

KE1 – Financial Accounting & Reporting Fundamentals

March 2018

Examiner's comments

Question-wise comments

Question 01

10 parts from different areas of the syllabus MCQ – Compulsory – 20 Marks

Most of the candidates were given incorrect answers for 1.2, 1.4, 1.5 and 1.9.

This is due to lack of sound knowledge on source documents (part 1.5) and accounting standards (part 1.2 & 1.9).

Question 02

10 parts from different areas of the syllabus – Compulsory – 30 Marks

This section contained 10 sub questions in different topics; some of them are calculations and some of them required short or explanatory answers.

Part 2.1

Almost all the candidates answered this part and scored marks; but some of the candidates failed to identify the meaning of “liability is limited” which is an advantage of limited liability company

Part 2.2

Responsibilities of audit committee were tested here. Majority of the candidates were not aware of the audit committee. They had misinterpreted it and had written about the internal audit, external audit program, duties of external/internal & government auditors, etc. It is very important to refer to subsequent additions to the subject area published by the Institute.

Part 2.3

This question was based on conceptual framework for financial reporting.

The expectation was to identify the scenario given as an asset or not. Most of the candidates had identified correctly but were unable to justify the reason for their decision referring to the conceptual framework. Therefore, some of the candidates had referred to the accounting concepts such as accrual basis.

Part 2.4

The need for maintaining the primary books were tested.

Most of the candidates had given the answer which was not expected by the examiner. Most of them answered for “what is” instead of “need for”.

Some of the candidates do not have an understanding of the difference between a source document and a primary book (accordingly a few had mentioned that sales/purchase return day books are documents)

Part 2.5

Tested basic double entry recording based on the source documents. Performance is at an acceptable level Further some students lost marks as they hadn't written figures (incompleteness). In addition, some misunderstandings were noted in the answers to part ii, which demonstrated lack of knowledge over which party who should have originated the credit note.

Part 2.6

Reconciliation of control accounts balance was tested in this question and this was a practical application question. Most of the candidates had answered, assuming the routine pattern, i.e. considering all given errors should be adjusted, and therefore they had considered Rs. 53,000 as the adjustment (sales day book under cast value which does not have an impact on control accounts).

Part 2.7

Knowledge of preparation of bank reconciliation was tested in this question.

Paying attention to action verbs seemed lacking in answers and some of the candidates had mentioned only examples without giving reasons for difference between bank statement balance and cash book balance. This resulted in loss of marks.

Part 2.8

Knowledge of adjusting and non-adjusting events (LKAS 10) had been tested. Most of the students had not identified the requirement of the question and tried to give more examples rather than explaining the principle. The principle behind identification of adjusting and non-adjusting events was not discussed properly (e.g.: identification of the period, nature of both the events were not correctly written).

Part 2.9

Candidates were expected to identify the criteria to be satisfied, for a provision to be recognized.

This question was well answered by the most of the candidates.

However, some had lost marks due to incomplete writing, improper or wrong wordings and incomplete knowledge on LKASs (e.g.: best estimate instead of reliable estimate/ definite outflow instead of probable outflow/ future obligation instead of present obligation).

Part 2.10

Basic accounting ratios were tested.

Only part (iii) was properly answered. Some of the candidates had written the formula but had considered wrong data for calculations and some of the candidates were unaware of the meaning of the components given in the formula.

Question 03

Optional - 10 marks

The connection between “dual aspect” of accounting and the accounting equation and in part (b) knowledge of Journal entries required for error correction is tested in this question.

In some cases, students’ knowledge on application of figures in a given scenario, into the accounting equation was not satisfactory. As this is fundamental, students should be thorough on it (Part a). In part b, correcting errors using Journal entries some students had used “Suspense Accounts” which is principally wrong.

Question 04

Optional - 10 marks

Knowledge of partnership accounting was tested in this question giving more emphasis on appropriation of profit with guaranteed income accounting while other partners’ agreed to share the shortfall, if any.

Minimum net annual income was not properly understood by most of the candidates. Annual income consists of Profit and Interest on Capital for Vipul. Most of the candidates had only taken the profit component for this adjustment. Further to that, some candidates distributed the difference arising from the income guarantee between the other two partners.

Adjustment required for insurance claim receipt was not properly understood and wrong amended profit was taken to appropriation account.

Some of the candidates had shown drawings in the appropriation account which showed the lack of knowledge in principles.

Interest on loan given by the partners was taken to the appropriation account by some of the candidates.

Fair number of candidates had not given attention to the monthly salary given and considered it as annual salary amount. Some of the candidates had drawn capital accounts and irrelevant entries had been posted, displaying lack of knowledge in principles.

Question 05

Optional - 10 marks

Required to prepare the Income Statement and the Statement of Financial Position for a sole proprietorship.

In most of the cases students' knowledge on clearly identifying assets, liabilities, income & expenditure was not satisfactory. (e.g.: advance paid for furniture was taken as an expense, salary paid by owner's money was not taken as an expense, rent deposit was taken as an expense, other expenses were not accounted in the business's accounts)

Accrual basis in accounting was not followed correctly by some candidates (in computing rent expense).

The correct accounting formats for the Income Statement and the Statement of Financial Position had not been followed by the some candidates (e.g.: incomplete formats, wrong categorisation of items in the Financial Statements).

A few had not properly understood the requirement of the question and provided an Income & Expenditure Account instead of an Income Statement.

Some had not provided workings / descriptions for figures in the Financial Statements, hence lost marks.

Question 06

Optional -10 marks

This is a question about cash flow statement based on indirect method.

Most of the candidates had well answered this question.

In some cases, some of the students had confused the indirect method with the direct method whilst some have taken irrelevant figures. Instances were found where some of the items were recorded under the incorrect category (e.g.: share issue under investing activities and investments under financing activities)

Some instances were found that incorrect adjustments to profit before tax and working capital changes.

Question 07

Preparation of Financial Statements– Compulsory – 20 marks

This question was mainly framed to test the basic knowledge on accounting of deferred taxation, Finance lease and accounting for disposal of revalued building.

Deferred Taxation

The carrying amount of the machine (i.e. Rs. 20,400,000) was not taken as accounting base. The acquisition cost of the machine (i.e. Rs. 25,500,000) was incorrectly taken as accounting base. The adjustment for depreciation incorrectly computed. Hence the tax base (i.e. Rs. 25,500,000x 1/8 * 6 years = Rs. 19,125,000) was not computed or had been incorrectly computed. The temporary difference was incorrectly computed by a large number of candidates. (i.e. incorrect answer Rs. 25,500,000- Rs. 20,400,000 = Rs. 5,100,000 , correct answer Rs. 20,400,000 – Rs. 19,125,000 = Rs. 1,275,000). Most of the candidates had used the corporate tax rate (28%) correctly for deferred taxation.

