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 2011. 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 2011
- Background information on the setting, marking and adjudication of SAICA examinations
- General comments on Part I of the Qualifying Examination 2011
- Professional paper 1 – detailed comments by question
- Professional paper 2 – detailed comments by question
- Professional paper 3 – detailed comments by question
- Professional paper 4 – detailed comments by question
### Statistics for Part I of the Qualifying Examination 2011

<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>80%</td>
<td>1 584</td>
<td>397</td>
<td>1 981</td>
</tr>
<tr>
<td>Repeat candidates</td>
<td>35%</td>
<td>394</td>
<td>735</td>
<td>1 129</td>
</tr>
<tr>
<td>All candidates</td>
<td>64%</td>
<td>1 978</td>
<td>1 132</td>
<td>3 110</td>
</tr>
</tbody>
</table>

Average marks per question

<table>
<thead>
<tr>
<th></th>
<th>Question 1</th>
<th>Question 2</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Paper 1</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total marks</td>
<td>60</td>
<td>40</td>
<td>100</td>
</tr>
<tr>
<td>Average marks</td>
<td>35.79</td>
<td>13.44</td>
<td>49.23</td>
</tr>
<tr>
<td><strong>Paper 2</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total marks</td>
<td>60</td>
<td>40</td>
<td>100</td>
</tr>
<tr>
<td>Average marks</td>
<td>27.33</td>
<td>20.17</td>
<td>47.50</td>
</tr>
<tr>
<td><strong>Paper 3</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total marks</td>
<td>38</td>
<td>62</td>
<td>100</td>
</tr>
<tr>
<td>Average marks</td>
<td>18.52</td>
<td>30.25</td>
<td>48.77</td>
</tr>
<tr>
<td><strong>Paper 4</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total marks</td>
<td>68</td>
<td>32</td>
<td>100</td>
</tr>
<tr>
<td>Average marks</td>
<td>39.60</td>
<td>13.71</td>
<td>53.31</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 (IPD Committee), takes overall responsibility for the setting of the examination paper. Examination questions can 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
- Alex Bretteny
- Kim Bromfield
- Helouise Burger
- Stefani Coetzee
- Muneer Hassan
- Dewald Joubert
- Jana Lamprecht
- Rowan Lang
- Francois Liebenberg
- Ben Marx
- Goolam Modack
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 (IPD 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 (IPD 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 (IPD 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 (IPD 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 (IPD 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 auditing. 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. The questions tested the candidates’ abilities to intra-integrate their knowledge across topics and to plan their answers within the time allocated to each section of the question.

- The **tax questions** were of an appropriate to high standard with most of the candidates passing Paper 1 Question 1. However, candidates did not perform as well as expected in Paper 4 Question 2 as a result of a lack of basic and current tax knowledge.

- The **management accounting and financial management questions** were adequately integrated with auditing topics. The standard of the questions was considered moderate to easy and appropriate for the questions in Paper 1 and 3. 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 questions** was relevant, topical and considered to be well set questions, with adequate topic coverage of the syllabus. The aspects examined were of importance and relevance, integrating the companies act, corporate governance and professional ethics which were supported by various SAICA accredited universities. 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. It is disappointing to see that some candidates did a memory dump of theory and refrained from applying these concepts to the information of the question.
3 Specific comments

From a review of candidates’ answers to the seventy examination questions for the January 2011 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. **Workings done in pencil will not be marked as outlined in exam rule 8.5 of the SAICA Examination Regulations.** 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 for which presentation marks are awarded.**

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

- Writing on flags – As per section 4.4 of the SAICA examination regulations: “Candidates will only be allowed to highlight, underline, sideline and flag in the permitted texts. Writing on flags is permitted for reference and cross-referencing purposes only, that is, writing may only refer to the name or number of the relevant discipline, standard, statement or section in the legislation”. Any contravention of regulation 4 will be considered to be misconduct.

- 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!!*
**PROFESSIONAL PAPER 1**

<table>
<thead>
<tr>
<th><strong>Paper 1</strong> consisted of two questions that dealt with the following aspects:</th>
</tr>
</thead>
</table>
| **Question 1**  
This question was solely a taxation question, counting 60 marks in total. The question required candidates to calculate the taxable payable by an individual which included Capital Gains Tax and VAT consequences. |
| **Question 2**  
This question was solely a Management Accounting and Finance question, counting 40 marks in total, dealing with revenue and profitability analysis. The question contained additional intra-integration which required candidates to identify the operating leverage issues of the company. |
| **Presentation marks were available for both 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>35.79</td>
<td>2570</td>
<td>542</td>
</tr>
</tbody>
</table>

**Level of difficulty of the question**
Easy to moderate. The question tested basic concept in an intra-grated manner, combining various concepts in Taxation from various topics.

**Topics examined**
This question was solely a Taxation question that dealt with the following topics:
- Calculation of tax payable by an individual taxpayer
- Capital Gains Tax consequences of disposals made by the taxpayer (including disposals of individual assets and a business as a whole)
- Value-Added Taxation consequences of the business run by the taxpayer (he is a sole proprietor)
- Lump sums received by the taxpayer and other retirement benefits

**General comments**
Candidates generally performed well in the question. The markers were, however, still disappointed at the mistakes candidates made which resulted in easy marks being lost.

**Areas the candidates handled well**
Candidates generally performed well in the question. Candidates handled the calculation of taxable income well and also seem to understand the link between the taxable income calculation (part (a)) and the Value-Added Taxation consequences (part (d)) of transactions.

