MARKERS’ AND UMPIRES’ COMMENTS QUALIFYING EXAMINATION
Part I – MARCH 2004

This report has been compiled from the analysis of examiners on candidates’ performance in Part I of the Qualifying Examination, which was written in March 2004. 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 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.

STATISTICS FOR THE QUALIFYING EXAMINATION

In 2004 1 783 candidates passed Part I of the Qualifying Examination, compared to 1 534 in 2003.

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<th>% Pass</th>
<th>Passed</th>
<th>Failed</th>
<th>Total</th>
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<tbody>
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<td>First attempt</td>
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<td>1 219</td>
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<tr>
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<td>46%</td>
<td>1 783</td>
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Average marks per question:

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<tr>
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<th>Question 1</th>
<th>Question 2</th>
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<tr>
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**BACKGROUND**

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 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 Education 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 Senior Executive responsible for the examination; 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 Education Committee devotes a great deal of time to the review and refinement of mark plans to ensure that the plans are consistent with its expectations for each question.

Before marking of the scripts commences, copies of the examination papers and suggested solutions are forwarded to all participating universities for comment. The markers and umpires decide on a suggested solution and mark plan 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 Education Committee, who 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 at least four 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 by two different persons who record their marks on a mark list. 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 Education Committee as soon as possible after the Senior Executive: Education and Training has received the mark list.

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 Education 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 Education Committee considers all relevant evidence, including the following:

- The Education 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 academe who is a member of SAICA’s Education Committee is allowed to serve on the Examinations Committee, and that candidates’ anonymity is preserved until the final adjudication has been completed.

In order to ensure that the whole marking and adjudication process remains anonymous, the instructions to candidates clearly state that their names should not appear anywhere. This aspect also relates to questions where candidates are required to write a letter or a report to management. In these cases questions should be signed off using words like “Joe Bloggs”, “QE candidate”, “A Student” etc.
GENERAL COMMENTS ON RESPONSES

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 Comments

From a review of candidates’ answers to the eight examination questions for the March 2004 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 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, i.e. in the form of a letter, memorandum or a 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. Candidates should use dark ink when answering questions.

The use of abbreviations should be limited and where abbreviations are used these should be official abbreviations only. Candidates seem to increasingly use unofficial abbreviations where markers are expected to guess what candidates are saying. If a marker does not understand what a candidate is writing no marks can be awarded!

Some candidates also wrote answers on the back of the answer sheets. This is very easily missed in the marking process.

2.2 Technical knowledge

A specific concern raised by markers of this year’s examination was that candidates demonstrated a lack of technical knowledge in some areas considered to be basic. Candidates were confused with the content and applicability of accounting standards and often mixed up the concepts in different
Candidates also did not demonstrate a sound knowledge and understanding of the Public Accountants’ and Auditors’ Act or the Companies Act.

Candidates should not rely on the fact that books are available in the examination and consequently neglect basic knowledge of technical pronouncements and legislation.

2.3 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.

2.4 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.

Markers also found that some candidates waste time by highlighting and underlining key points in their solutions.

2.5 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.

2.6 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.

2.7 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 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 sitting for 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 Open-book examination

A particular 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 essential 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 before will be disadvantaged as they are unlikely to finish the paper.

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 anyplace worth going”.

A person who has a dream knows what he is willing to give up in order to go up.

- John C. Maxwell

Best of luck!!
Paper 1 consisted of four questions that dealt with consolidated financial statements, statutory and other considerations relating to the financial position of a company and remuneration of executive directors, a taxable income calculation for an individual and capital budgeting and break-even calculations for a business.

Question 1

Number of scripts marked: 3 857

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<th>Marks &gt; 50%</th>
<th>Marks &lt; 50%</th>
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<td>90</td>
<td>38</td>
<td>1 126 (29.2%)</td>
<td>2 731 (70.8%)</td>
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Level of difficulty: Average

In this question candidates had to draft a letter to the accountant of a large listed conglomerate company dealing with four scenarios regarding the consolidated financial statements. Part (a) related to the inclusion of future expected losses of Australian branches of a subsidiary. Candidates then had to discuss the appropriate date of acquisition of a subsidiary (part (b)) and calculate the cost of acquisition of another subsidiary (part (c)). In part (d) candidates had to prepare the translated trial balance of a foreign subsidiary and prepare the pro-forma consolidation journal entries. Part (e) required extracts from the consolidated cash flow statements relating to the acquisition of shares in a subsidiary.

