quality of candidates’ answers**

**Part (a)**

The quality of the answers was poor to average and specific examples have been outlined below:

- The candidates did not address all revenue categories and thus did not obtain the maximum marks, for example very few candidates identified or discussed the revenue arising from discount purchases.
- The candidates often did not apply the theory to the question, for example the measurement of deferred income was poorly handled and was not addressed by many candidates. It also appeared as though some candidates wrote down any theory which might be applicable to the question, without really applying it to the information given.
- There was a strong tendency to focus on measuring the different components against the recognition requirements of IAS 18.14 or .20, which would be sufficient at a second-year level, but not at a Board level (a maximum of 3 marks was awarded for this).
- Candidates showed poor planning of the solution with evidence of mind dumps, with little evidence of having thought through or planned the process before attempting the question. Candidates often started out with one argument and ended up with a totally different point of view.
Part (b)
The quality of the answers was average to fair given the nature of the question. However, candidates did not score as well as expected in this section; specific examples have been outlined below:

- Although there was still poor planning, layout and time management, this was slightly better than in part (a). For example, a number of candidates spent more time on the parts of the question relating to finance, which negatively impacted on the marks achieved for this section.
- Quite a few candidates supported their discussions with journal entries which were not required.
- Some candidates failed to address all the accounting issues of the customer loyalty programme. A number of candidates did not identify IFRIC 13 as being applicable, which resulted in them basing their solutions on whether or not the loyalty programme was a liability in terms of the Framework.
- Few candidates considered the application of the recognition and measurement criteria of IFRIC 13. The solution included marks for a number of specific issues that very few candidates identified.

Presentation

Two marks were awarded for arrangement and layout as well as clarity of expression and language usage.
QUESTION 3 PART B

<table>
<thead>
<tr>
<th>Maximum mark</th>
<th>Average mark</th>
<th>Marks &gt; 50%</th>
<th>Marks &lt; 50%</th>
</tr>
</thead>
<tbody>
<tr>
<td>40</td>
<td>22.76</td>
<td>1 629 candidates</td>
<td>1 292 candidates</td>
</tr>
</tbody>
</table>

Level of difficulty

Question 3 Part B was a moderate to easy management accounting question. However, it was integrated into a financial accounting question and it may have proved challenging for candidates to switch mindsets in answering the question as a whole.

Main subjects examined in the question

The question was a 40-mark question, including 2 presentation marks, which covered:
- Business strategy (10 marks);
- Variable costing calculations (16 marks);
- Calculation of financial ratios (6 marks); and
- A discussion on the allocation of head office costs (6 marks).

General comments

Parts (c) and (f) required candidates to identify and discuss/describe issues, and the mark plan awarded 1 mark for correct identification and 1 mark for explaining each valid observation. The brevity of many answers was disappointing, with many candidates only scoring 1 mark for identifying an issue and failing to adequately explain the issue.

Areas the candidates handled well

Candidates performed adequately but no section was generally well answered.

Areas the candidates handled poorly

Specific comments on each of these sections are detailed below. Part (f) in particular was poorly answered.

Specific comments on sections of the question

Part (c)

This part of the question required candidates to identify and describe the potential advantages and disadvantages of selling use of a golf driving range through annual memberships. As stated previously, many candidates failed to adequately explain valid advantages and disadvantages which they had identified, as a result only scoring 1 mark when 2 were available for each valid aspect.

Some candidates repeated the same observation in different words, wasting valuable time.

Part (d)

Candidates were required to calculate the net profit for the Golf Driving Range and Restaurant divisions using the variable costing approach. It was disappointing to note that many candidates –
- failed to show detailed workings of their calculations; and
- made careless mistakes because they failed to read the information provided in the question.
Part (e)
This part required candidates to calculate the return on total asset ratio for each operating division. Most candidates performed adequately, but many failed to allocate the cost of the land to the divisions.