Finance Lease

Most of the candidates were totally unaware of the accounting treatment for finance lease. The candidates ignored the present value of minimum lease payments (Rs.4,626,000) and had incorrectly taken the higher value of the machine (Rs. 5,000,000) as cost, therefore had incorrectly computed the depreciation for the year. (Incorrect answer Rs. 5,000,000/4 = Rs. 1,250,000, correct answer Rs. 4,626,000/4 = Rs.1, 156, 500). Interest calculation for two years was incorrect too due to the reason of not working out the correct opening balance. The incorrect computation is Rs. 6,000,000- Rs. 2,400,000 x15%= Rs. 540,000. The correct computation is Rs. 4, 626,000 – Rs. 1,200,000= Rs. 3,426,000x15%= Rs. 513, 900 for 2017 and Rs. 3,426,000+Rs.513, 900 – Rs.1, 200,000 = Rs. 2,739,900 x15% =Rs.410,985 for 2018. Due to these errors the lessors balance was incorrectly apportioned to the current and non-current liabilities.

Almost all candidates incorrectly presented the finance lease machine in the statement of financial position as at 31 -12- 2017.

Disposal of revalued property

Most of the answers were incorrect due to computation of depreciation of the revalued building that had been disposed. The number of years after revaluation on 31-12-2015 was only 16.5 years but this was incorrectly taken as 20 years. The disposal profit was incorrect too, due to the above mistake.

Most of the candidates failed to transfer the revaluation surplus from the revaluation reserve to retained earnings after disposal of the building as per LKAS.

Few candidates had simply written the Statement of Financial Position for the year ended instead of mentioning a specific date.

The depreciation of finance lease of the machine was not included in Cost of Sales by a large number of candidates; similar adjustment was repeated in the previous examinations too.

The deferred tax was not added to the provision for taxation by a large number of candidates in the Income Statement.

The net realizable value of the inventory which was higher than its cost was incorrectly taken to cost of sales by few candidates.

KE2 – Management Accounting Information

March 2018

Examiner's comments

Question-wise comments

General comments about submission of workings

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

General comments about candidates' handwriting

There were a number of instances, where the marking examiners found it extremely difficult to read the candidates' handwriting. If the examiner is unable to read what has been written, then no marks can be awarded to the illegible section.

Question 01

Percentage Selection by Candidates Question No.	A	B	C	D	N/A
1.1	67	6	26	1	0
1.2	20	39	31	9	1
1.3	5	5	24	66	0
1.4	15	33	34	18	0
15	16	12	68	4	0
1.6	9	62	12	16	1
1.7	37	38	17	8	0
1.8	31	27	29	13	0
1.9	13	55	25	6	1
1.10	4	45	44	7	0

Correct answer has been squared.

The answer to Question 1.4 was the poorest answer as it showed that many students had not read and understood the question and confused the Gross Profit Margin with the Profit Mark-up.

It was noted that some students had not answered some questions even though these were Multiple Choice Questions.

Question 02

- Q.2.1 Fairly answered by many candidates. However, some had given the correct examples for both Simple Cost units and Composite Cost Units but had failed to explain these terms.
- Q. 2.2 2.3, 2.7 and 2.10 satisfactorily answered by majority of the candidates.
- Q. 2.4 Part (i) has been answered correctly by majority of students but performance on Part (i) and (iii) was very poor.
- Q.2.5 Performance was poor with many candidates scoring low marks on this question. It is evident that these type of questions were not practiced by students.
- Q.2.6 Some candidates had applied the incorrect formulae in their calculations of the monthly installment. Many did not understand that the monthly installment deposit should commenced immediately and therefore, applied the formula incorrectly.
- Q.2.8 Fairly answered by many candidates. However, some had calculated only the profit maximizing sales quantity but not the change to be done to maximize the profit.
- Q.2.9 Inflation adjustment had not been considered by many students but an average number of students had applied the High-low method to develop the Linear Equation.

Question 03

Optional 10 marks

This question has been designed to test the Intended Learning Outcomes (ILO) of Chapter 5 “Accounting for Labour” of ICASL Study Guide.

Some students had not attempted this question and the students who attempted had not performed well. The average marks for this question was 2 -3 marks. Very few no. of students had scored more than 5 marks.

Part (a)

Overtime premium had not been adjusted correctly and therefore, students ended up with incorrect minimum daily payment.

Part (b)

Most of the students had not compared the labour pay with the minimum daily payment computed in Part (a) and many students had proportionated the Production Overhead Expense even though it is a fixed cost.

Part (c)

Many students had correctly calculated the productivity ratio but were very poor in computing the capacity ratio.

Question 04

Optional 10 marks

This Question had been designed to test the Intended Learning Outcomes (ILO) of Chapter 8 “Probability” of ICASL Study Guide.

Although, only 35% -40% students had attempted this question, they had not applied the probability correctly. This shows poor technical knowledge in application of the probability concept.

A large number of students considered only sales probability and failed to apply the joint probability concept which appears that students were not very familiar with the joint probability concept and that their understanding was restricted to simple probability attached in a single dimension.

Many students had not identified the advertising cost of Rs. 6 million as a fixed component of the cost.

Some students had just recommended the advertising campaign because of the positive value in profit after advertising, but in fact the decision should be based on the comparison of profits with advertising and without advertising.

Question 05

Optional 10 marks

This question has been designed to test the Intended Learning Outcomes (ILO) of Chapter 13 “Project Appraisal Fundamentals” of ICASL Study Guide.

Part (a)

Most of the students had not identified the operational cost cash flow since it is varying from the 6th year onwards.

Some students had considered the project period as 10 years and applied the cash flows.

An average no. of students had computed using the IRR method.

Part (b)

Many students did not seem to have the technical knowledge on how to use the IRR factor to compare two projects and their answers reflected that they had good knowledge on NPV to evaluate the two projects.

Part (c)

Most of the students had failed to explain the Payback period technique but had explained the features of the payback period.

Question 06

Optional 10 marks

This question had been designed to test the Intended Learning Outcomes (ILO) of Chapter 17 “Budgetary Control and Budgetary Systems” of ICASL Study Guide.

Part (a) - Many students had performed in this part and scored 3-4 marks out of 7 marks. Few students had mistakenly considered the number of units as 800 for the calculation of flexible budget.

Most of the students had not computed the semi-variables cost correctly in preparing the flexible budget.

Part (b) - Very few students answered satisfactorily on this part. This shows that students do not have a sound theoretical knowledge on the disadvantages of comparing the actual results against the fixed budget for decision making.

Question 07

Compulsory Question 20 marks

This question has been designed to test the Intended Learning Outcomes (ILO) of Chapter 14 “Standard Costing” of ICASL Study Guide for Part (a), (b) and (c) and Chapter 11 “Absorption, Marginal and Activity Based Costing” of ICASL Study Guide for Part (d).

Part (a) Many students answered correctly on this part of the answer, however some students had referred to the accounting standards instead of standards costing.

Part (b) Students performance on this part is poor and some students referred to the accounting standards.

Part (c) Students performance on this part of the question was very poor and they could not produce the answer professionally. They simply mentioned the advantages of the use of technology and didn't provide reasons why the use of standard costing in advanced manufacturing technology environment was not worthwhile.