Many candidates did not answer the question in letter format. Candidates generally performed well in part (a). Some candidates discussed discontinued operations in this section but no marks were awarded for these discussions. Candidates alluded to restructuring provisions and onerous contracts, without going into further discussion as required, and applying the statements to the question concerned.

Although candidates could generally state the definition of control, as per AC131 they were unable to identify the dates in question and debate the actual date of acquisition in part (b). Many candidates were unable to grasp the fact that divisions are operating units of the company itself, and not separate legal entities.

Candidates generally passed part (c) of the question but did not deal well with the bonus payable to directors. Further, although candidates could quantify the cost of acquisition, they did not supply reasons for what they did. Some candidates were unable to differentiate between the calculation of the cost of acquisition versus the underlying net asset value of the subsidiary being purchased. This
lack of understanding resulted in incorrect goodwill figures in the journal entries requested as a portion of part (d).

Part (d) was generally handled well by candidates although many candidates did not do an equity analysis, which was necessary in order to do the translation of the trial balance. Further candidates did not make the necessary adjustments before translation of the trial balance. Many candidates were not able to prepare consolidation journal entries. It was clear from many of the scripts that there is a limited understanding of the underlying concepts of consolidation.

Many candidates prepared the cash flow statement in part (e) on a proportionate consolidation basis. This was incorrect and no marks were allocated for such answers. Candidates were unable to determine that the underlying assets and liabilities of the subsidiary company were purchased at fair value. Few candidates calculated the goodwill relating to the increase in shareholding in the subsidiary company, and the amount relating to outside shareholders. There were a handful of candidates who were able to calculate the non-cash flow items relating to the inclusion of the subsidiary company.
Question 2

Number of scripts marked: 3 857

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<td>30</td>
<td>15</td>
<td>2 114 (54.8%)</td>
<td>1 743 (45.2%)</td>
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Level of difficulty: Average

This question dealt with specific issues relating to the finalisation of the audit of a listed company. Part (a) required a discussion of the financial position of the company and related reporting requirements or considerations. Candidates were to specifically consider the requirements of Statements of Generally Accepted Accounting Practice, the Companies Act, the Public Accountants’ and Auditors’ Act and South African Auditing Standards. In part (b) candidates had to discuss the composition and role of the Remuneration Committee and in part (c) they had to discuss considerations to be borne in mind from the Companies Act in response to the remuneration of executive directors. Finally, candidates had to provide an analysis of the accounting implications of an event after balance sheet date and also had to draft the appropriate note to appear in the annual financial statements (part (d)).

Part (a)(i) – discuss the requirements of GAAP

Generally candidates performed well in this section. Most candidates were able to indicate the going concern issues and assumptions that required consideration. Candidates also considered the disclosure of the factors causing uncertainty about the going concern and preparing the financial statements on the liquidation basis.

Part a (ii) – discuss the issues that arise from the Companies Act

This section was poorly answered. Candidates appeared to lack the knowledge necessary to provide an appropriate answer relating to the application of the Companies Act. Those candidates who earned marks did so by virtue of a theoretical reference to section 424 of the Companies Act and the resultant possibility of being held personally liable.

Very few candidates referred to the judicial precedence or provided any distinction between “factual” and “commercial” insolvency.

Part a (iii) – discuss the requirements of the PAA Act and SAAS

It was surprising how poorly candidates answered this section.

Candidates were not able to identify the two problems being the “going concern problem” and the “material irregularity relating to the mechanism and manner of paying remuneration to directors, the no payment to the fiscus of withholding taxes and the apparent inability of the company to pay its debts when due.”
In most cases very general answers were provided, with no linkage back to the question and the scenario given to candidates. Where marks were earned this was the result of candidates describing the process of reporting a Material Irregularity as opposed to analysing the situation.