**Areas the candidates handled poorly**
Candidates struggled with the following:
- The tax consequences related to retirement benefits (i.e. lump sums received from funds), specifically calculating the cumulative lump sum received and knowing which lump sum tax table to use to calculate the tax on the lump sum received. There were many principle marks allocated to these calculation and if candidates did not follow the correct approach and thought process, these easy marks were be lost.
- The required specifically stated the following: “Where you are of the opinion that an accrual or expense has no tax effect, provide brief reasons to support your answer.” However, many candidates missed out on easy marks by not properly motivating why a transaction does not have tax consequences. Proper exam technique is so crucial, it can make the difference between a pass and a fail!

**Specific comments on individual sections of the question**

**Part (a)**
In this section, candidates were required to calculate the normal tax liability of an individual taxpayer.
This section was generally well-answered.
Candidates specifically struggled with the following concepts:
- Many candidates did not realise that section 24I will not be applicable to the forex loss of R338. This indicates that candidates struggle to apply the scope of section 24I to a scenario.
Candidates struggled with the application of section 11(l) on the contributions to funds paid by employers on behalf of employees.

**Part (b)**
In this section, candidates were required to calculate the tax consequences arising from the individual taxpayer making withdrawals from retirement funds. This section was generally answered poorly. Many candidates tried to still apply the old legislation to the scenario due to a lack of knowledge of the amendments to the Second Schedule. Candidates also struggled to distinguish between withdrawal benefits and retirement benefits and the tax consequences related to each. This seems to be a topic that many candidates need to improve their knowledge on.

**Part (c)**
In this section, candidates were required to calculate the capital gains tax consequences arising from the sale of the taxpayer’s business, specifically related to goodwill and residential property. This section was generally well-answered. Some candidates do not understand how to value a pre-valuation date asset for CGT purposes. This is a basic principle that all candidates should be able to apply correctly.

**Part (d)**
In this section, candidates were required to calculate the Value-Added Taxation due to the South African Revenue Service. This section was generally well-answered. Candidates generally demonstrated a lack of proper exam technique in this part of the question. The required clearly stated that brief reasons should be provided for including or excluding numbers from the calculation. However, most candidates did not adhere to this instruction and therefore lost out on many easy marks for motivating why amounts should be included or deducted.
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>13.44</td>
<td>214</td>
<td>2898</td>
</tr>
</tbody>
</table>

Level of difficulty:
The question was set at an appropriate level of difficulty for Part I of the Qualifying Examination.

This question was not difficult, yet it appears that many candidates were unable to cope with the question.

Main subjects/topics examined in the question
This question was solely a Management Accounting and Finance question counting 40 marks in total.

Revenue and profitability analysis, specifically a detailed gross profit analysis. The question contained additional integration which required candidates to identify the operating leverage issues of the company, in the form of high levels of fixed costs when compared to variable costs.

Part (b) included strategic considerations on improving profitability and cash flow management for the company.

General comments:
Very few candidates were able to excel (and present themselves in a critical thinking approach) in the question. Generic, standardised approaches were applied by most candidates. There was an inherent lack of commanding the data at hand and providing concise, articulate and decisive interpretations.

In general candidates did not address all parts of the required in full, eg: “Identify and outline” required candidates to first identify the action required and outline how this will improve cash flow. In most cases candidates only mentioned the actions without outlining how will improve cash flow.

The question contained numerous available marks – far in excess of the maximum marks. On several of the marks the question also required interpretation by the marker. To address this “markers’ guidelines” were compiled for the first mark, and updated again for the second mark. The result was that the two independent marks were very close to each other and it further necessitated fewer reconciliations to be performed for the final mark.

Layout and presentation
In spite of the added reading time, candidates’ layout and presentation was very poor. It appears that 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. The quality of handwriting is also an ongoing problem. Poor spelling and use of unintelligible abbreviations remain problematic.

Irrelevancy
Candidates provided discussion which was not part of the required, this was particularly evident in part (a), where candidates prepared numerous ratios which were scoped out by the required. 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.
Basic numeracy skills
It was disappointing to note that many candidates did not display basic numeracy skills. This is elaborated on later.

Examination technique
Many candidates did not address what was required by the questions and, for example, provided analysis and interpretation of matters that were not required.

Application of knowledge
Candidates were unable to apply their knowledge to the scenarios described in the questions.

Areas the candidates handled well:
Part (b) of the question was handled relatively well by candidates.

Areas the candidates handled poorly:
Part (a) of the question. Candidates were required to analyse and comment on the revenue and gross profit performance. However most candidates spent time on computing as many ratios as possible. Most of these did not relate to revenue and gross profit and little commentary on the performance of revenue and gross profit was made.

Overall the candidates struggled with the question. Most were however able to do the basic revenue change and gross profit calculations.

Specific comments on sections of the question (where questions are subdivided into different parts):

Part (a)
For an analysis and interpretation question, proper planning of the exact ratios and figures to calculate is essential. Based on solutions offered, candidates either failed to plan, or planned ineffectively. Furthermore, a significant number of candidates misinterpreted the clear instructions contained in the question and offered solutions addressing aspects other than the required. This is definitely not as a result of ambiguity in the question; instead these candidates did not heed the numerous warnings offered by most universities and SAICA, in this regard. This wasted valuable time and resulted in lower marks.

Candidates often failed to display basic numeracy skills, specifically for this part of the question. Here it was concerning that many candidates could not accurately calculate, for example, the percentage movement from one year to the next.

Candidates normally struggle to take matters into account that are not immediately obvious from the information presented. Again, very few candidates earned the 2 marks allocated to the identification of additional information affording meaningful further analysis, for example.

Attempts by candidates did not address the question (analysis and comment) and were more focused on computing the ratios. Candidates struggled to analyse ratio’s calculated, and also did several time-wasting superfluous calculations.

The issues below are raised not to identify students that represented the exception to the norm, but rather to highlight the concerning volumes of students that were prone to make the errors listed below:
Examples include issues such as:

Example 1

Question states that volumes (in the brick industry) declined by 25% in 2009 and a further 5% in 2010.