Part (d) Many students had calculated the FPOH absorption rate and unit cost under the absorption costing method but some students applied the number of units produced in the cost of sales calculation, instead of the number units sold.

Many students had not computed the over absorption correctly under the absorption costing approach. Candidates had mistakenly considered the difference between the number of units sold and the number of units budgeted to sell and ended up with under absorption.

E.g. Under absorption = $(95,000 - 100,000) * 75 = \text{Rs. } 375,000$

Some students had also proportionately applied the FPOH to the cost units sold under the Marginal Costing system.

KE3 (A) – Fundamentals of Taxation

March 2018

Examiner's Comments

Question-wise comments

The paper comprised of three (03) questions.

Question 01

- (a) This is a five (05) part multiple choice question requiring candidates to choose the most correct answer out of the four (04) given options.

The question tested students' knowledge in the undermentioned areas of taxation:

- 1.1 Section 9 (d) - exemption of interest income from income tax.
- 1.2 Section 202 – penalty for failure to furnish a return of income on the due date.
- 1.3 Section 117 – PAYE deduction in respect of a non-executive director whose name is included in the payroll.
- 1.4 Dividend tax payable by a company on distributions out of own profits and out of dividend received from a listed company.
- 1.5 Nation Building Tax (NBT) liability of a manufacturer of chemical products which are partly exported and partly sold in the local market.

- (b) This is a five (05) part short answer question.

The candidates were required to:

- 1.6 List two (02) differences between direct taxes and indirect taxes.
- 1.7 Compute total statutory income, assessable income and taxable income of an individual who has a twelve (12) years old son. Both father and son derive income from rent (section 6 and section 31)
- 1.8 Calculate Value Added Tax (VAT) payable by a company engaged in providing entertainment services whose taxable supply includes exempt supply.
- 1.9 Section 163 – state two (02) instances where on assessment could be issued.
- 1.10 State the due dates for payment of Nation Building Tax (NBT) and the due date for the submission of NBT return in respect of a particular quarter.

General comments

- (a) Overall performance in this (multiple choice) question was excellent. Majority of the candidates scored 60% or more of the allocated marks.

Specific comments

- (a) Common mistakes made by the candidates. Majority of the candidates failed to give correct answer to the undermentioned parts of the question.

Parr 1.3 the failure is due to ignorance of section 117
Part 1.5 the failure is due to ignorance that export of chemical products is not liable to NBT.

- (b) Instances where the requirements from the candidates are not understood.

- (i) Part 1.7 The candidates were required to compute the total statutory income, assessable income and taxable income of Kamal. A few candidates computed Kamal's income tax liability which was not required in the question.
- (ii) Part 1.9 The question required the candidates to state two (02) instances where an assessment could be issued.
Some candidates mentioned instances for opening an income tax file.

Errors of principle/shortcomings in technical knowledge

- (i) Part 1.8 Some computed VAT on the wrong base.
- | | |
|-------------------------------|------------|
| E.g. Taxable <u>supply</u> | xx |
| Less: Input VAT | <u>xx</u> |
| | <u>xxx</u> |
| VAT payable – 15% of | xxx |

- (ii) Part 1.10 – a good number of candidates computed NBT payable on quarterly basis.

Building/planning of the answer

Part 1.7 The question required candidates to compute the total statutory income assessable income and taxable income of Kamal who has a son under 12 years old and both are in receipt of rental income. Kamal also paid interest on housing loan.

Some candidates gave the correct answer but failed to give the buildup of the computation.

E.g. of an answer

Total statutory income	<u>xx</u>
Assessable income	<u>xx</u>
Taxable income	<u>xx</u>

Question 02

This is a mini scenario question. The candidates were required to compute the gross income tax liability and the balance tax payable by a private limited company engaged in providing consultancy services and having an annual turnover less than Rs. 750 million.

The question included:

- (a) Calculation of statutory income from the following sources:-
 - (i) Trade – this included an adjustment to profits.
 - (ii) Interest income – from treasury bills
 - (iii) Dividend – received net
- (b) Qualifying payments relief under section 34.
- (c) Calculation of income tax liability of an undertaking eligible for concessionary rate of income tax under section 59B.
- (d) Tax credits.

Specific comments

Instances where information given in the question was not understood.

- (i) The question states that furniture costing Rs. 850,000 was purchased during year of assessment 2018/2017. It is evident from the information given in the question that this expenditure has not been deducted in arriving at the net profit for the year of assessment 2016/2017. However, some candidates disallowed this cost in arriving at the adjusted profit from trade.
- (ii) Income tax rate – the intention of the examiner was to test candidates' knowledge of section 59B. The business carried on by CS Works (Pvt.) Ltd. satisfies the conditions laid down in 59B for eligibility for concessionary rate of income tax. Majority of the candidates failed to understand this.
- (iii) The information given in the question relates to taxation of a company. However, many candidates claimed tax-free allowance and applied progressive rates of taxation which are appropriate to taxation of an individual.

Errors of principle/shortcomings in technical knowledge

- (i) Business income
 1. Computation of adjusted trade profit – a few candidates computed this commencing with turnover instead of net profit as per accounts.
 2. Economic service charge (ESC) - a few candidates treated this as an allowable expense in the computation of adjusted trade profits. ESC is an advance payment of income tax and can be claimed as a tax credit.
 3. Capital allowance – many candidates applied erroneous rates.
- (ii) Interest income (net) – some candidates mentioned that this does not form part of the assessable income since withholding tax (WHT) has been deducted. In the case of companies such income is not a final withholding payment and WHT can be claimed as a tax credit (in the case of treasury bills as notional tax credit).

- (iii) Qualifying payments relief – many candidates made mistakes in applying the limitations to the claim in respect of donation to an approved charity which provides institutional care for the sick and needy.
- (iv) Taxation – a good number of candidates applied a single rate (28% or 12%) of tax on the taxable income of the company. In the case CS Works (Pvt) Ltd, two rates of tax are applicable as follows:
 1. 12% rate – the profit and income of the business carried on by this company is eligible to this concessionary rate of income tax under section 59B since it satisfies the stipulations mentioned thereon.
 2. 28% on other sources of income.
- (v) Tax computation – some candidates displayed very poor knowledge of taxation of a company.
 - E.g. 1. Claiming tax free allowance
 2. Applying progressive rates of tax
- (vi) Errors of principles – a good number of candidates made the undermentioned errors which are serious in nature.
 1. Deducting qualifying payments relief under section 32.
 2. Deducting tax credits from taxable income.

Mistakes made in the application of concepts/formulae

Qualifying payments relief

The claim for relief in respect of donation on approved charity providing institutional care for the sick and needy is subject to following restriction-

lower of : actual donation

$1/5^{\text{th}}$ of the assessable income and Rs. 500,000

A good number of candidates did not mention all the above conditions when claiming the relief.

Common mistakes made by the students

Taxation

Two rates of tax (12% and 28%) are applicable on the taxable income of CS Works (Pvt.) Ltd.