**Part b – discuss the composition and role of the remuneration committee**

It was pleasing to observe a strong level of awareness of the general requirements of the King Code and Corporate Governance as related to the remuneration committee.

**Part c – discuss the remuneration structures utilised by the directors**

This section was poorly answered.

Candidates did not answer in a lateral manner, with answers focusing only on a single aspect – for instance disclosure or remuneration or approval under section 226.

**Part d - consider flood damage to grain in storage and a related insurance claim and provide illustrative disclosure**

Candidates either scored very well on this section, or scored very poorly.

Many candidates have not updated their knowledge levels and referred to outdated terms and concepts when considering the event after balance sheet date.

Further, despite it being clear that the event (a flood) occurred after year-end, many candidates convinced themselves that the event was an adjusting event on the basis of unrelated factors (the roof had leaks at year end).
Question 3

Number of scripts marked: 3 857

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<td>35</td>
<td>24</td>
<td>3 677 (95,4%)</td>
<td>180 (4,6%)</td>
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Level of difficulty: Easy

Candidates were required to calculate the taxable income of an individual. The scenario included information relating to pension, dividends and interest (local and foreign), income from a property and an equity unit trust, a net capital gain from disposal of unit trusts and other financial instruments, other capital gains and losses, income from temporary employment (including fringe benefits), income from a trust, expenses (interest, medical and dental) and donations.

Candidates should take care when performing calculations to ensure accuracy. Candidates made basic transposition mistakes and basic calculation errors (for example, adding R18 000 to R1 200 to get R30 000).

The most common errors candidates made were as follows:

- Inclusion of withholding taxes and/or underlying taxes with the foreign dividends.
- The exemption of the R10 000 local dividend received from the trust (it is an annuity).
- Deduction of R6 000 in respect of interest incurred to earn foreign dividends was limited to R2 400.
- The wrong reasons were given for the disallowing of the rental expenses incurred.
- Rental expenses incurred were misread as being rental income accrued to Mr Rose.
- Donation was incorrectly claimed. Lack of knowledge of section 18A.
- Many candidates were not aware of the sequence in which the tax computation for an individual needs to be done.
- The capital gains tax portion was answered poorly. Many candidates did not know how to apply the R10 000 exclusion for individuals, nor reasons for non-taxing of capital gains, nor the issue that all gains and losses must be aggregated before the annual exclusion and the inclusion percentage is applied.
- Deduction of the primary rebate against taxable income rather than against tax payable. The latter which was not tested.
- A section 6quat reduction was calculated. This was not part of the required.
- Some candidates used an interest exemption of R6 000 in terms of section 10(1)(i), which was the exemption in 2003.
- The salary for Mr Rose for the period that he worked overseas was multiplied by 2 by a small number of candidates who did not read the question properly.
- A good proportion of candidates used a 50% inclusion rate for individuals, rather than the inclusion percentage of 25% in respect of the capital gain.
- Cellular telephone and entertainment expenses were incorrectly deducted.
- Many candidates did not know that the foreign dividend exemption could be utilised against foreign interest.
- Many candidates deducted 5% of taxable income for the medical deduction.
Question 4

Number of scripts marked: 3 857

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<td>20</td>
<td>1 427 (37,0%)</td>
<td>2 430 (63,0%)</td>
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</table>

Level of difficulty: Average

Candidates were presented with information about a company operating ten health clubs in the Western Cape, wanting to expand their activities to Gauteng. For part (a) candidates were required to assimilate information in the question and prepare a capital budget in order to determine the net present value of forecast cash flows. Candidates had to identify non-relevant cash flows, and incorporate working capital and rent deposits into forecasts. Candidates then had to perform a break-even calculation (part (b)). Part (c) required candidates to list the benefits of leasing as opposed to purchasing gym equipment. Part (d) dealt with factors to consider in determining a discount to offer members for paying membership fees in advance and part (e) required a list of procedures to assess creditworthiness of new members.