Part (f)
This section required candidates to identify and discuss the arguments for and against the allocation of head office costs to each of the divisions. Many candidates did not seem to understand what was required and discussed irrelevant issues such absorption, variable and ABC costing.
Paper 2 consisted of three questions, and dealt with the following aspects:

**Question 1**
This question was solely a financial accounting question counting 60 marks in total. The question dealt with pro-forma journal entries in respect of two different subsidiaries of a parent company. The pro-forma journal entries addressed the accounting for a sale-and-leaseback transaction and the accounting for a loss of control.

Part (a) of the question counted 38 marks while part (b) counted 20 marks.

**Question 2**
This was a 40-mark question consisting of 30 marks for tax and 10 marks financial accounting. The question consisted of five parts:

*Part (a)*: In this section candidates were required to calculate a company’s and an individual’s taxable income as well as CGT.

*Part (b)*: Here candidates were required to deal with IFRS 5 and the applicable accounting journal entries.

*Part (c)*: In this section candidates were required to apply the definition of a dividend.

*Part (d)*: Candidates were required to calculate the CGT consequences of a share buyback transaction.

*Part (e)*: Candidates were required to deal with capital distributions received before 1 December 2007.

**Question 3**
The question was a 100-mark integrated question which examined aspects of integration from the financial accounting and management accounting core disciplines.

**Part A**
Part A of the integrated question consisted of 40 marks which covered valuations, cost of capital, capital budgeting and capital structure.

**Part B**
Part B of the integrated question consisted of 60 marks of financial accounting, which dealt with the following issues:

- The identification and discussion of a **contingent liability** in respect of recognition at the acquisition date of a business combination effected through the direct acquisition of assets and liabilities as a business.
- The identification and discussion of a **provision for environmental rehabilitation** in respect of recognition at the acquisition date of a business combination effected through the direct acquisition of assets and liabilities as a business.
- The identification and discussion of a **compound financial instrument** in respect of recognition and measurement at the acquisition date of a business combination effected through the direct acquisition of assets and liabilities.
liabilities as a business.

- The journalisation of the **direct acquisition of assets and liabilities** constituting a business combination, incorporating interesting assets and liabilities introduced by the amended IFRS 3, *Business Combinations*, and fair valuation of assets and liabilities at the acquisition date in a business combination. Candidates also had to calculate and consider the deferred taxation consequences that could arise in a business combination at the acquisition date.

Presentation marks were available for all three questions. These marks were clearly and separately stated in the “required” sections of each question.
QUESTION 1

<table>
<thead>
<tr>
<th>Maximum mark</th>
<th>Average mark</th>
<th>Marks &gt; 50%</th>
<th>Marks &lt; 50%</th>
</tr>
</thead>
<tbody>
<tr>
<td>60</td>
<td>30.85</td>
<td>1 352 candidates</td>
<td>1 569 candidates</td>
</tr>
</tbody>
</table>

Level of difficulty

The question was moderately difficult. It was adequately integrated and set at an appropriate level of difficulty for Part I of the Qualifying Examination. University comments supported the assessment of this question as an appropriate level for the examination with adequate topic coverage.

Main subjects / topics examined in the question

This question dealt solely with financial accounting aspects, counting 60 marks in total. The question required pro-forma journal entries in respect of two different subsidiaries of a parent company. The pro-forma journal entries addressed the accounting for a sale-and-leaseback and the accounting for a loss of control.

Part (a) of the question counted 38 marks while part (b) counted 20 marks. The remaining 2 marks were allocated to layout, cross referencing and journal narrations.

General comments

In general the answers given by the majority of candidates were fairly disappointing. The Qualifying Examination Part I is known to test knowledge and principles by way of pro-forma journal entries, and the importance of pro-forma journal entries is also stressed in the list of examinable accounting pronouncements that is issued by SAICA. In addition, many candidates appear to have a lack of understanding of certain principles of business combinations and consolidations, especially the more complex ones. Furthermore, a general lack of proper examination technique was also apparent (refer to more specific comments below).

Areas the candidates handled well

- Answers were generally fairly neat and well organised.
- The majority of candidates at least considered the tax implications of transactions where necessary.
- Based on supporting calculations given by candidates, it was also clear that they generally knew how to account for a sale-and-leaseback transaction in the separate accounting records of the two companies involved (although the formulation of pro-forma journal entries based on this appeared to be a problem – again refer to the comments that follow).