The profits and income of company are taxable at the concessionary rate of 12% under section 59B while the income from other sources are taxable at 28%. Majority of the candidates either applied erroneous rate of 10% on the profit from business or applied 28% rate on the total taxable income. On a positive note, a majority of the candidates displayed sound knowledge in the construction of the structure, identification of the statutory contents and the presentation of an income tax computation of a company.

Question 03

This is a large scenario question. The candidates were required to compute the gross income tax liability and balance tax payable by a resident individual who is a retired government servant presently employed as the principal of an international school.

The question included:

- (a) Calculation of statutory from the following sources.
 - (i) Employment income – section 4.
 - (ii) Net Annual Value (NAV) of a place of residence section 5.
 - (iii) Business income – this included an adjustment to profit.
- (b) Identification of income exempt from tax and final withholding payments.
- (c) Deductions under section 32.
- (d) Qualifying payments relief under section 34.
- (e) Tax credits

Specific comments

Instances where information given in the question was not understood.

1. The question states that Seneviratne is 61 years of age and receives interest from a Bank in respect of which withholding tax (WHT) has not been deducted. Seneviratne is a senior citizen for the purpose of section 8 (hh) in terms of which such interest income is exempt from income tax. A good number of candidates failed understand this and stated that such interest is liable to tax since withholding tax has not been deducted.
2. Seneviratne owns two (2) houses. He lives in one house and his brother lives in the second house.
3. The intention of the examiner was to test section and section II (1)(a) in terms of which the net annual value (NAV) of one house owned and occupied by the owner or on his behalf, is exempt from income tax. A number of candidates did not understand this and computed the net rent income under section 6 and made erroneous adjustments.

Errors in principles/shortcomings in technical knowledge.

- (i) Employment income
 - Variable benefit – most students mentioned that benefits upto Rs. 50,000 per month is exempt from employment income. Only a few candidates qualified the vehicle benefit accruing to Seneviratne.
 - Pension – a good number of candidates mentioned that the pension received is liable to income tax. Under section 8 (1) (c), such pension income is exempt from income tax.
- (ii) Income from property.

A good number of candidates computed net rent and net annual values of both houses and mentioned that the higher value is exempt.
- (iii) Income from investment
Interest or fixed deposits – a good number of candidates mentioned that this is liable to income tax since WHT has not been deducted.
- (iv) Business income
 1. Adjusted trade profit – a few candidates commenced this with the turnover instead of net profit before tax as per accounts.
 2. Profit on disposal of photocopy machine – many candidates did not know that the profit on disposal of an asset in respect of which capital allowance has been claimed is profit from business.

- (v) Deduction under section 32 – loss brought forward from Y/A 2015/16. Some candidates limited the deduction to 35% of the tax loss brought forward or 35% of the assessable income.
- (vi) Calculation of tax liability. Majority of the candidates made mistakes in the application of the progressive tax rates.
- (vii) Tax credits. Surprisingly, a few candidates did not know that payments/deductions like self-assessment tax, PAYE are advance payment of income tax liability and such candidates deducted such amounts from assessable income or taxable income.

Building/planning of the answer

- (i) Income from property.
In computing the net annual value (NAV) of the houses, some candidates gave only the final figure without showing the buildup as follows:

Rating assessment	xx
Less 25% thereof	<u>xx</u>
Net Annual Value	<u>xx</u>

- (ii) Income tax computation
A few candidates claimed statutory deduction at improper places.

- E.g.
1. Deducting loss b/f from previous Y/A under section 35 as a qualifying payment relief
 2. Deducting tax credits from assessable income or taxable income.

Good side of the answers produced.

1. Majority of the candidates displayed excellent knowledge in the construction of the structure, identification of the statutory contents and presentation of the income tax computation of an individual.

Any other comments to be communicated to the students

1. Read the 'instructions to candidates' given in the question paper before attempting to answer any question.
2. Question 01 (a) – multiple choice questions. Candidates should answer this in the specially formatted answer sheet. It was noticed that a significant number of candidates entered the answers in the normal paper of the answer script.
3. Read each question carefully and understand the information given and requirements clearly before attempting to answer. It may be necessary for the candidates to read the question more than once to ensure the requirements are clearly understood.

This will help you to save valuable exam time by avoiding irrelevant and/or lengthy answers.

Candidates are given 15 minutes extra time to read and plan the answer.

Examples;

Question 01 (b)

Part 1.7 The candidates are required to compute only the statutory, assessable and taxable incomes of Kamal. A few candidates went further and computed the Kamal's tax liability as well.

Part 1.9 The candidates were required to list 2 instances where an assessment could be issued by Piyal, Assistant Commissioner of IRD. Some candidates listed instances for opening an income tax file.

4. Computation of adjusted trade profits. Always commence with 'net profit as per accounts' figure.

Some candidates commenced the computation with the "annual turnover" figure. This method should be avoided as it is cumbersome and very time consuming.

5. Improve your handwriting and communication skills.

An examiner cannot award marks to an answer which he cannot read or understood.

KE3 (B) – Fundamentals of Law

March 2018

Examiner's Comments

Question-wise comments

Question 01

These multiple choice questions are based on areas covered by the study text provided by CA Sri Lanka. Candidates who had prepared well using the study material given in the study text, were expected to have done well.

It was evident that some candidates had not prepared well and displayed lack of knowledge especially on the following topics;

1. Letters of credit (LC)
2. Where the state is liable for the Acts of its agents.
3. Termination of workmen (special provisions) Act no. 45 of 1971 (1.9)

The students' overall performance is very satisfactory. Many candidates had scored 20 out of 20 marks in certain sections except for a few candidates, who mostly scored between 12 - 18 marks.

Question 02

This question is straight from the book. Candidates who studied the study text provided by the CA, would have found it easy to provide the correct answers.

In general, performance has been good. However, the following mistakes, errors and inadequacies were noted.

Some candidates:

1. Did not know matters within the Jurisdiction of the Supreme Court of Sri Lanka.
2. Did not know differences between void and voidable contracts.
3. Failed to do the gratuity calculation.
4. Mistakenly assumed gratuity as terminal benefits which includes EPF and ETF.

Question 03

- (a) A party to a contract may rescind the contract only due to breach of a condition in the contract by the other party.

On the other hand, breach of warranty does not entitle the other party to rescind the contract.

In this question, candidates were required to discuss with reference to a decided case whether Ravi can rescind the contract.

The question tested the knowledge of candidates on the terms of contracts and whether these terms fall under conditions on warranty and the respective legal consequences of breach of such terms.

The candidates who were familiar with relevant case law, particularly “Bettini vs. Gye”, had answered well. Based on this case law, it can be seen that Sarigama’s breach of term was a warranty and not a condition. Condition is a term which goes to the root or foundation of a contracts. Warranty does not go to the root of the contract and breach of such term does not allow repudiation of a contract.

Many candidates had wasted time by repeating what is given in the question.