Candidates would:

· conclude that volumes declined by 30% in 2 years!! They clearly show a lack of numeracy skills and interpretation thereof. Alternatively stated, if sales declined by 50% in 2009 and a further 60% in 2010, is the implication that there are no sales after 2 years? (i.e. a 110% decline?).

· In a similar vein, if the gross profit % margin in one year is 40% and 36% in the following year, the decline is 4%! (as opposed to 4% on 40% = 10%!)

Example 2

· once they correctly determined that Supremo’s sales volumes declined by 20% in 2010, they concluded that it was 15% worse than the brick industry average decline of 5%, ignoring that vastly different items, volumes etc (and changes therein) are at hand here and hence the subtraction of these percentages is totally meaningless!

Example 3

Candidates would conclude that gross profit % on sales amounted to 40.3% (2009) and 35.8% (2010), and then proceed with an attempt to interpret these percentages.

This would then be followed up by cost of sales % on sales of 59.7% (2009) and 64.2% (2010), to which the findings would be totally contrary to the findings for the gross profit% determined above. Candidates were oblivious of the fact that the same data is being analysed.

The question did not require many calculations, but the few that were required revealed a serious lack of numeracy and/or mathematical and/or technical skills.

Further to the lack of numeracy skills the students showed a lack of understanding as to what factors affect sales and gross profit, and provided pages of ratios (eg. interest cover, debtors days, net operating profit % or ROA) that do not affect these two sets of ratio data.

It seems as though many students did not read Part a) thoroughly, they did not analyse the Sales and GP, but instead went on to calculate profit and earnings ratios. This wasted time and did not earn the students any marks. Candidates displayed little understanding of how to interpret the calculated ratios in context of the case study.

Candidates also did not appear to know where to focus their time and energy for this question and lost a lot of marks because of this. Vital information from the case study was mostly not extracted and pulled back to the ratio analysis.

Part (b)
Candidates repeatedly displayed poor examination technique, by failing to clearly indicate whether their discussion related to actions to improve cash flow, or profitability.
Candidates often displayed illogical thought, for example, by first stating that the business should maximise free creditors finance, but then stating that the business should ensure that they obtain payment discounts from creditors, the latter implying early settlement. Moreover, these candidates also failed to indentify if and how the suggested action would benefit cash flow or profitability.

Candidates made impractical recommendations, for example, “the company should also transport sand or building rubble”, failing to take into account that the company owns flat-bed trailers, and making no mention of cost-effective modifications, etc.

Furthermore, candidates failed to incorporate matters that should be common knowledge at this level, for example, recommending the issue of shares to the public, in spite of the limitations placed on a private company in this regard.

Lastly, candidates often recommended actions that seem to be based more on popular ‘buzz words’ rather than any real thought of its relevance in this scenario. For example, “the company should list shares” or “merge with another company to obtain synergy”.

Their inability to distinguish between profit and cash-flow effects is concerning and candidates would use these terms interchangeably as if they ultimately represent the same set of information.

Regrettably the question did not limit the candidates to just two suggestions to improve profitability and just two suggestions to improve cash-flows, and consequently they simply dumped a list of numerous factors that would affect profitability and cash-flows and earned marks in many instances for listing very generic factors.

**Part (c)**
Candidates often displayed a distrusting attitude towards the information provided in the question, for example, “is the price fair?”, even though it is clearly stated in the question that the selling price represents the “fair market value” and that the rental is “market-related”.

Furthermore, many candidates offered an extensive discussion of only the financial accounting matters (earning a maximum of 1 mark), instead of providing a comprehensive discussion of all matters to be considered in this case.

Most of the candidates did struggle with the calculation of CGT, which required exclusion of recoupment from the proceeds and base cost.

From a numeracy perspective, it was concerning that many candidates used 12 monthly instalments \((12 \times R200\,000)\times 5\text{ years} = R12\text{ million}\). Time value of money principles were simply non-existent.

Students often assumed this to be an accounting question only and thus discussed leases in detail without delving into other pertinent issues.
**PROFESSIONAL PAPER 2**

<table>
<thead>
<tr>
<th>Paper 2 consisted of two questions that dealt with the following aspects:</th>
</tr>
</thead>
</table>
| **Question 1**  
This question was of an integrative nature testing both financial accounting and auditing, counting 60 marks in total. The question tested the candidates’ understanding of accounting for various investments and the auditing of these investments. |
| **Question 2**  
This question was intra-integrated within financial accounting, counting 40 marks in total. Topics examined within this question were relevant due to the global nature of the financial accounting and trading of companies which are of importance both in practice as well as in the academic syllabus. |
| Presentation marks were available for both 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>27.33</td>
<td>1192</td>
<td>1920</td>
</tr>
</tbody>
</table>

**Level of difficulty:**

This was a 60 mark question. The level of difficulty of the question has been assessed as fair level of difficulty for the Part 1 of the Qualifying Examination. The level of integration and coverage of topics between auditing and financial accounting has been assessed as very good. The sections have been assessed individually as follows:

*Part (a) – 6 marks:* This question is fair, but candidates performed worse than expected. The question required candidates to identify risks of material misstatement.

*Part (b) – 20 marks:* The question is fair and set at the appropriate level of difficulty. The majority of the marks could be obtained through calculating the effective interest rate and present values as well as noting relevant disclosure requirements.

*Part (c) – 15 marks:* This question was fair and had 31 available marks. The question required candidates to describe audit procedures to audit the valuation assertion of various investments.

*Part (d) – 8 marks:* This question was easy since candidates had to quote relevant sections from the auditing standards relating to communication to those charged with governance.

*Part (e) – 7 marks:* This question was fair and required candidates to draft a schedule of audit differences.