Areas the candidates handled poorly

A few areas relating to general exam technique are highlighted, which may be of use to future candidates in their examinations:

- Candidates did not specify the type of account affected in their pro-forma journal entries. This is a problem for line items such as non-controlling interest. For example, candidates often debited non-controlling interest and credited non-controlling interest, but did not specify that the debit goes to profit or loss and the credit goes to the statement of financial position.
These are two separate accounts and details must be specified. Markers were cautious in awarding marks where they were not able to clearly determine to which account the candidate was referring. A similar issue was encountered in respect of deferred tax.

- Although answers were generally set out in a fairly organised manner, candidates must ensure their calculations are cross referenced to their answers – many candidates failed to do so in this question.

**Specific comments on sections of the question**

**Part (a)**

In this section, candidates were required to provide pro-forma journal entries in respect of the first subsidiary (Protea).

Candidates amongst others had to account for a fair value adjustment on land at the acquisition date of this subsidiary. The scenario was further complicated by an inter-company sale-and-leaseback transaction that was classified as an operating lease. The property that was subject to the operating lease also had to be reclassified from investment properties to property, plant and equipment, because of owner occupation at group level. Candidates also had to deal with the tax consequences (especially CGT) relating to this subsidiary in pro-forma journal entries.

This section was generally answered better than part (b), but the following problematic areas were identified:

- A number of candidates referred to “consideration” in their pro-forma journal entries instead of “investment in subsidiary”. The correct account name was “investment account”.
- The vast majority of candidates credited a bargain purchase gain in respect of the first subsidiary instead of retained earnings. The controlling interest was acquired before the beginning of the current year, therefore the credit needed to go to retained earnings.
- Quite a number of candidates neglected to reclassify investment properties to property, plant and equipment in respect of the land that was subject to the inter-company operating lease.
- Many candidates were unable to integrate principles in respect of a sale-and-leaseback transaction with principles in respect of the elimination of unrealised profits arising from an inter-company sales transaction. Even though the majority of candidates calculated the unrealised profit and were able to split this between the recognised and deferred portions, many did not manage to formulate a proper pro-forma journal entry to eliminate these profits.
- It was also evident that some candidates got bogged down in the sale-and-leaseback calculations and journal entries and so ran out of time. They therefore failed to score the easier marks available for the elimination of the inter-company dividend and the attribution of current and prior year profits to the non-controlling interest.
- Only a small portion of candidates identified that the portion of the profit on the sale-and-leaseback transaction that was higher than the market value had no tax consequences due to the principles of connected persons contained in the Income Tax Act (i.e. only R2 million of the unrealised profit had tax consequences). This indicates that candidates still struggle to integrate issues relating to different subject areas.
- A large number of candidates did not adjust the since acquisition reserves and profits with other pro-forma journal entries (specifically in respect of the inter-company sale-and-leaseback transaction) before calculating the non-controlling interest on these reserves and profits.
Part (b)
In this section, candidates were required to provide pro-forma journal entries in respect of the second subsidiary (Bafana).

In respect of this subsidiary a change in ownership occurred which led to the subsidiary becoming an associate during the most recent reporting period. The scenario was complicated by the necessity to re-measure the remaining investment in the associate to its new fair value, as well as the reclassification of fair value gains on available-for-sale assets of the subsidiary from other comprehensive income to profit or loss upon the loss of control of the subsidiary. Candidates were not required to consider tax implications in respect of the second subsidiary.

This section was answered fairly poorly in comparison to part (a). The following problem areas were identified:

- Candidates over-ran on the time they spent on part (a) – most likely due to the sale-and-leaseback transaction.
- Two alternatives could have been followed to answer this part of the question. In the first alternative, the investee is treated as an associate and consolidated as such. In the second alternative, a chronological approach is followed in terms of which the investee is first consolidated as a subsidiary up to the date of change in ownership, and then it is “deconsolidated”, after which it is treated as an associate for the remainder of the year. Many candidates started with one alternative and then switched over to the other alternative. This clearly indicates a lack of understanding of key principles.
- Many candidates neglected to value the remaining investment in the associate at fair value and many candidates neglected to perform the reclassification adjustment on the available-for-sale financial assets of the subsidiary turned associate.
- Many candidates used inappropriate account descriptions in respect of certain amounts, e.g. “share of profit of associate” where they should have debited “dividends received” and “mark-to-market reserve” where they should have debited “share of other comprehensive income of associate”.