- (b) When a contract comes to an end due to frustration, the parties to the contract are released from their rights and obligations.

Frustration can occur due to destruction of the subject matter. In this scenario, the concert hall was destroyed due to no fault of parties to the contract.

As the parties were discharged from their rights and obligations, Thompsons was not entitled to claim damages from TPL.

Some candidates had assumed that the ownership of the property had passed to Thompsons and therefore, he cannot claim damages. However, the question did not mention such an ownership transfer.

Many candidates had wasted time by writing the same facts given in the question.

Study text provided by CA adequately covers this area and candidates who had studied the study text could have produced better answers.

Question 04

- (a) According to the given scenario, the contract was to deliver cupboards on Friday and assemble and fit on Saturday to Junaid by Murali.

Here the important aspects tested by the examiner was when the property in the goods was passed to the buyer and legal consequences thereon.

Many candidates had failed to understand that assembling and fitting cupboards was also a part of the contract.

As per the Law, when the seller is bound to do something to put the goods into deliverable state, the property of the goods passes to the buyer only after this act is performed by the seller and the buyer is notified of the same. This relates to passing of property of specific goods in a deliverable state. The pantry units were not in a deliverable state when placed in Junaid's garage. Therefore, the property in the pantry cupboards had not passed to Junaid at the time of those were stolen.

Candidates should study relevant cases with relevant facts. It was noted that some candidates had quoted cases with incorrect facts. Some candidates had understood the question and produced good answers.

Study text covers this subject area. Candidates should read the question carefully, understand what the examiner expects and answer the question. This will enable candidates to produce good answers.

- (b) As per the question, what was expected was to 'explain whether an agency relationship had been created between Amal and Bimal. Accordingly, candidates were expected to touch on the following.

To create an agency by necessity the following conditions must be satisfied.

1. Impossible to get principal's instructions.
2. There must be an actual and definite commercial necessity.
3. The agent must act in good faith in the interest of all parties.

In the given scenario, Bimal had not tried to contact Amal although there was a possibility of contacting him. Therefore, the 1st condition had not been satisfied. Consequently, the hostel bill should be borne by Bimal.

Some candidates had quoted cases with wrong facts. It is necessary to study case law with correct facts.

Only a few candidates had provided good answers.

KE4 – Processes, Assurance and Ethics

March 2018

Examiner's Comments

Question-wise comments

General Comments

This question paper consisted of three sections. Section 1 contained one question with 10 multiple choice questions (MCQs) and one question with 10 short answer questions. Section 2 contained 4 questions carrying 10 marks each. Only three questions are to be answered out of four questions. Section 3 contained one compulsory question carrying 20 marks.

The average performance in this paper was satisfactory. Some candidates wasted time focusing on the minutiae of a point and writing everything they knew about the topic without considering its relevance to the question. This style of writing attracted only one or two marks.

Specific comments

Question 01 (MCQ)

Many candidates had managed to understand the questions and answered them well. The average performance was not that satisfactory in the following questions.

- 1.4 Which is the correct document used in evaluation of the internal controls?
- 1.6 Which is the main business risk in the given scenario?
- 1.7 Select the customers to be considered for evaluation of the credit worthiness.
- 1.8 Which is the most appropriate reason as to why an accountant who deal with money should behave ethically?

The average performance was as follows;

- 1.1 Average 84% answered satisfactorily
- 1.2 Average 80% answered satisfactorily
- 1.3 Average 85% answered satisfactorily
- 1.4 Average 75% answered satisfactorily
- 1.5 Average 95% answered satisfactorily
- 1.6 Average 60% answered satisfactorily

- 1.7 Average 60% answered satisfactorily
- 1.8 Average 60% answered satisfactorily
- 1.9 Average 75% answered satisfactorily
- 1.10 Average 90% answered satisfactorily

Question 02

Some candidates have produced descriptive answers without considering the action verbs of the question as guidance on the requirement. Some of these answers were neither relevant nor required.

- 2.1 The question required candidates to list the common environmental factors relating to a business organization. Majority of the candidates had failed to produce satisfactory answers to this part as they had misunderstood the question's requirement. The mistake was candidates started writing everything they knew about the topic without reading and comprehending the question properly resulting in irrelevant answers being produced. Most of them wrote the external risks in the business environment such as PEST, whereas the question required listing of the environmental and ecological factors relating to a business organization. Some candidates had written completely irrelevant answers such as GDP, inflation, population growth and customers.
- 2.2 Students were required to explain why the risks faced by the businesses should be managed and kept within acceptable limits. Some candidates reproduced the question in the answer paper without explaining reasons for managing risks. Many had failed to provide satisfactory answers again resulting from a failure to understand the question requirement. Candidates should have explained in brief what the business risks were and state why those should be managed, but many had failed to do so.
- 2.3 It was required to explain the term segregation of duties with an example from petty cash payments. Most of the candidates did not appear to have read and comprehended the question and came to a hasty conclusion that the question was on petty cash payments. They had written lengthy descriptive answers on the process of petty cash payments. Most of the answers reflected poor knowledge on segregation of duties, although they knew two tasks should not be done by one person, but were unable to explain the principle behind that. Some candidates were of the view that separating petty cash payments from the main cashier resulted in a segregation of duties
- 2.4 It was required to state inherent limitations in operating effectiveness affecting the internal control system. Some of the candidates had ignored the part of the question which specified inherent limitations in operating effectiveness and referred to it as poor design of controls and further mentioned that employees were unaware of the controls, cost effectiveness, controls are ignored in practice, failure to achieve the objective, etc., which are the inherent limitation of internal controls and not operating effectiveness of controls.
- 2.5 The candidates were required to identify the given document in the procurement process. Many candidates had failed to identify the document correctly. Some were not aware of the difference between the purchase requisition and the material requisition. Most of the candidates had identified the document incorrectly as a purchase order and explained the purpose of a purchase order and as a result they did not earn any marks for this part. This reflects the poor knowledge of candidates in procurement process.

- 2.6 Students were required to state the business risks associated with the property, plant and equipment management process of an organization. Most of the candidates had produced satisfactory answers and obtained full marks.
- 2.7 Candidates were required to state the purpose of the given documents in the sales process. Many candidates had answered well with regard to the delivery note and the sales invoice. Although, a majority of the candidates were unable to state the purpose of the sales order. There were a number of candidates who had displayed poor knowledge on sales invoice being a prime document in the sales process.
- 2.8 This question was on general and application controls in an IT system. It was disappointing to note that many were unable to explain the importance of IT controls. The only common answer was that IT general controls support effective functioning through access security. Some had given general answers stating that IT controls help to provide accurate data without specifying general or application controls. The candidates should provide specific answers, as only application controls and not the general controls, help to provide accurate data.
- 2.9 Most of the candidates have answered this part of the question satisfactorily. There were some candidates who produced a common answer for ethics and morality ignoring the two different meanings.
- 2.10 It was required to explain the reasons why compliance with SLAuS is necessary in conducting an audit. It was observed that some who lacked the technical knowledge wrote that compliance with SLAuS is required by law. The average performance of this part was good.

