EXAMINERS’ COMMENTS

Part II of the
Qualifying Examination-
Financial Management
November 2010
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Financial Management
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This report has been compiled from the analysis of examiners on candidates’ performance in Part II of the Qualifying Examination (Financial Management), which was written in November 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;
• tutors in preparing candidates for the Qualifying Examination; and
• future 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 examination paper.

The purpose of Part II of the Qualifying Examination is to test the integrated application of practical knowledge gained in commerce and industry.
### Analysis of first time and repeat candidates over the period 2004 – 2010:

<table>
<thead>
<tr>
<th>Year</th>
<th>FAIL</th>
<th>PASS</th>
<th>TOTAL</th>
<th>% PASS</th>
</tr>
</thead>
<tbody>
<tr>
<td>2010 First timers</td>
<td>30</td>
<td>109</td>
<td>139</td>
<td>78.4%</td>
</tr>
<tr>
<td>2010 Repeats</td>
<td>19</td>
<td>20</td>
<td>39</td>
<td>51.3%</td>
</tr>
<tr>
<td>2010 Overall 2008</td>
<td>49</td>
<td>129</td>
<td>178</td>
<td>72.5%</td>
</tr>
<tr>
<td>2009 First timers</td>
<td>36</td>
<td>82</td>
<td>118</td>
<td>69.5%</td>
</tr>
<tr>
<td>2009 Repeats</td>
<td>18</td>
<td>14</td>
<td>32</td>
<td>43.8%</td>
</tr>
<tr>
<td>2009 Overall 2008</td>
<td>54</td>
<td>96</td>
<td>150</td>
<td>64.0%</td>
</tr>
<tr>
<td>2008 First timers</td>
<td>32</td>
<td>140</td>
<td>172</td>
<td>81.4%</td>
</tr>
<tr>
<td>2008 Repeats</td>
<td>10</td>
<td>18</td>
<td>28</td>
<td>64.3%</td>
</tr>
<tr>
<td>2008 Overall 2008</td>
<td>42</td>
<td>158</td>
<td>200</td>
<td>79.0%</td>
</tr>
<tr>
<td>2007 First timers</td>
<td>28</td>
<td>48</td>
<td>76</td>
<td>63.2%</td>
</tr>
<tr>
<td>2007 Repeats</td>
<td>41</td>
<td>29</td>
<td>70</td>
<td>41.4%</td>
</tr>
<tr>
<td>2007 Overall 2007</td>
<td>69</td>
<td>77</td>
<td>146</td>
<td>52.7%</td>
</tr>
<tr>
<td>2006 First timers</td>
<td>38</td>
<td>39</td>
<td>77</td>
<td>50.6%</td>
</tr>
<tr>
<td>2006 Repeats</td>
<td>35</td>
<td>12</td>
<td>47</td>
<td>25.5%</td>
</tr>
<tr>
<td>2006 Overall 2006</td>
<td>73</td>
<td>51</td>
<td>124</td>
<td>41.1%</td>
</tr>
<tr>
<td>2005 First timers</td>
<td>39</td>
<td>60</td>
<td>99</td>
<td>60.6%</td>
</tr>
<tr>
<td>2005 Repeats</td>
<td>16</td>
<td>8</td>
<td>24</td>
<td>33.3%</td>
</tr>
<tr>
<td>2005 Overall 2005</td>
<td>55</td>
<td>68</td>
<td>123</td>
<td>55.3%</td>
</tr>
<tr>
<td>2004 First timers</td>
<td>25</td>
<td>51</td>
<td>76</td>
<td>67.1%</td>
</tr>
<tr>
<td>2004 Repeats</td>
<td>4</td>
<td>7</td>
<td>11</td>
<td>63.6%</td>
</tr>
<tr>
<td>2004 Overall 2004</td>
<td>29</td>
<td>58</td>
<td>87</td>
<td>66.7%</td>
</tr>
</tbody>
</table>
Average marks per question:

<table>
<thead>
<tr>
<th>Total marks</th>
<th>Question 1</th>
<th>Question 2</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total</td>
<td>100</td>
<td>100</td>
<td>200</td>
</tr>
<tr>
<td>Average</td>
<td>48.4</td>
<td>56.2</td>
<td>104.6</td>
</tr>
</tbody>
</table>

BACKGROUND

The Examinations Committee constantly strives to improve its ability to determine whether candidates demonstrate their ability to qualify as Chartered Accountants. This is done by means of an ongoing process of evaluation and improvement in 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 examination questions are drawn from three sources:

- Questions (the majority) are set specifically for a particular examination by the members of the Examinations Committee (a subcommittee of the Initial Professional Development Committee), who are all specialists in a particular subject area;
- Questions on a particular subject may be commissioned from persons in commerce and industry as well as in public practice by the Project Director: Education; and
- Questions submitted by practitioners, accountants in commerce and industry, and academics are added to a question pool that has been built up over the years and are also used in the examination papers.