Common mistakes made in part (a) included:
- Including financing costs in forecast cash flows
- Excluding return of rent deposit and working capital invested at the end of budgeting period
- Including tax in cash flows when question clearly stated that the discount rate was a pre-tax rate of return

Overall performance in part (b) was very poor mainly due to the inability to distinguish between fixed and variable expenses. The question was very clear on the nature of costs and many candidates failed to read and apply given information.

Parts (c), (d) and (e) were well answered.
Paper 2 consisted of four questions, and dealt with the accounting treatment of customer acquisition costs, a defined benefit fund and a Black empowerment transaction, tax implications for a company on a government tender and disposal of an investment in property, process costing in a manufacturing concern, considerations regarding the outsourcing of functions, identification of business risks and implications for the overall audit plan, as well as issues regarding the SAICA Code of Conduct and the King Code 2002.

Question 1

Number of scripts marked: 3 848

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<tbody>
<tr>
<td>70</td>
<td>33</td>
<td>1 766 (45,9%)</td>
<td>2 082 (54,1%)</td>
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Level of difficulty: Average

In this question candidates were presented with a scenario relating to a listed company that is the owner and operator of a cellular telecommunications network. The question required candidates to evaluate the recognition and measurement of customer acquisition costs and recommend changes where appropriate. Secondly, candidates had to discuss the income tax and deferred tax implications of the customer acquisition costs. For part (c) candidates had to prepare journal entries to record the movement in the defined benefit asset or liability arising from the company’s pension fund. In part (d) candidates were required to prepare a reconciliation of the defined benefit asset/liability as disclosed in the financial statements to the plan assets and defined benefit obligations of the pension fund. Finally (part (e)) candidates were required to discuss the appropriate recognition and measurement of a potential bonus payment to a company as part of a Black economic empowerment transaction.

Part (a) was answered poorly by most candidates, despite the fact that generous marks were allocated to theory from the AC statements. Candidates generally dumped a lot of information without drawing any conclusions – therefore not applying their theoretical knowledge in response to what was required.

Candidates’ performance in part (b) was disappointing. The knowledge required for this section was deemed basic but candidates were generally unable to apply their taxation knowledge to the given scenario. The level of discussion provided by candidates was not sufficient in respect of the
deductibility of the costs. Many candidates noted that the costs were deductible but did not expand on the requirements of the Act and how the costs met the requirements of the Act. The discussions surrounding the deferred taxation implications of the acquisition costs were fairly comprehensive, resulting in most candidates being able to pass part (b).

Part (c) was generally answered well by candidates.

The markers felt that part (d) provided candidates with some easy marks as the solution literally only required an answer in terms of AC116. However, candidates performed very poorly in this section.

Part (e) was fairly difficult, but candidates’ knowledge of financial instruments was very poor and candidates generally did not score well in this section.
Question 2

Number of scripts marked: 3 848

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<tbody>
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<td>21</td>
<td>2 389 (62.1%)</td>
<td>1 460 (37.9%)</td>
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</table>

Level of difficulty: Average

This question required candidates to advise on two tax issues that arose during the audit of a group of companies. The first issue related to a government tender to provide computers to the Department of Education. The company received an advance payment for these computers, had to manufacture and deliver the computers on agreed dates over a period of three years and invoice the Department for deliveries made. The company also made a payment for advertising space in a local IT magazine. Candidates were required to state the amounts to be included in taxable income as well as any tax deductions arising from these transactions for each of the affected tax years.

The second issue related to a subsidiary who owns an office building and the holding company was considering disposing of the building. The question presented two options to dispose of the building, the one option being a sale of the shares of the subsidiary and the other one winding up the company. Candidates were requested to advise (giving supporting reasons and calculations) the Board of the holding company as to the option that would result in the greater cash proceeds on disposal after taking tax into account.

The question was practically oriented as it tested the candidates’ ability to combine different aspects of taxation and not only required of them to focus on one specific issue. The paper, therefore, tested the candidates’ understanding of taxation and how it influences cash flows.

Generally candidates could see the different aspects that were involved in the calculations, but did not necessarily address cash flows as required.

A lot of candidates made simple errors for example presenting amounts in millions and then switching to thousands or inserting amounts under the incorrect year of assessment.