QUESTION 2

<table>
<thead>
<tr>
<th>Maximum mark</th>
<th>Average mark</th>
<th>Marks &gt; 50%</th>
<th>Marks &lt; 50%</th>
</tr>
</thead>
<tbody>
<tr>
<td>40</td>
<td>17.78</td>
<td>1,079 candidates</td>
<td>1,842 candidates</td>
</tr>
</tbody>
</table>

Level of difficulty

The question was rather difficult but was set at an appropriate level for Part 1 of the Qualifying Examination. The question was adequately integrated between topics as well as other subjects. A good balance was maintained between calculation and discussion sections.

Main subjects / topics examined in the question

The question consisted of five parts:

**Part (a)**
Candidates were required to calculate a company’s and an individual’s taxable income as well as calculate CGT. The maximum number of marks allocated to this part was 13 marks.

**Part (b)**
In this section candidates were required to deal with IFRS 5 and the applicable accounting journal entries. The maximum number of marks allocated to this section was 10 marks.

**Part (c)**
In this section candidates were required to apply the definition of a dividend. The maximum number of marks allocated to this section was 5 marks.

**Part (d)**
Candidates were required to calculate the CGT consequences of a share buyback transaction. The maximum number of marks allocated to this part was 5 marks.

**Part (e)**
In this section candidates were required to deal with capital distributions received before 1 October 2007. The maximum number of marks allocated to this section was 4 marks.

Three marks were allocated for presentation, which includes the narrations of the journal entries, language and layout.

General comments

This question was regarded as difficult because of the topic and type of combination. Overall, candidates struggled with this question and most candidates did not complete it, probably as a result of poor time management. In general the candidates missed the easy marks as a result of poor exam technique. Candidates did not read the question properly and did not answer what was required of them.
Areas the candidates handled well

In general parts (a) and (d) were answered fairly well and the answers were provided in a logical format.

Areas the candidates handled poorly

Part (a)(i)
- It would seem that candidates did not understand the question and many provided a descriptive answer and left out most if not all the calculations and tax implications.
- The recoupment of the motor vehicle and the CGT implications for Holdco were in general well answered.
- Candidates did not show base cost – allowances = R1 300 000 – R1 300 000 = 0.

Part (a)(ii)
- Most candidates did not recognise that the capital distribution of R1 million received was a part disposal for CGT purposes.
- Many candidates only picked up on the dividend implications or CGT or vice versa and not both.
- Most candidates did not apply the individual’s tax tables to correctly calculate the tax liability.

Part (b)
- Candidates showed poor accounting technique in the preparation of journal entries (i.e. no dates, narrations and at times confused debits and credits).
- In many instances NO narrations were provided.
- Candidates used abbreviations, such as R15 000’ instead of R15 000 000. This really complicated the marking process.
- Candidates made the error of not reading the question and did journals for only 1 motor vehicle instead of 10 motor vehicles.

Part (c)
- Candidates did not apply the dividend definition.
- There was a correct section selection, but poor application, with the result that many candidates drew the wrong conclusion.
- Most candidates applied the exclusion in paragraph (g) incorrectly as they did not recognise that the cost of the share had not been reduced in terms of GAAP.
- Candidates used the application of paragraph (c) instead of paragraph (cB).
- Many candidates discussed the tax implications for Subco and Holdco, which wasted a lot of time since the tax implications for Subco were not required.
- Candidates did not differentiate between the two dividends.