Question 03.

This question is based on the study text. It was observed that the candidates who were well prepared and studied the text book had written satisfactory answers and earned full marks.

Part (a)

Students were required to identify the most appropriate type of risk faced by the company with reference to the issues given in the scenario. This question was expected to test the theoretical knowledge of the candidates. Some candidates had listed out all possible risks such as strategic, operational, market risk, etc. without identifying the specific risk to the given issues. Many candidates had wasted time in writing lengthy answers explaining the concepts of internal and external risks.

Part (b)

Candidates were required to identify the risk response method adopted in the given issues. The performance of this part of the question was not satisfactory. Many candidates had written risk identification, risk analysis and risk management as steps to mitigate risks. Some have correctly understood the question requirement but were unable to link the correct risk response to the given issues. Some candidates have written alternative responses to the given points in the question, such as recruit new qualified staff in order to reduce risks, change the delivery staff to overcome thefts, etc. Some candidates had written completely irrelevant answers such as, evaluation, measurement, compliance, etc.

Question 04

Part (a)

It was expected to discuss the control deficiencies in respect of the bank reconciliation activity in the given scenario. The performance of this part of the question was not satisfactory. In order to answer the question, the candidates should have known the controls expected from performing a bank reconciliation, which is to ensure that all receipts and payments to and from bank account are properly accounted for and accounting records are correct. The answer should be based on the control procedures to be in place, and the reason for the expected controls to be ineffective.

As students lacked the knowledge in controls, they failed to identify the control deficiency in the given scenario. Some who knew segregation of duties is one of the internal controls stated that not having segregation of duties as a control weakness but this was not relevant to the given issue. Some candidates had written not maintaining separate bank accounts as a control deficiency which was not relevant to the question as well. Majority of the candidates had written that as the staff were not competent they could not prepare the bank reconciliation; the deficiency being the bank reconciliation was neither prepared nor reviewed. Many candidates have written the issues in the scenario without linking them to the required controls. It was observed that some candidates who had not understood the term 'reconciling items', wasted time in explaining how to prepare the bank reconciliation.

Part (b)

- (i) Students were required to discuss the ethical behavior faced by the finance manager in the given scenario. This part of the question was answered satisfactorily. Some candidates had obtained fewer marks as they identified the incorrect threat and some candidates who had identified the correct threat were unable to explain how such a threat arises.
- (ii) Candidates were required to state two fundamental principles of professional ethics for accountants. Some candidates had ignored the question requirement and listed all principles of professional ethics and wasted time in explaining such principles. Further, it was observed that some candidates had not understood the question requirement and produced irrelevant points such as independence, compliance with SLAuS, etc.

Question 05

As this question is one of the optional questions only about 60% of the candidates had attempted this question.

Part (a)

It was required to explain the given elements in relation to an independent auditor's report of an external audit.

Three party relationships - Majority of the candidates obtained full marks. It was observed that candidates were not aware of the difference between stakeholders and shareholders. Some candidates who had not understood the question wrote general answers such as third party which doesn't represent any party.

Subject matter - Some candidates had produced relevant answers, but some had written the definition of the subject matter. Some had wasted time in explaining that the subject matter should be identifiable and collectable. Most of them knew what the subject matter was but were unable to explain it in relation to an external audit. The examiner expected the candidates to identify the subject matter in an independent auditor's report of an external audit since the subject matter is the financial statements.

Part (b)

Candidates were required to explain three Es of a VFM audit. Many candidates had written in point form, ignoring the action verbs and as result obtained less marks. There were some irrelevant answers such as electronic banking, E-money and Ecommerce. Some candidates who had not understood the question or who did not have the subject knowledge had referred to audit and written enquire, examine, evaluate, evidence, existence, etc.

Question 06

As this is an optional question only a few candidates had attempted this question.

Part (a)

It was required to state the appropriate audit evidence for the given factors. Some candidates obtained full marks for this part. The candidates were expected to know what is appropriate to enable the practitioner to make his professional judgment on the subject matter. Some candidates, who had not understood the information given in the scenario, had written audit procedures such as checking assets register, checking the accounting entries, etc. Some candidates demonstrating lack of subject knowledge, stated 'to check the relevant documents'. Even though some candidates have written descriptive answers, explaining the documents required to use as audit evidence, they were not able to specify the most appropriate documents.

Part (b)

In this part of the question, it was expected to explain the difference between tests of control and the substantive audit procedures. And was further, expected to test the knowledge of the candidates in concepts. Some candidates had produced relevant answers. There were some candidates who have written the definition of the two concepts without identifying the difference between two tests.

Question 07

This question was on control procedure in sales process and cash process. The overall performance in this question was average. The candidates demonstrated poor technical knowledge and lack of planning in answering the questions. Some candidates had ignored the action verbs and wasted time in producing descriptive answers when asked to identify. The question requirement was to identify two control weaknesses, but candidates produced three or four weaknesses thereby wasting their time.

As the risks and controls are key elements in the syllabus, the candidates should be thorough with such areas in applying to any business process. Some candidates who planned the answer for part (a), (b) and (c) had answered the three parts in a tabular form and produced the answer satisfactorily.

In part (a) of the question, the examiner expected the candidates to identify the control weaknesses in the sales process of Speed Travel (Pvt.) Ltd. Candidates should have identified the controls to be in place for the sales management process of Speed Travel to reduce risks in business process before answering this part of the question. There should be efficient and effective operation, reliable financial reporting and compliance with laws and regulations in a sound control system. The significance of the control weakness depends on the possible consequence of the risk event happening, that should have been prevented by introducing adequate control measures. Candidates could have easily planned the answer by reading the scenario and identifying the activities in the sales management process, such as customer evaluation, order acceptance, invoicing and delivery of service.

Some candidates had referred to the scenario and identified the risk event but failed to link that with the control weakness such as;

- Marketing assistant adjusts package rates – authority not mentioned
- Invoices are prepared based on customer agreed rates - not mentioned about the approval
- Sales invoices are on a word document - not mentioned that invoices are not serially pre-numbered
- Routes are changed at the request of customer - not mentioned about the authority and additional charge for extra miles

Many candidates had tried to explain the weakness in the manual system, ignoring the fact that controls are more or less similar in the both manual and computerized system. Some candidates had identified serving corporate customers as a control weakness.

Part (b)

In this part candidates were required to state the risks arising from each control weakness identified. The first requirement is to identify risks which cause losses and even threaten the future of the business. Some candidates had stated relevant risks such as frauds and errors, under invoicing, etc. Majority of the candidates misunderstood the question requirement and wrote events in the sales process such as;

- Providing services to corporate customers
- Using emails for quotations as risks
- Difficulty in collecting cash as invoices are sent at the end of the tour
- Adjusting package rates will result in loss of goodwill of the company and the demand for tour packages.