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 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 after 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, who authorises the final suggested solutions and the mark plans that are 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 at least two 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 that they retain. Once marking has been completed both markers marks are entered on the front cover and where there are more than two marks different the markers confer and jointly decide on the final mark to be awarded. The final mark is then noted 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 Initial Professional Development (IPD) Committee as soon as possible after the Project Director: Education has received the mark list from the umpire.

The members of the Committee receive lists of candidates – who are identified only by a ranking number based on marks obtained for the examination – together with the marks awarded to every candidate for every question. The members of the Initial Professional Development Committee base their decisions of which candidates passed with honours, which candidates passed, and which did not pass, on the marks as set out in these lists.

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

- The Initial Professional Development Committee’s expectations for each question;
- The level of difficulty for each question;
- Comments from universities, markers and umpires with regard to any marking difficulties which were encountered or candidate time constraints which were noticed;
- 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 academia who is a member of SAICA’s Initial Professional Development Committee is allowed to serve on the Examinations Committee, and that candidates’ anonymity is preserved until the final adjudication has been completed.
GENERAL COMMENTS ON RESPONSES

1 Objective

In view of the primary objective of Part II of the Qualifying Examination (Financial Management), namely to test the integrated application of practical 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 Comments

From a review of candidates’ answers to the two examination questions for the November 2010 examination the following basic deficiencies were identified. These problems affected the overall performance of candidates, and it is a matter of concern that candidates annually make the same mistakes. 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.

2.1 Layout and presentation

Candidates’ layout and presentation has improved since prior years. Candidates should allocate time to planning, layout and presentation of their answers before committing thought to paper as the presentation marks account for 5% of the total available marks. 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, such as a letter, memorandum or report.

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. Poor spelling and use of unintelligible abbreviations remain problematic.

It is crucial that candidates make use of proper language styles in presenting their answers as the use of “sms language” is an unacceptable form of communication for Part II of the QE.

2.2 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.

2.3 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.

2.4 **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.

2.5 **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, provided answers in the form of statements while calculations were required or presented financial statements where a discussion of the appropriate disclosure was required.

2.6 **Basic numeracy skills**

It was disappointing to note that many candidates did not display basic numeracy skills. We expect at this level that candidates are able to apply basic numeracy skills, particularly as they have already successfully completed Part I of the Qualifying Examination. Basic numeracy skills are important both in this exam and in practice and it is important that candidates have a good grasp of these basic skills.

3 **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. This is a major concern, because by the time candidates qualify for entrance 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. After all, in a work situation no accountant can expect to deal with textbook type clients and situations, neatly set out in logical format!

4 **General comments by the umpires**

The format of the examination changed in 2007. Previously, candidates wrote the entire paper in one sitting. The exam was divided into two separate questions with each question allowing an additional 20 minutes reading time over and above the normal 2 and ½ hours writing allocated. This should have allowed candidates to read and absorb the facts of the question before committing their answers to paper. In addition, it should have prevented the overrunning of time between the two questions.
The paper was challenging overall and dealt with practical issues. It is clear from the analysis of the results that candidates found question 2 to be easier than question 1. However, the standard of Question 1 was found to be appropriate and in line with prior years.

Generally the exam technique displayed by most candidates was disappointing. This would include:
- not reading the required carefully;
- dumping information in the hope that the examiner will award marks for something (this only irritates markers and the candidate wastes valuable time);
- time management;
- a legible handwriting and setting out answers in a manner that is easy to read;
- poor spelling and use of unintelligible abbreviations;
- candidates inability to apply their knowledge to the scenarios presented in the questions; and
- clarity of expression.

Detailed analyses of the questions are set out for each question later in this report. But in general it is clear that candidates struggled with sections that required application of knowledge and/or original thought.