Part (d)
- Most candidates used the valuation date value as base cost rather than the base cost as calculated in part A.
- Some candidates did not take the 1 October date into account.
- Many candidates used 1% instead of 10%.
- Very few realised that 10% of R500 000 = R50 000, should be added to proceeds.
- Very few candidates deducted the base cost as calculated in part A.
Part (e)

- Most candidates did not complete this section, possibly as a result of poor time management.
- Most candidates did not answer this part correctly. Candidates in general did not know paragraph 76A of the eighth Schedule and did not apply it correctly, if at all.
- Most candidates mentioned that there was a CGT implication but did not give details of why and when the CGT must be accounted for.
QUESTION 3 PART A

<table>
<thead>
<tr>
<th>Maximum mark</th>
<th>Average mark</th>
<th>Marks &gt; 50%</th>
<th>Marks &lt; 50%</th>
</tr>
</thead>
<tbody>
<tr>
<td>40</td>
<td>19.15</td>
<td>1 388 candidates</td>
<td>1 533 candidates</td>
</tr>
</tbody>
</table>

Level of difficulty

The question was integrated with financial accounting, which was set at an appropriate level of difficulty for Part I of the Qualifying Examination.

Main subjects / topics examined in the question

The question integrated the following capital budgeting and cost of capital concepts:
- Valuations
- Cost of capital
- Capital budgeting
- Capital structure.

General comments

The format of the question, which required commentary on the inclusions rather than preparing a cash flow forecast, was in general not handled well. This shows that candidates have an understanding of the mechanics of capital budgeting, rather than a full grasp of the concepts.

Presentation in general was below that expected in a professional examination.

Areas the candidates handled well

Calculations to determine which financing was the most cost effective in part (c)(i) was handled well.

Areas the candidates handled poorly

- Presentation in general was poor, both with regard to commentary and calculations. Candidates did not structure their solutions in a coherent manner that showed a logical thought path.
- Linking of theory points to the scenario was poorly performed.
- Discussion of the question in the context of the current economic climate was poorly handled.

Specific comments on sections of the question

Part (a)
- Several candidates experienced difficulty in answering the question as the format was different from the de facto standard, indicating a limited grasp of the concepts, or alternatively, their predisposition to follow existing programming.
- In this question, candidates had to identify errors and omissions from a supplied cash flow forecast. Here they failed to realise amongst others that a terminal value was applicable to this case, instead of a continuing value (the usual situation), as the entity had a limited lifespan. Moreover, candidates often contradicted themselves with comments such as, “interest on the loan is erroneously included in the projections and should be removed”, but
then later indicating “loan payments are to be deducted”.

- Some candidates also erroneously approached the management accounting paper with a financial accounting bias. As a result numerous candidates identified errors and omissions by comparing the supplied cash flow forecasts to financial accounting principles. Even though there is some overlap between fair value accounting and cash flow forecasts, these candidates did not directly address what was required and their bias led to them receiving fewer marks. This was perhaps due to the integration of the question with the financial accounting question.

- Phrasing of the discussions was also problematic. As an example, it was sometimes difficult to ascertain whether there was a 1 million outflow or 800 000 outflow left in terms of opportunity cost.

- Presentation in this section was generally poor.

**Part (b)**

- Presentation was below par for this part, with candidates not clearly formulating the relevant advantages and disadvantages, relative to the usage of the entity’s own cash.

- Candidates failed to rigorously address all relevant factors and neglected to incorporate the obvious link between cash and the current liquidity crisis.

**Part (c)(i)**

- This part of the question required candidates to calculate and determine the most cost-effective financing instrument. Most candidates achieved more than 50% for this part, but a surprising number of candidates failed to apply discounting or to incorporate the time value of money in their decisions.

- The candidates who did incorporate these concepts often failed to compare like with like in reaching a conclusion (e.g. an IRR was compared to an effective cost, or a NPV discounted at 7,92% was compared to a NPV discounted at 23%).

- Presentation was also below par with many candidates failing to clearly indicate if a calculation represented a present value, or a present cost.

- Directions of the cash flows (it being inflows or outflows) were not clearly indicated in many cases.

- Many candidates put through interest cash flows annually although the question stated that the payment would be made at the end of the loan term, but in part (ii) they then seemed to realise that there was a bullet payment. Candidates also seemed to have forgotten about the STC during the calculation and then remembered it in part (ii) – this suggests poor planning of questions.