Some candidates had stated the risks in the given scenario as operational risks resulting from failure in internal processes but were unable to collaborate that with the major issues in the scenario. Some candidates who had recognized the relevant risk and collaborated with the incorrect issue in the scenario, wrote that since they maintain a manual system there can be frauds. There were some scripts listing out the risks such as strategic, operational, financial, compliance which were not related to the issue.

Part (c)

In this part, it was expected to identify control measures to be established to address the identified weaknesses. It was expected to test the knowledge of the internal controls of the candidates. There were only a few scripts which carried satisfactory answers. Most of the candidates wrote that the;

- Sales system should be computerized.
- The invoices should be in printed forms or in an excel sheet.

Some candidates had written following without linking to the event and the risk.

- Fix the rates
- Allocate a representative to each tour

Part (d)

In this part of the question the candidates were required to identify the lapses in the cash process of the given scenario. It was expected to test the knowledge in cash process such as collection of cash, safe keeping deposit with the bank, updating the cash book, etc. If the candidates had listed the events given in the scenario, they could have easily identified the lapses. As per the given information, it was implied that the scenario referred to a centralized cash process. As per the scenario;

- Cash collection of the branch is deposited in the bank once in three days. This information implies that there is an issue with the security of cash.
- Sales summary together with copies of invoices are sent to head office, and they are filed. As per this information it reflects that there is an issue with the accuracy of recorded receipts.
- The cash book and the sales ledger are updated based on the collection summary. This reflected that there was an issue with regard to accounting.
- They considered buying safes vaults for branches. It reflected that there was an issue with the security of cash.

Most of the candidates had failed to identify the lapses in the cash process requirement. Majority of the candidates have identified the deposit of some collections recorded in the cash book that were not realized for more than three days, but were unable to link that to the process where the lapse was that the deposit slips were not checked with the collection summary. Some candidates had looked at the issues in a business approach and discussed the cost effectiveness of buying safes and transporting cash which was not the question's requirement.

There were some candidates who identified the lapses but presented the answer as control tests such as check collection summary with the sales invoices, check deposit slips with the collection summary. They had referred to the scenario and written steps to overcome the risk which was not the question's requirement. Some of those steps written are as shown below;

- Bank daily without keeping cash in the drawer,
- Update the cash book with the deposit slips and check with the collection summary.

Conclusion

It is clear that many candidates had not prepared properly for the exam and failed to learn the topics in sufficient depth. As the question paper was within the syllabus, they could have easily earned the required marks if they had read the study text. It was disappointing to note that some candidates who have the subject knowledge were unable to produce the relevant answer as they were unable to comprehend the question and plan the answer accordingly. The common mistakes reflected by unsuccessful candidates, were that they did not attempt to comprehend the question requirement and manage the time. They could have overcome these weaknesses if they had done few past papers.

KE5 – Commercial Insight for Management

March 2018

Examiner's Comments

Question-wise Comments

Question 01

General comments

Overall performance of the candidates was good for this Multiple Choice Questions (MCQ) which carried 20 marks. The MCQs were based on characteristics of a service, measure of efficiencies, top management skills, calculation basis for GNP, environmental dynamism, effectiveness of advertising expenditure, accountability, law of marginal returns, minimum efficient scale and analytical models for unstructured decision making.

Specific comments

Most of the students could not choose the correct answer for Q. no. 1.5 & 1.9. A fair number of students had selected the correct answer for example 1.2, 1.3 & 1.4.

Question 02

General comments

Overall performance of the candidates was good. This question carried 30 marks and required candidates;

- 2.1 To explain the terms 'Vision' and 'Mission'.
- 2.2 To explain allocative efficiency in a perfect competition using a diagram.
- 2.3 To explain social and demographic trends to be used for making business decisions.
- 2.4 To explain two factors that need to be considered to outsource a particular service.
- 2.5 To state advantages of having a matrix Organizational structure.
- 2.6 To explain the difference between the terms 'power' and 'authority'.
- 2.7 To state 3 activities involved in tactical control.
- 2.8 To state 3 characteristics of end products produced under continuous flow production method.

- 2.9 To explain 2 examples of external economies of scale.
- 2.10 To explain the difference between marketing orientation and production orientation.

Specific comments

- 2.1 'Overall aspiration for the future representing Origination's strategic intent' is the vision for some students who earned allocated marks. Some correctly explained that 'mission' expresses basic functions of an Organization in terms of products and services it produces for its clients. Some incorrectly identified vision as 'future objectives' of an Organization. Some viewed 'mission' as an explanation to the vision statement. According to some, the mission includes 'strategies'.
- 2.2 Allocative efficiency is achieved under perfect competition in the long run when $MC=price$ and where resources are allocated in an optimal way, i.e. most cost effective way. Most of the students, could not provide this answer. Some had correctly drawn the diagram but could not clearly indicate the main condition under which allocative efficiency operates, i.e. $MC=price$.
- 2.3 Changing age structure of the labour force, will have an impact on the businesses. Income and wealth and buying pattern of customers also make an impact on the business. Goods and services could be marketed to people at specific stages of age, wealth & income. Some just cited without explaining environmental factors and trends like environmental and climate changes, level of education etc. as factors that businesses need to be aware of when making decisions.
- 2.4 Both direct cost and indirect cost of outsourcing, period of requirement of outsourcing, degree of specific business knowledge about the service subject to be outsourced, etc. are some factors that need to be considered when deciding to outsource, as per some students who earned the allocated marks. Almost all mentioned that cost of outsourcing needs to be considered. Some had given lengthy explanations on the possibility of impact on goodwill when services are outsourced which earned only a few marks.
- 2.5 Some had correctly stated that greater flexibility of workflow and decision making, enhancement of inter-disciplinary co-operation, motivation and employee development as advantages of having a matrix Organizational structure. Some incorrectly stated that matrix organizations will help in identifying human resources of the organization and delegation of authority, etc. Some stated that the matrix structure will help to exercise better supervision which earned no marks.
- 2.6 A few candidates held a wrong view on 'power' and 'authority'. According to them, 'Authority' related to the Board of Directors and 'Power' is the persons who hold responsibilities. Power is the ability to get work done and authority is the right to take certain decisions within certain boundaries, according to some candidates who earned full marks.
- 2.7 Tactical planning, Budgeting, Development and implementation of procedures and monitoring are some activities involved in tactical control. Nevertheless, some wrongly stated financial control, cost control, stock control, etc. as activities involved in tactical control, while some others stated promoting employees, making decisions, etc. as activities under reference.

- 2.8 Characteristics of the end products produced under the continuous flow production are produced in high volume and standardized where the range of products are not diverse. But some stated that cost of production is minimal and production is made on orders received for which marks were not awarded.
- 2.9 Since specialized support services like external educational services, transport service, provision of components, etc. are created due to large scale production, external economies of scale will accrue to large scale producers. Some incorrectly explained that due to the use of large scale machinery, benefits could be accrued. Some just stated 'advertising', 'news papers' without being explaining how they help in earning external economies of scale.
- 2.10 Under Marketing Orientation, organizations need to interpret customer needs and produce products and services that meet customer requirements. Production orientation means producing goods and services at optimum quality and at minimum cost where the customer needs and wants are not given due consideration. Some did not have a clear understanding over the difference of that in comparison to production orientation, where organizations make available goods and services abundantly for customer satisfaction. Some just stated production orientation is based on production and market orientation is based on customers without providing an explanation.