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

The question integrates financial accounting and auditing, testing the candidates’ understanding of accounting for various investments and auditing these investments. The financial accounting principles in IAS 39 and IFRS 7 were tested with the candidate being required to discuss the application thereof. Assessment of material misstatements in the financial statements, calculation of effective interest rate, present values and impairment losses relating to held to maturity bonds, the design of detailed substantive procedures, preparation of a schedule of audit differences and communication to those charged with governance.

The question is straight forward, well structured with no identified ambiguities and considered fair in terms of level of difficulty.

**General comments:**

The question was well balanced with appropriate levels of calculation and application. This question was also a good integrated question which contained a couple of key concepts.

The exam requirements were appropriate and unambiguous; with the final average mark aligned to the test pack average. Although significantly more marks were available in both parts (a), (b), (c) and (d) than the maximum per section, there was very little evidence of candidates running into the maximum number of marks.

There was no evidence of time constraints as this was the first question in the paper.

**Areas the candidates handled well:**

Part (b) was handled well by candidates. Effective interest rate and present value calculation s were performed well and candidates seemed to answer methodical questions better.
Areas the candidates handled poorly:
Part (a), (c) and (d) were handled poorly with (c) and (d) being worse than (a). While the questions were on different topics, answers generally lacked an appropriate level of depth and only covered one or two concepts. It was felt that candidates did not apply themselves to all aspects of the question. More details are provided below.

Specific comments on sections of the question (where questions are subdivided into different parts):

Part (a):
In this section, the candidates were required to identify risks of material misstatement relating to the audit of investments. The quality of the answers was poor to average. Candidates generally provided the obvious risks of misstatement, but did not identify risks which require more application. Candidates would for example identify that the calculation to be performed by management was complex but would fail to comment on the individual variables within the calculation.

Some candidates also got lost in the detail, focusing too much on the assumptions and the factors impacting these instead of identifying the actual risks.

Candidates spent a lot of time on this part of the question considering the marks allocated.

Part (b):
In this section candidates were required to calculate the original effective interest rate of bonds held by the company, the present value of the bonds with new cash flows and future values and the impairment losses. Candidates also had to indicate disclosure requirements and requirements for accounting for held-to maturity investments. This all had to be communicated in a memorandum to the audit partner.

This question was answered well by the candidates and candidates scored the most marks in this section and seemed to be more confident answering this section of the question.

The answers were mostly set out in a logical manner and were fairly easy to mark. Easy marks were lost where candidates did not carry forward their calculated values to the disclosure sections.

Consequential marking was applied which resulted in additional marks for candidates.

Part (c):
Candidates had to detail audit procedures relating to the valuation assertion of various investments held.

This question was answered poorly by the candidates. The question required candidates to audit the valuation assertion of various investments.

Candidates generally failed to describe procedures using appropriate terminology such as “Inspect”. Marks were therefore awarded for the principle of the procedures articulated even if the appropriate terminology was not used.

Candidates did not provide procedures for all the investments in the question, but rather focused on one or two investments. This resulted in a lot of lost marks for basic procedures, impacting on the overall marks for this section.

Candidates did not apply themselves to the specific investments being audited and basic procedures were provided for the investments without application. Candidates would for example
describe using a valuator but would not comment on evaluating the independence of the valuator or reviewing the working papers prepared by the valuator.

Candidates also lacked structure in answering this question, possibly indicative of the lack of planning. Procedures were “added on” in an attempt to score marks and were not part of a planned structure.

Overall, the answers lacked an appropriate level of depth for a qualifying examination.

**Part (d):**
A lot of candidates failed to identify the relevant audit standard applicable. The question required the candidates to discuss the obligations of the auditor with regard to communicating the issues identified in the audit of investments. Their solution should also have included a description of the content of the communication and to whom it should be addressed to. The majority of the candidates discussed the communication relating to Reportable Irregularities and not communication to those charged with governance as required by ISA 260.

Where candidates did identify the appropriate auditing standard, the candidates did not apply themselves to the content of the communication and how that applied to the information in the question.

**Part (e):**
Candidates were required to draft a schedule of audit differences based on the information calculated in other sections of the question.

This question was also answered poorly by the candidates and the candidates lost easy marks by not commenting on the other investments were no misstatement occurred.

A lot of candidates also did not treat the section as a question on its own and failed to identify additional calculations required in this part of the question. The schedule of audit differences therefore became a summary of the differences identified in other sections of the questions. Candidates also failed to deduct the differences already adjusted by management from their calculations. Some candidates did not attempt the section at all as a lot of time was spent earlier on 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>40</td>
<td>20.17</td>
<td>1713</td>
<td>1399</td>
</tr>
</tbody>
</table>

**Level of difficulty:**
The question was on a good standard as can be expected for Part 1 of the Qualifying Examination. The question was adequately intragrated between topics within financial accounting and also incorporated knowledge relating to (deferred) taxation. The question was of medium difficulty and required candidates to have a good knowledge of and a solid foundation regarding the basic principles underlying the topics. Topics examined were relevant due to the global nature of financial accounting and trading of companies, and were also of importance both in practice as well as in the academic syllabus. The difficulty of the question was slightly elevated by the fact that this was a foreign subsidiary where a loss of control occurred (i.e. a significant event in terms of IAS 27), but candidates appeared to have handled the question very well anyway. All universities furthermore commented that the difficulty level of the question was appropriate for the examination.