**Part (c)(ii)**

- This part of the required was poorly answered. Candidates failed to comprehensively discuss the other factors to be considered in deciding which instrument to use.

- Discussions commonly merely stated the obvious without incorporating the specifics of each instrument.
QUESTION 3 PART B

<table>
<thead>
<tr>
<th>Maximum mark</th>
<th>Average mark</th>
<th>Marks &gt; 50%</th>
<th>Marks &lt; 50%</th>
</tr>
</thead>
<tbody>
<tr>
<td>60</td>
<td>27.70</td>
<td>240 candidates</td>
<td>2 681 candidates</td>
</tr>
</tbody>
</table>

Level of difficulty

The question was of a good standard as can be expected for Part 1 of the Qualifying Examination. The question was adequately integrated between financial accounting and management accounting topics and also incorporated knowledge relating to (deferred) taxation. The question was quite difficult and required candidates to have a good knowledge of and a solid foundation regarding the basic principles underlying the topics. Topics examined were relevant and of importance both in practice and in the academic syllabus. The difficulty of the question was elevated by the integration of two subjects, namely financial accounting and management accounting. All universities commented that the difficulty level of the question was appropriate for the examination.

Main subjects / topics examined in the question

This question was integrated between financial accounting and management accounting, counting 100 marks in total.

The financial accounting section (60 marks) of the question dealt with the following issues:

- The identification and discussion of a contingent liability in respect of recognition at the acquisition date of a business combination effected through the direct acquisition of assets and liabilities as a business.
- The identification and discussion of a provision for environmental rehabilitation in respect of recognition at the acquisition date of a business combination effected through the direct acquisition of assets and liabilities as a business.
- The identification and discussion of a compound financial instrument in respect of recognition and measurement at the acquisition date of a business combination effected through the direct acquisition of assets and liabilities as a business.
- The journalisation of the direct acquisition of assets and liabilities constituting a business combination, incorporating interesting assets and liabilities introduced by the amended IFRS 3, *Business Combinations*, and fair valuation of assets and liabilities at the acquisition date in a business combination. Last, candidates had to calculate and consider the deferred taxation consequences that could arise at the acquisition date in a business combination.

General comments

The question was interesting and dealt with issues that are commonly encountered in practice. There is still concern about some candidates’ general exam technique when completing an integrated question, especially when combining different subjects as in this question. The question tested the candidates’ abilities to integrate their knowledge across topics and subjects and to plan their answers within the time allocated to each section.
Areas the candidates handled well

Part (e) of the question, relating to the journalisation of the assets and liabilities directly acquired in the business combination at the acquisition date, was generally well answered by candidates and they appeared to have a good general knowledge of the topics/issues examined.

Areas the candidates handled poorly

The following areas relating to this question should be highlighted, as it may be of use to future candidates for examination purposes:

- Poor exam technique was shown in parts (d)(i) to (d)(iii) relating to the discussion (theory) part (part (f)) of the question. It should be noted that the onus is on the candidate, and not on the marker, to provide legible, logical and well-presented answers in a professional exam.
- There appears to have been an absence of knowledge of even the basic application of the principles relating to contingent liabilities, provisions and financial instruments. Answers were especially poor on financial instruments (compound financial instruments). This is due to the fact that candidates appear to fall short in their ability to structure their arguments properly, make use of relevant and convincing theory from the financial accounting standards and to apply the theory and principles to the scenarios given to them. There was no healthy balance between the listing of theory and the application of the theory.
- There seems to be a general lack of knowledge regarding the application of the principles of deferred tax. Candidates who actually tried to calculate the deferred tax balance applied incorrect tax rates and incorrect tax bases and calculations were just generally poor. Many candidates also did not remember (or identify) that the initial recognition exemption from deferred tax (as identified in IAS 12, Income Taxes), does not apply to a business combination and candidates equated the tax base of assets and liabilities to the carrying amounts at acquisition date, which is clearly incorrect in terms of IAS 12.
- Time management still seems to be a problem for many candidates. This could have been partly due to the fact that the question was the last in Paper 2 (i.e. day two) when candidates were tired and under pressure. However, this does not detract from the importance of proper time management.
- Certain candidates had a major problem in providing legible answers. Their handwriting is very difficult to read and this, together with a poor layout, made their answers very difficult to mark. This is a problem that candidates should address to the best of their abilities.
- It was a concern that some candidates had not attempted some of the sections at all. This would have been partly due to the integration of the topic with management accounting and the related understanding of the approach to follow once the management accounting information had been sifted through.