ISSUE 1

Some candidates did not pay attention to the required part of the question and only presented comments and explanations applicable in general and not specific amounts to be included and deducted for each of the three years of assessment.

Most candidates correctly included in gross income R5 million in 2004, R40 million in 2005 and R60 million in 2006. A few candidates included the full R105 million in gross income in the 2004 tax year.

A surprisingly large number of candidates identified that the company received money upfront, which needed to be used to finance future expenditure in terms of a contract. Quite a lot of them called the tax relief a “section 24 debtors allowance”, although it seemed as if they understood the
reasoning behind it. Most candidates who identified the section 24C allowance remembered that they needed to add it back in the subsequent year of assessment.

Common errors included:
- Calculating a section 12B capital allowance (50/30/20) instead of section 12C
- Calculating the section 12C allowance (20% for 5 years) instead of the accelerated 12C allowance (40%/20%/20%/20%)
- Allowing a section 12C capital allowance as from the 2004 year of assessment
- Allowing the R6 million paid for the manufacturing machinery in full in the 2004 tax year.

Very few candidates mentioned the treatment of trading stock (being either closing or opening stock).

Quite a few candidates argued that the advertising costs would bring about an enduring benefit and therefore, being capital in nature, was not deductible in terms of section 11(a). Many candidates argued that the advertising costs would be deductible in terms of section 11(a), but that section 23H applied and, therefore, they deducted R45 000 in the 2004 tax year and R15 000 in the 2005 tax year.

**ISSUE 2**

A few candidates did not compare the net cash flows from the two options as the question specifically instructed them to do. Instead, they compared the tax consequences of the two options. Many candidates did not appear to understand the principles of cash flows.

Many candidates did not conclude as to which would be the better option.

It seemed that several candidates used a recipe to calculate specific items without seeing the bigger picture. A clear example of this was the fact that they knew how to calculate the income tax recoupment on the asset and the CGT on assets, but did not understand how the two calculations influenced each other.

A large number of candidates did not address the STC implications or only referred to the very basic principles.

A few candidates mentioned the section 47 election which was not relevant in this scenario.

Candidates who presented a structured solution did well in this part of the question without really indicating whether they truly understood the principles tested.

**Option A**

This was generally answered well by candidates.

Some candidates included the R4 million in the proceeds and therefore calculated the capital gain as R27 million – R21 million = R6 million.
Quite a few candidates deducted the R4 million received for the loan in the calculation of the net cash flow instead of adding it.

A few candidates also deducted stamp duty or transfer duty in calculating the net cash flow from this option.

**Option B**
Most candidates calculated the normal tax and CGT payable by the subsidiary, but forgot about the STC-consequences on the declaration of the dividend to the holding company.

Quite a lot of candidates forgot that the STC would be payable by the subsidiary. They used 12.5% instead of 12.5/112.5.
A few candidates even identified that the subsidiary could have elected section 64B(5)(f).

The capital gain on the sale of the office building was answered well and calculated correctly. A few candidates calculated a recoupment of the section 13(1) tax allowance claimed previously (which is obviously incorrect as this was not a factory but an office building.)

The sale of motor vehicles was generally answered well. However, quite a number of candidates calculated a capital gain or even a loss on the sale of the motor vehicles. Most candidates, however, identified that there would be no CGT consequences, but sometimes for the wrong reason (e.g. personal use asset).

Many candidates claimed a section 11(i) bad debt allowance of R800 000 on the trade receivables. They therefore did not identify the R800 000 as a capital loss.

Only a few candidates calculated a net capital gain before multiplying by 15%. Some even calculated a capital gain or loss for the office building, motor vehicle and debtors jointly.

Calculation of STC – common errors:
- Most candidates calculated the capitalisation issue correctly and knew that the R5 million transferred from share premium is subject to STC. A few candidates calculated it as R3 333 333.
- Some candidates calculated STC on part of the NDR.
- Quite a number of candidates calculated STC on the net proceeds from the sale instead of on the reserves.

Generally candidates handled the cash distributed to Cemer Holdings Ltd well. Some candidates forgot about the cash on hand of R700 000. Some candidates mixed the net proceeds and the reserves. Quite a lot of candidates added the R4 million loan repayment.