The paper covered a broad range of issues and was a fair test of candidates’ ability to apply knowledge to specific scenarios. However, it was clear that most candidates are still not comfortable attempting “case study” type questions.

University comments

We received commentary from the Universities. Most Universities were highly complementary of the overall paper. Certain universities criticised the paper for focusing too much on financial analysis. The Universities perceived question 1 as the more difficult question.

The mark team reviewed the detailed university comments and amended the mark plan(s) where appropriate.

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

Please start preparing for next years’ examination in good time.

Opera singer Beverly Sills once observed: “There are no shortcuts to any place worth going” and John C. Maxwell said: “A person who has a dream knows what he is willing to give up in order to go up.”

Best of luck!!

Sandy van der Walt
Project Director: Education
Brainz (Pty) Ltd is a large consulting practice group with various subsidiaries. The key subsidiary had performed poorly in the 2010 financial year due to the economic conditions and as a result of certain ill-timed and ill-conceived strategic decisions. Brainz also recently acquired a 40% interest in an internet dating company based in the Bahamas. Brainz is intent on improving its corporate governance ahead of its planned listing on the JSE.

<table>
<thead>
<tr>
<th>Topics examined</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corporate governance (King III)</td>
<td>18</td>
</tr>
<tr>
<td>Critical analysis of marketing strategy &amp; performance</td>
<td>12</td>
</tr>
<tr>
<td>Financial analysis</td>
<td>30</td>
</tr>
<tr>
<td>ROE and business sustainability</td>
<td>7</td>
</tr>
<tr>
<td>Ethics (conflicts of interest)</td>
<td>8</td>
</tr>
<tr>
<td>Critique of a valuation</td>
<td>20</td>
</tr>
<tr>
<td>Presentation</td>
<td>5</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>

Candidates generally struggled with parts (d) and (e) in Question 1. Part (d) required candidates to identify and discuss why a subsidiary yielded a high ROE and to comment on the sustainability of the business. Part (e) asked candidates to identify and discuss potential conflicts of interest arising from Brainz acquiring a minority stake in an entity from Brainz’ controlling shareholders.

Specific comments made by the examiners:

Overall, candidates’ performance in Question 1 was disappointing given the opportunity to score well in part (a), (c) and (f).

Part (a)
This part required a listing of areas of non-compliance with KING III and the reasons for non-compliance. Good results were obtained for this part, but nevertheless, candidates often seemed to venture a guess as to area of non-compliance and its reason. As a result, for the 2nd mark, we updated the marking approach to award 2 marks, or zero, per line in the mark plan – with the argument that a candidate needed to identify the intricate link between the area of non-compliance
and its corresponding reason, to earn the marks. Furthermore, the layout of candidates’ answers could be improved - it should rather follow a layout similar to that of the mark plan.

**Part (b)**

Part (b) required a review and discussion of the marketing strategy and performance of one of the divisions, based on the supplied information. It contained many easy marks, e.g. several half-marks for a discussion of the graphs supplied in the question. Candidates scored marks for these, but their comments often stated the obvious without adding sufficient value to earn a mark. No marks were available for repeating information supplied in the question.

**Part (c)**

This required a critical analysis and comment on the historical and forecast performance of a division. It also contained many easy marks, e.g. calculation of expenditure as a percentage of gross revenue, or the percentage change. Candidates scored marks for these, but sometimes failed to calculate the figures for all the required years, or made basic calculation errors. Due to the relative ease with which marks could have been earned here, marks were allocated only where amounts for all years were calculated correctly (after allowing for slight rounding differences). The mark plan should highlight that calculation marks were easily achievable however, commentary thereon required higher level application.

**Part (d)**

This part required identification, with reasons, of why a specific division yielded a high ROE and comments on its sustainability. Candidates’ answers were disappointing, and the presentation of their answers often did not offer a clear distinction between the two components required (ROE and sustainability). Some candidates did not attempt part (d) at all.

**Part (e)**

This required identification and description of possible conflicts of interest arising from an investment made. This part was generally answered poorly and candidates failed to display the proper insight. It is disappointing to note that the overall performance in this section, which dealt with ethical issues, was poor.

**Part (f)**

In a typical fashion, part (f) required a critical review and comment on a valuation performed with appropriate calculations, instead of performing a valuation. Generally this was well answered, but candidates failed to score marks for the allowed calculations and also missed some of the ‘finer’-points of valuation (such as a the concept of a ‘minority discount’, a comparison with earlier valuations and transactions, the performance of sensitivity analysis, and the comparison with benchmark entities).