**Main subjects/topics examined in the question**
This question was intragrated within financial accounting, counting 40 marks in total. The question dealt with the following issues:

- The identification and discussion of the **most appropriate fair value for inventory** in respect of recognition at the acquisition date of a business combination effected through the acquisition of a controlling interest in another foreign company **(7 marks)**;

- The calculation of the **consolidated gain or loss on disposal of the controlling interest** in a foreign operation in terms of the requirements of IAS 27.34. This also incorporated the realisation (and in certain instances the reclassification) of certain components of other comprehensive income (such as the foreign currency translation reserve) **(19 marks)**;

- The calculation of the **consolidated profit after tax** of the reporting entity, taking into account the disposal of the controlling interest in the preceding section, certain intragroup transactions, preference dividends having been classified in terms of IAS 32 *Financial Instruments: Presentation* **(12 marks)**;

- Presentation marks **(2 marks)**.

**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 intragrated question. The question tested the candidates’ abilities to intragrate their knowledge across topics and to plan their answers within the time allocated to each section of the question. The solution to the question was also of a consequential nature as each section of the question impacted another either directly or indirectly. The question was generally viewed as at the right level of difficulty by all accredited universities.

**Areas the candidates handled well**
Candidates did not appear to be struggling with the question and the general feeling among the mark team is that the candidates handled most sections in the question quite well. Candidates seemed to have a proper understanding of what was required in the major parts of the question and it was evident that there were numerous approaches, all of which had been accommodated on the final mark plan, to calculate the numbers required to solve the question.
Areas the candidates handled poorly
The following areas should however be highlighted, which may be of use to candidates for future examination purposes relating to this question:

- Poor exam technique existed in part (a) relating to the discussion (theory) part 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 the basic application of the principles relating to fair value of inventory at the acquisition date in a business combination transaction and that the fair value is to be calculated from the point of view of the acquirer. 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 in the scenarios given to them. There was no healthy balance between the listing of theory and the application of the theory.

- Time management still seems to be a problem for some candidates. This could have been partly due to the fact that the question was the last in Paper 2 when candidates were tired and under pressure. This however does not take away from the importance of proper time management.

- Certain candidates have a major problem in providing legible answers. Their handwriting is very difficult to read and this, together with a poor layout, makes their answers very hard to mark. This is a problem that candidates should address to the best of their abilities.

Specific comments on sections of the question (where questions are subdivided into different parts):

Part (a)
In this section, candidates were required to identify and discuss the most appropriate fair value of inventory at the acquisition date in a business combination. The discussion was complicated by the fact that the inventory had become obsolete one month after the acquisition date, and whether this obsolescence was the result of a decision that was taken as part of the business combination or not.

8 marks could have been earned in this section, limited to the required 7 marks. Candidates failed to address the core issues relating to the valuation of the inventory at the acquisition date in a business combination.

This section of the question was marked in principle. This means that the candidates’ arguments were investigated by the markers and marks were awarded to all candidates who provided logical and sound reasoning for the fair values they had deemed most appropriate at the acquisition date. Most candidates’ arguments were very generic and they repeated theory from IFRS 3 Business Combinations directly – this indicates the lack of ability to APPLY the principles from a particular financial accounting standard to the information given in the question.
Part (b)(i)
In this section, candidates were required to calculate the consolidated gain or loss on disposal of a controlling interest in a subsidiary. What made the question interesting is that the subsidiary was a foreign operation – i.e. the candidate did not only have to calculate the gain or loss on disposal from a group perspective, but also had to deal with accompanying issues such as realisation and reclassification of underlying components of other comprehensive income, as the loss of control is regarded to be a “significant event” in terms of IAS 27 Consolidated and Separate Financial Statements.

There were 19 marks that could be earned in this section, limited to the required 19 marks. Marks were appropriately awarded to the relevant supporting calculations, and this was not impacted at all by the approach followed by the candidate to calculate the required amounts. Three main approaches were identified in the solution:

- Calculation of consolidated gain or loss on disposal based on a gross approach (i.e. working at 100% and incorporating all the steps as mentioned in IAS 27.34);
- Calculation of consolidated gain or loss on disposal based on a net approach (i.e. working only with the ownership interest of the parent (i.e. 80%) and only realising the goodwill relating to the parent – this meant that NCI did not play a role to a large extent in this calculation, neither did the goodwill relating to the NCI); and
- Following a short approach of taking the gain or loss on disposal as calculated in the separate financial statements of the parent and adjusting the amount by the loss of equity that had attached to the equity interest disposed of, since the acquisition thereof – this method proved to be the smartest and would have taken the least time to calculate (i.e. highest return on time investment).

Candidates probably fared the best in this section of the question, as the basic principles relating to the calculation of the consolidated gain or loss on disposal of a controlling interest are quite a focus point for this topic and most candidates spend enough time during their academic studies to master the topic – i.e. within the topic, there were no unexpected glitches that candidates had to deal with and the calculation was relatively predictable and doable.

Part (b)(ii)
In this section, candidates were required to calculate the consolidated profit after taxation for the reporting entity (which is a group). This was not a difficult issue.

The question examined candidates’ ability to calculate a number and they were not required to present this information in the various sections of the statement of comprehensive income or the statement of changes in equity, which they normally find quite difficult. 14 marks were available to be earned, and these marks were limited to a maximum of 12.

The marking process was kept very fair by marking “across borders” in parts (b)(i) and (b)(ii) of the question. This means that, due to there being some uncertainty among academics and practitioners about whether the realisation of the underlying components of other comprehensive income should form part of the calculation of the consolidated gain or loss on disposal of a controlling interest (i.e. there is no clear guidance in IAS 21 or IAS 27), candidates were awarded marks for calculating these components of other comprehensive income that were realised by the disposal of the controlling interest, whether they were included in the actual gain or loss on disposal of the interest or in the calculation of the consolidated profit after tax of the reporting entity – this made the marking of this issue very fair.