Specific comments on sections of the question

Part (d)(i)

In this section, candidates were required to discuss the recognition of a contingent liability relating to a court case at the acquisition date in a business combination. The discussion was complicated by the fact that candidates had to identify that there was a “deemed” present obligation, i.e. a present obligation that is “more likely than not” (probable), in the scenario.

Nine 9 marks could be earned in this section, limited to the required 5 marks. Candidates failed to address the core issues relating to the fact that contingent liabilities eligible for recognition in a business combination at the acquisition date would have to be present obligations of the entity, where the contingency related to the measurement or probability of the obligation.
Part (d)(ii)
In this section candidates were required to discuss the recognition of a provision relating to environmental rehabilitation at the acquisition date in a business combination. What made the question interesting is that the present obligation in respect of the provision does not arise all at once, but over time, i.e. the present obligation is incurred as the past obligating event (the damage done to the environment by the entity, which happens over time) takes place.

Eight marks could be earned in this section, limited to the required 7 marks. Marks were appropriately awarded to the relevant supporting theory from the financial accounting standards, application of the theory and the conclusion that the entity was not handling the provision correctly by ignoring it.

Candidates probably fared the best in this section of the question, as the basic principles relating to the recognition of a provision (even in a business combination) are not that complicated and were not encumbered by further challenges created by the information of the question.

Part (d)(iii)
Candidates were required to discuss the recognition and measurement of a financial instrument relating to compound financial instruments. The instrument was a compulsory convertible preference share, where the preference dividends were settled in cash and the capital of the preference shares would be redeemed by conversion of the instrument to equity (ordinary shares of the issuer of the preference shares). This was not a difficult issue.

The question examined candidates’ ability to discuss both recognition and measurement, for a total of 8 marks. This meant that candidates were not required to discuss either aspect in exceptional detail. There were 12 marks available.

Candidates were accommodated by marking the measurement part of this question in part (e), should they have calculated the split between debt and equity in part (e) instead. The candidates who discussed how the debt/equity split had to be calculated were also awarded marks, as this question required a discussion.

Part (e)
Candidates were required to journalise the direct acquisition of assets and liabilities in a transaction that was said to be a business combination in terms of IFRS 3, Business Combinations.

The following issues (difficulties) arose for candidates in this part of the question:
- General uncertainty about the discount rates that should be used to calculate the fair values of assets and liabilities at the acquisition date – this was addressed in the mark plan by awarding marks for various acceptable discount rates, unless the particular discount rate was clearly incorrect in principle.
- Identification of new (unfamiliar) issues in terms of the amended IFRS 3. These related to off-market components existing in operating leases and re-acquired rights. It appears that candidates had not carefully thought through these issues.
- Many candidates did not even identify the settlement gain or loss that occurred in respect of the settlement of a pre-existing relationship (the re-acquired right).
- Candidates struggled with the calculation of the deferred tax consequences of the direct acquisition of assets and liabilities at the acquisition date, taking cognisance of the fact that the initial recognition exemption of IAS 12, Income Taxes, did not apply to temporary differences arising at the acquisition date in a business combination.
- The mere fact that assets and liabilities were acquired directly in the business combination,
instead of the acquisition of a controlling interest in a subsidiary, created problems for many candidates. It was surprising (and disappointing) that many candidates performed pro-forma journal entries at the acquisition date, adjusting the carrying amounts of assets and liabilities per the financial statements of the acquiree to fair value as at the acquisition date, as if a consolidation were being done!

Presentation

Presentation marks were awarded if candidates indicated (financial position) or (profit or loss) in the journal entry for vital principle issues (1), if journal narrations were given (1), for calculations which were cross referenced to the journal entry (1) and if the report format was used in the theory section as required by the question (1).

#311837