Most candidates forgot about the CGT consequences in the hands of Cemer Holdings Ltd. Only a few candidates identified that par 26(3) applies and that the base cost must be limited to proceeds.
Question 3

Number of scripts marked: 3 848

<table>
<thead>
<tr>
<th>Maximum mark</th>
<th>Average mark</th>
<th>Marks &gt; 50%</th>
<th>Marks &lt; 50%</th>
</tr>
</thead>
<tbody>
<tr>
<td>40</td>
<td>22</td>
<td>2 569 (66,8%)</td>
<td>1 280 (33,2%)</td>
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</tbody>
</table>

Level of difficulty Easy

Candidates were presented with the draft budget and related information of a manufacturer of liquid fertiliser. The question also included information regarding the possible outsourcing of the transportation of its finished products to a third party transport company. Part (a) required a recalculation of the budgeted profit on an absorption costing basis. In part (b) candidates had to discuss the potential benefits of the company using a standard costing system and in part (c) candidates had to discuss how the company should evaluate the financial feasibility of outsourcing the transportation of the finished products. Finally, (part (d)) candidates were required to list the factors and potential issues to be considered in evaluating whether to outsource the transportation.

Most candidates did not attempt the question in a process costing format; based on the answers it appeared as if candidates were not familiar with process costing methodologies – very few candidates calculated equivalent units. However, in applying first principles many candidates were still able to earn a significant portion of the marks.

Given the fact that the question was comparatively basic, the average mark of the question was disappointing; the main reason for this was poor average marks for the numeric portion of the question.

In part (a) candidates generally did not exclude non-manufacturing costs (distribution costs) from the calculations.

In answering part (b) many candidates contrasted standard costing and activity based costing (ABC). This was not called for in the question; and in fact standard costing and ABC are not mutually exclusive.

Many did not realise that the question called for a long term analysis in part (c) i.e. that NPV analysis would have been called for and many candidates did not exclude sunk costs from the analysis.

Many candidates did not read the question properly and did not separate financial from non-financial considerations in answering parts (c) and (d).
Question 4

Number of scripts marked: 3 848

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<th>Marks &lt; 50%</th>
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</thead>
<tbody>
<tr>
<td>50</td>
<td>22</td>
<td>1 208 (31,4%)</td>
<td>2 640 (68,6%)</td>
</tr>
</tbody>
</table>

Level of difficulty  Difficult

The question related to an audit of a listed company that assembles and distributes personal computers. The scenario included information about a new governance process being implemented by the board of directors in order to meet their obligations under the King Code 2002 with regard to internal controls. The company established an Audit Risk and Control Committee and has requested that the auditors attend future meetings of this committee. Extracts from papers to be tabled at the next meeting were presented in the question and related to a proposed software upgrade, a price war in the personal computer market, statutory records, warranty repairs business continuity planning, cheque signing procedures, IT environment controls and the reconciliation procedures of accounts payable. Part (a) required of candidates to, for each of the issues set out in the committee papers, identify the potential risk to the business and list the factors to be considered in assessing the significance of those risks. In part (b) candidates had to discuss the effect of the issues (identified in part (a)) on the overall audit plan. Candidates then had to discuss issues arising from the SAICA Code of Conduct and in accepting the invitation to attend the Audit Risk and Control meetings (part (c)) and finally candidates had to list ways in which the audit firm could assist the directors in fulfilling their responsibilities under the King Code 2002 (part (d)).

While candidates were able to satisfactorily identify the business risks in part (a), they appeared unable to assess the significance of those risks.

In part (b) many candidates did not attempt to develop audit responses tailored to the specific risks identified, but instead provided generic answers. Candidates appeared generally incapable of formulating appropriate audit responses to the identified risks.

Part (c) was generally poorly answered. Answers provided were generally very short and many candidates could only identify independence as one of the considerations. This was either an indication that candidates had run out of time or did have sufficient knowledge to answer this section.

Part (d) was also not handled well by candidates. Candidates were unable to apply knowledge in this practical manner.