Presentation
2 marks were awarded to presentation in this question, as follows:

- Handwriting, layout, neatness  1
- Cross-referencing of calculations into final answer  1
Paper 3 was a 100 mark integrated question which examined auditing and financial management in two separate parts. The Paper consisted of two parts that dealt with the following aspects:

Part A
Part A was the auditing section of the paper, counting 38 marks out of a total of 100 marks, dealing with ethics, corporate governance and Company Act Aspects. It also covered risk of material misstatement and auditing reporting considerations.

Part B
Part B was the management accounting section of the paper, counting 62 marks out of a total of 100 marks. This part of the question dealt with, amongst other topics, pricing strategies, calculation of breakeven revenue and operating leverage decision making and ethics.

Presentation marks were available for both Part A and Part B of the question. These marks were clearly and separately stated in the “required” sections of each part of the question.
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>38</td>
<td>18.52</td>
<td>1605</td>
<td>1507</td>
</tr>
</tbody>
</table>

**Level of difficulty**
The auditing was integrated in a 100 mark question with financial management comprising short term decision making.

The question was relevant, topical and considered to be a well set question, with adequate topic coverage of the syllabus. The aspects examined were also of importance and relevance, integrating companies act, corporate governance and professional ethics. This view is also supported by the various university comments.

**Main subjects /topics examined in the question**
The auditing section of the question consisted of 38 marks of auditing integrating ethics, corporate governance and Company Act aspects. It also covered risk of material misstatement and audit reporting considerations.

**General comments:**
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. It was however disappointing to see that, as in previous years some candidates neglected the auditing and did not put in an assertive effort in the answering thereof and accordingly recorded very low marks.

Examination technique was again, as in previous years a problem. Many candidates did not read and consider the information of the question carefully, as was evident in the fact that many candidates did not limit their answers to the specific requirements and transaction/actions of part b, c and d, and accordingly went on the discuss aspects not covered by the required. Candidates also often did a memory dump of theory and refrained from applying these concepts to the information of the question.

**Areas the candidates handled well:**
The section on ethics and corporate governance, as well as the Companies Act was well answered.

**Areas the candidates handled poorly:**
Candidates had difficulty with sections c) and d), especially the auditor’s response to non corporate governance compliance as well as discussing the fraud risk and the impact on the audit report.

**Specific comments on sections of the question (where questions are subdivided into different parts):**

*Part (a)*
Part (a) of the question counted 3 marks and dealt with the need for a statutory audit.

This section was reasonably well answered.
**Part (b)**
Part (b) of the question counted 19 marks and required a discussion of the ethical, corporate governance and **statutory issues arising from the EA SA new business venture**.

This section was reasonably well answered, although certain candidates did not read the required carefully and accordingly did *not limit their answers to the new business venture*, and accordingly dealt with aspects not covered under the required.

This again stresses the importance of sound examination technique applied by candidates.

**Part (c)**
Part (c) of the question counted 7 marks and required of candidates to discuss the boards compliance with King III regarding the issue of appointing the CEO as Executive Chair, as well as the auditors response in this regard.

Many candidates incorrectly dealt in detail with the composition of the board of directors, which was not what was asked. Candidates also had difficulty in identifying and explaining the auditor's response.

This again stresses the importance of sound examination technique applied by candidates.

**Part (d)**
Part (d) of the question counted 7 marks and required of the candidates to discuss the fraud risk factors *from the new business venture* and the impact on the audit report thereof.

This section was answered poorly. Relevant fraud risks were not always identified and candidates further failed to apply the impact of the risks logically to audit report.

**Presentation**
This counted 2 marks, being awarded for arrangement and layout (1) and handwriting and presentation (1).
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>55</td>
<td>30.25</td>
<td>1534 candidates</td>
<td>1578 candidates</td>
</tr>
</tbody>
</table>

**Level of difficulty**

Paper 3B was a moderate to easy Management Accounting question which had a good balance between calculations and discussion required.

**Main subjects examined in the question**

The question was a 62 mark question, including 3 presentation marks, which covered:

- Calculation of impact of entering into joint venture on operating profits (18 marks);
- Discussion regarding the key considerations for decision making purposes regarding the joint venture including an ethical issue (18 marks);
- Critique of the company’s pricing strategies (10 marks); and
- Calculation of breakeven revenue and operating leverage (13 marks)

**General comments**

Part (e) was challenging as it required candidates to distinguish between relevant and irrelevant information and select the most appropriate manner in which to analysis impact on profitability. Devoting too much time to this section could have prejudiced candidates’ performance in other sections.

**Areas the candidates handled well**

The majority of candidates scored well in part (h) – calculation of breakeven revenue.

**Areas the candidates handled poorly**

Parts (f) and (g) were generally not well attempted. Candidates continue to dump a 'laundry list' of information in the hope that some of this may be relevant to the question. Discursive answers have improved in recent years however, candidates are urged to focus on answering the question rather than to irritate markers with endless lists of relevant and irrelevant factors.

**Specific comments on sections of the question**

**Part (e)**

This calculation was challenging and required candidates to assimilate significant information and apply only relevant information for management decision making in calculations. Too many candidates confused themselves for example, by attempting to calculate the incremental impact on profits of the joint venture to then adopt another method halfway through answering the question. This made marking very difficult!

Candidates may be disappointed with their results in part (e) with hindsight. The candidates who scored well tended to follow a methodical and consistent approach and set out their workings clearly.

**Part (f)**

Part (f) required an identification of the key factors to be considered prior to decision making re the joint venture. Many candidates wasted invaluable time listing issues which were not important in the decision making process or in fact irrelevant. Candidates are urged to apply their minds to the scenario and avoid dumping a memorized list of potential factors for consideration.

**Part (g)**
This part was unusual in that it required candidates to critically assess the stated policy and strategies of pricing a six night game lodge experience. Candidates would be more comfortable discussing the costing aspects rather than determining an appropriate price point or range for a service offering. This was apparent by the number of candidates entering into a detailed analysis of particular costs which did not address the required.