In certain areas of the valuation, several candidates failed to incorporate the circumstances of the case in hand by merely presenting standard or memorised arguments. For example, this valuation was of a new company offering internet-dating services, charging US$10 per client per month for
the service throughout the forecast period. However, we would expect candidates to apply their minds and recognise potential competition and the trend of ‘free’ internet based sites generating advertising revenue which may result in declining membership fees over time..

Presentation

This area could be improved upon. Language usage displayed an average level of proficiency even when considering the effects of the time-pressure, with many spelling errors. Candidates should be careful of making contradicting statements in their answers as this jeopardises their chances of achieving marks for logical argument.

Question 2

Number of scripts marked: 178

<table>
<thead>
<tr>
<th>Maximum mark</th>
<th>Average mark</th>
<th>Marks &gt; 50%</th>
</tr>
</thead>
<tbody>
<tr>
<td>100</td>
<td>56.2</td>
<td>76%</td>
</tr>
<tr>
<td>Highest mark</td>
<td>Lowest mark</td>
<td>Marks &lt; 50%</td>
</tr>
<tr>
<td>82</td>
<td>33</td>
<td>24%</td>
</tr>
</tbody>
</table>

Level of difficulty: Average to easy

Sassi Stores is a well established retailer selling clothing and accessories. The business is considering establishing a division to provide credit to customers.

<table>
<thead>
<tr>
<th>Topics examined</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rolling forecasts</td>
<td>10</td>
</tr>
<tr>
<td>Retaining surplus cash or gearing business?</td>
<td>8</td>
</tr>
<tr>
<td>Analysis and commentary on business plan of proposed Credit division</td>
<td>27</td>
</tr>
<tr>
<td>Estimation of IRR of proposed Credit division</td>
<td>12</td>
</tr>
<tr>
<td>Decision making re establishing Credit division</td>
<td></td>
</tr>
<tr>
<td>• Business risks</td>
<td>16</td>
</tr>
<tr>
<td>• Other key issues in deciding whether to start division</td>
<td>12</td>
</tr>
<tr>
<td>Identification of key internal controls in Credit division</td>
<td>10</td>
</tr>
<tr>
<td>Presentation</td>
<td>5</td>
</tr>
<tr>
<td></td>
<td>100</td>
</tr>
</tbody>
</table>

Candidates performed poorly in the financial analysis section [part (c)] and in part (e) (ii) which required higher level application from candidates in identifying issues for consideration in establishing the credit division.
Specific comments made by the mark team:

Part (a)

This part was generally well attempted. Candidates who did not score well often did not answer the question or simply said agree/disagree with no further explanation.

Part (b)

The question required a critical discussion of, inter alia, Ms Sassoni's view that surplus cash should be paid out as dividends. It was disappointing to note that many candidates listed theories re dividend policy without answering the question. For example, certain candidates discussed the ‘signaling’ effect of dividends which was not relevant given that Sassi Stores is a private company.

Part (c)

Candidates’ performance in this section was generally disappointing, and this appears to be a trend in financial analysis type questions in recent years. Candidates appear to struggle to comprehend what is required by ‘critically analyse and comment’.

Candidates often missed ‘easy’ marks for calculating relevant ratios. It was disappointing to note how few candidates analysed and commented on average purchases, repayments and balances of account holders. It was disturbing to note that certain candidates wrote 2 pages on pin card revenues and charges when this was immaterial in amount.

Part (d)

The calculation of the IRR of the Credit Division presented an opportunity for candidates to score well. Most did however, it is concerning that certain candidates included non-cash flow items in IRR analysis. Many candidates failed to include working capital movements and an estimation of the terminal value of the division.

Part (e)(i)

Candidates generally perform well in the identification of business risks, and this trend continued in this exam.

Part (e)(ii)

Most candidates performed poorly in this section. This is a concerning trend in exam performance where candidates generally are unable to apply their minds and indentify key issues in decision making. A review of the final mark plan will reveal that many marks were available.

Part (f)

Most candidates scored well in this section, displaying a good understanding of internal controls relating to debtors and credit management.
Presentation

Poor spelling and use of unintelligible abbreviations remain problematic for markers. Presentation marks accounted for 5% of total available marks and we would have thought that this deserved more attention from candidates.

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