Yet again, candidates are urged not to dump theoretical knowledge but rather to apply their minds to the specific scenario.

Part (h)
This section was generally well answered and candidates scored well. However, it was disappointing to note that many candidates were unable to distinguish between variable and fixed costs. Most candidates did not know how to calculate the operating leverage ratios which may indicate that this is not covered at undergraduate level.
PROFESSIONAL PAPER 4

Paper 4 consisted of two questions that dealt with the following aspects:

Question 1
This question was solely a financial accounting question, counting 68 marks in total. The question dealt with reportable operating segments, calculating the effects on the statement of comprehensive income of various transactions and the presentation of an extract of the statement of financial position dealing with a sale-and-leaseback which included the corresponding deferred tax implications.

Question 2
The question was solely a tax question, counting 32 marks in total, dealing with aspects of normal income tax. Candidates were required to discuss, with reference to case law, the tax consequences of a claim for damages received by the taxpayer to cover a loss of normal income, repairs to be effected and a loss of goodwill.

Presentation marks were available for both 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>68</td>
<td>39.60</td>
<td>2507 candidates</td>
<td>605 candidates</td>
</tr>
</tbody>
</table>

**Level of difficulty:** The question was of a moderate difficulty. It was adequately intra-integrated and in the context of the financial accounting questions, it was 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 question for the examination with adequate topic coverage.

**Main subjects/topics examined in the question**
This question was solely a financial accounting question counting 68 marks in total. The question dealt with:

- part (a) – a discussion on reportable operating segments,
- part (b) – calculating the effects on the statement of comprehensive income of various transactions, including an available-for-sale investment in debentures and the importing of PPE with the corresponding capitalisation of borrowing costs on a foreign loan, and
- part (c) – presentation of an extract of the statement of financial position dealing with a sale-and-leaseback (finance lease) and corresponding deferred tax implications.

Part (a) of the question counted 7 marks, part (b) counted 41 marks and part (c) counted 15 marks. There were 5 presentation marks which were awarded for the subsections.

**General comments:**
In general the candidates answered the question fairly well as reflected by the average mark indicated above. However, the fact that candidates generally neglected to calculate all foreign exchange differences was disappointing; candidates generally lost out on many marks due to this.

**Areas the candidates handled well:**
- Answers were generally fairly neat and organised.
- In respect of the discussion on operating segments (part (a)), the majority of candidates identified the issue at hand and came to the correct conclusion.
- The majority of candidates calculated the cost of the imported PPE (excluding capitalised borrowing costs) and the resulting depreciation correctly (part (b)).
- The sale-and-leaseback (part (c)) was generally answered well.

**Areas the candidates handled poorly:**
A few areas should however be highlighted, which may be of use to candidates for future examination purposes relating to general exam technique:

- Although answers were generally laid out in a fairly organised manner, it is advisable that candidates ensure their calculations are cross-referenced to their answers since many candidates failed to do so.
- As indicated earlier, the calculation of foreign exchange differences was problematic (refer to specific comments below).

**Specific comments on sections of the question (where questions are subdivided into different parts):**
Part (a)
In this section, candidates were required to discuss the appropriateness of a decision made by management not to present segment information in a scenario where various operating segments existed. Candidates had to make a conclusion by applying, amongst others, the definition of “operating segments”, the quantitative thresholds, aggregation criteria and scope of IFRS 8.

Candidates generally identified the issue at hand and came to the correct conclusion. However, the following problem areas are highlighted:

- **Application** of the principles in IFRS 8 was often vague and incomplete. For example, many candidates did not apply the requirement of “discrete financial information” by referring to the fact that financial information was available for the two segments separately. Therefore, candidates still fail to apply their theory appropriately and fail to demonstrate a thorough understanding thereof in discussion questions.
- Although almost all candidates came to the conclusion that separately reportable operating segments existed, many of them failed to answer the question, i.e. whether they agreed or disagreed with management’s decision. A statement that operating segments should be reported is inappropriate.
- Many candidates failed to address all the issues because they focussed on the different geographical areas (SA, Middle East & North America) as opposed to the different product lines (Fitness and Marine).

Part (b)
In this section, candidates were required to calculate the effects on the statement of comprehensive income of various transactions (largely financial instruments and foreign exchange transactions). More specifically, the arrangements/transactions included:

- **Part b(i)**: an investment in debentures classified as available-for-sale and a corresponding reversal of a prior period impairment loss on the investment.
- **Part b(ii)**: the importing of PPE from foreign suppliers financed by a specific foreign loan and related depreciation and foreign exchange differences.

The following problem areas were identified:

**Part b(i)**
- This subsection was answered poorly. Many candidates treated the investment in debentures as an investment in ordinary shares (i.e. without accounting for effective interest on the debentures before making fair value adjustments). In many instances the candidates simply included the coupon receipt as finance income in profit/loss in the statement of comprehensive income (as opposed to effective interest).
- The reversal of the impairment loss was the most challenging part of this subsection. As IAS 39 does not provide specific guidance, this part of the subsection tested the candidate’s ability to apply their mind to a logical and reasonable approach to reversing the impairment. Unfortunately, many candidates could not find a reasonable basis to reverse the impairment loss. This was further complicated by those candidates that accounted for the investment in debentures as an equity instrument. These candidates reversed the full amount of impairment to other comprehensive income.

**Part b(ii)**
- The main reason for cases of poor marks in this section was a lack of application of the principles of IAS 21, e.g. many candidates were unable to determine the appropriate amounts of borrowing costs to be capitalised. The problem existed more with the exchange differences than with interest. Candidates were able to determine the correct amounts of interest expense to be capitalised and used the appropriate exchange rates to translate the interest expense. As
the scenario tested all statement of comprehensive income effects, qualifying borrowing costs (i.e. qualifying interest expense and qualifying exchange differences) should be capitalised to PPE affecting depreciation to be recognised in profit or loss, whilst the remaining interest expense and exchange differences would be recognised in profit or loss.

- Some candidates calculated the cost of the different components of the PPE correctly, but failed to include such amounts in the cost of the PPE (e.g. they expensed such amounts).
- Some candidates determined the cost of the PPE on a cash basis, based on cash payments made, rather than on an accrual basis – when the risks and rewards actually transferred. These candidates also therefore used the incorrect exchange rates.
- Some candidates did not know how to calculate the borrowing costs. This was a specific loan and therefore the interest on the loan simply had to be calculated on the full £3.6 million capital for the full capitalisation period. The fact that the costs of the PPE were incurred on different dates was therefore irrelevant for purposes of calculating the borrowing costs incurred. Similarly, the interest earned on surplus funds had to be calculated on £1.1 million (being the £3.6 million funds obtained less £2.5 million cash immediately spent). No further cash was spent up until the end of the capitalisation period and therefore the surplus funds remained at £2.5 million for the full capitalisation period. In this regard, many candidates confused the incurrence of expenditure with the spending of cash (these are two different events and only the spending of cash had to be taken into account in calculating the amount of surplus funds available – also see point above).

Part b(i) and b(ii)

- Candidates often calculated the effects on the statement of comprehensive income correctly, but failed to specify whether the effect had to be recognised in P/L or OCI.

Part (c)

In this section, candidates were required to present extracts from the statement of financial position in respect of a sale-and-leaseback arrangement (finance lease).

The following problem areas were identified:

- The main reason for poor marks in this section was a failure to address the deferred tax consequences of the sale-and-leaseback. Where candidates did address the deferred tax consequences, the principles were often incorrectly/incompletely applied.
- Some candidates were unaware of the fact that the profit on sale should be deferred in the case of a sale-and-leaseback (finance lease).
- Many candidates neglected to reduce the depreciable amount of the PPE with the residual value, or they used the incorrect depreciation period (the remaining (useful) life on the date of sale-and-leaseback should have been used). The same applies for the amortisation of deferred profit.
- Candidates often calculated the lease liability incorrectly. Some candidates did not even discount the lease payments at all (used undiscounted amounts).
- In some instances the candidates did not prepare an extract of the statement of financial position, or failed to transfer calculated amounts to this statement. Moreover, many candidates did not split the lease liability between its current and non-current portions.
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>32</td>
<td>13.71</td>
<td>1091 candidates</td>
<td>2021 candidates</td>
</tr>
</tbody>
</table>

Level of difficulty:

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

Main subjects /topics examined in the question

This question examined normal income tax aspects only and there was no integration with other areas.

In part (a) the candidate was required to discuss, with reference to relevant case law, the tax consequences of a claim for damages received by the taxpayer to cover a loss of normal income, repairs to be effected and a loss of goodwill. It also examined the deduction, for tax purposes, of the related legal expenses.

Part (b) required of the candidate to calculate the provisional tax payments due in respect of the same year of assessment.

General comments:

The candidates did not do as well as was expected.

Areas the candidates handled well:

Very few candidates handled the question well.

Areas the candidates handled poorly:

The following areas should be highlighted, which may be of use to candidates for future examination purposes relating to general exam technique:

- The main problem that candidates had, in part (a), was to identify what the problem (or issue) was that needed to be covered. As the compensation accrued to the taxpayer, it was surprising to see how many candidates discussed section 11(a) principles, which were clearly not applicable or appropriate.
- The authority provided in the answers by candidates were, more often than not, not in support of (or relevant) discussion or the conclusion reached. What was required in a question like this (part (a)), was for the candidate to identify the issue, quote the relevant principle (supported by reference to the Income tax Act or the appropriate principle from a court decision) and then to make a conclusion, and this approach was lacking in most answers.

Specific comments on sections of the question (where questions are subdivided into different parts):

Part (a)
In this part a candidate was required to discuss, with reference to relevant case law, the normal tax consequences of a claim for damages received by a company and the deduction, for tax purposes, of the related legal expenses.

The most appropriate court case relevant to the question was the Fourie Beleggings v CSARS (168/08) [2009] ZASCA 37 (31 March 2009) case. This case was on the list of prescribed cases, but it was evident that many candidates did not read this case. The decision merely confirmed old principles, but if the candidates had read the case, they would have done better in their attempts.

With regard to the compensation received to effect (or compensate for) repairs to be effected, candidates really struggled. Comprehensive discussions were given regarding the application of section 11(d), but candidates then failed to link the compensation to this and to conclude that the receipt may be a recoupment.

With regard to the legal expenses many candidates discussed and applied section 11(a) principles. However, section 11(c), which specifically provided for a deduction under these circumstance, had to be applied. Candidates therefore missed marks as they did not address the issues required.

Many candidates missed the fact that the receipt in respect of goodwill must be in respect a disposal and did not deal with the capital gain consequences.

**Part (b)**

In this part it was required of the candidate to calculate the provisional tax payments due in respect of a (the same) year of assessment. This part was generally not well-answered and many candidates did not even attempt it.

The most common errors made were:

- Candidates did not increase the last assessed amount with 16% (or only increased it with 8%) to arrive at the basic amount for the first payment.
- They in general did not discuss (or calculate) whether additional tax may be levied in terms of paragraph 20 (of the Fourth Schedule).
- Very few candidates mentioned that the additional tax (in respect of the second period) is at the discretion of the Commissioner. It was therefore clear that they did not know that different rules applied to a taxpayer with a taxable income of more than R1 million.

#354390