Question 03

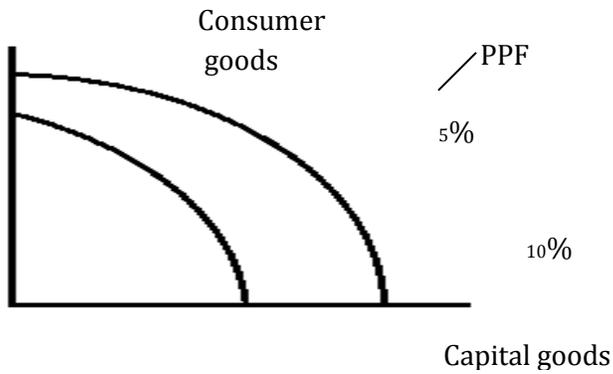
General comments

Overall performance of the candidates was good. The question carried 10 marks and required candidates to;

- (a) State four factors of production and factor payments associated with each factor.
- (b) Explain effects on quantity demanded of inferior goods and luxury goods as a result of a change in household income.
- (c) Explain the impact on the Production Possibility Frontier (PPF), if higher technological improvement in the production of capital goods than that in the production of consumer goods (ii) in an economic recession.

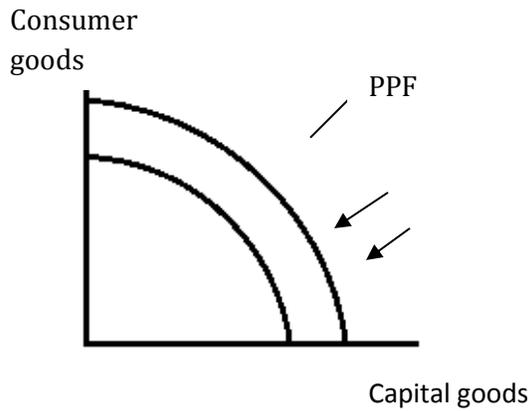
Specific comments

- (a) Most of the students stated Land, Labour, Capital and Entrepreneurship as factors of production and rent, wages, interest and profit respectively as factor -payment. A few made mistakes like machinery as factor payment for capital and equity as factor payment for Entrepreneurship.
- (b) Income elasticity of inferior goods is negative and Income elasticity of luxurious goods is positive. Most of the students had correctly identified the relationships between income and demand for inferior goods and luxury goods. Some could not adequately explain as to why the demand of inferior goods falls when income increases i.e. Households will start moving towards quality goods. A few stated that Income Elasticity (IE) of inferior goods is positive and IE of luxury goods is negative which earned no marks.
- (c) (i) When technology is improved in production of capital goods than that of consumer goods, (e.g. 5%) more capital goods (e.g. 10% increase) could be produced with the given resources. As a result, Production Possibility Frontier (PPF) will shift to the right and will appear as given below.

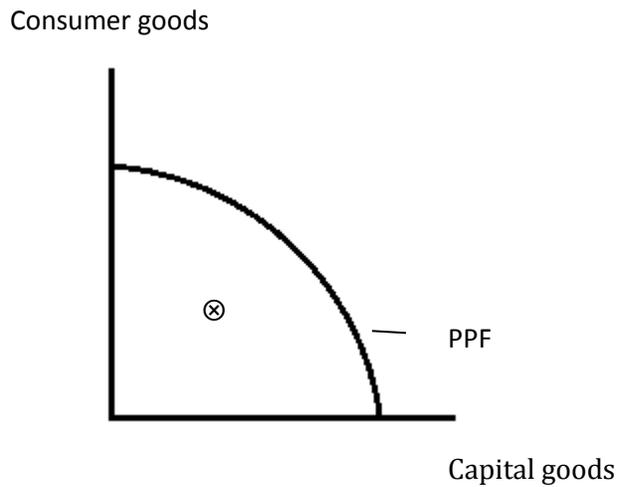


Some candidates were wrongly inclined to the view that capital goods could be produced more due to technological advancement but at a higher cost.

- (c) (ii) Economic recession results in reduction of production capabilities and therefore PPF curve will shift inwards as shown below.



Some have marked an inefficient production point as given below to show the outcome of a recession for which marks were not awarded.



Question 04

General comments

Most of the candidates scored less than 5, i.e. less than 50% for this 10 mark question. Candidates were required to;

- (a) List 3 characteristics of an oligopoly
- (b) Explain kinked demand curve
- (c) State 3 factors that determine the success of a price cartel

Specific comments

- (a) Some correctly listed characteristics of oligopoly as A few large firms, barriers to entry, homogenous products or differentiated products, Firms' production decisions are inter-dependent and both price and non-price competition. Some identified an oligopoly firm as a price taker for which no marks were allocated. Some identified the players in the oligopoly market as 'suppliers' rather than 'firms'.
- (b) Some have drawn kinked demand curve ($D=AR$) highlighting elastic and Inelastic portions. Most of the students were unable to answer this part correctly whilst some had drawn the (equilibrium) graph meant for a Monopolist.
- (c) Some incorrectly mentioned that success will depend on the number of items produced, cost incurred, etc. A few stated correctly that success of a cartel depends on whether all or most of the producers are included in the cartel and whether there are no close substitutes for the product. Also, price elasticity of demand has to be inelastic, for a cartel to be successful.

Question 05

General comments

Average performance of the candidates was poor. This question carried 10 marks and required candidates to;

- (a) State 4 reasons for reduction in consumer spending due to a rise in interest rates.
- (b) Explain 3 actions an international trading that a Company can take to reduce the risk of suffering losses on foreign exchange transactions.

Specific comments

- (a) A rise in interest rates will result in lesser borrowing, lesser consumption, higher savings and depress the value of non-monetary assets. Some had just mentioned that consumer income will come down as a result of rise in the interest rates. They should have mentioned that a rise in interest rates leaves less income for consumers.
- (c) Action taken to mitigate risks of suffering losses include, inter alia, buying currencies forward, dealing with strong currencies, using derivatives, etc. Some explained incorrectly that the two countries concerned could negotiate for fixed exchange rate to mitigate the exchange losses, whereas some others were of the view of discouraging imports and encouraging exports so that exchange losses could be reduced, for which no marks were awarded.

Question 06

General comments

Performance of the candidates was at acceptable level. The question carried 10 marks and required candidates to;

- (a) State 4 objectives of having a performance appraisal for employees
- (b) Identify 4 benefits the organization would achieve by providing training & development to employees
- (c) State 2 methods of on-the-job training

Specific comments

- (a) According to some students, objectives of Performance Appraisal (PA) included, comparing the individual's level of performance against a standard, identifying the individual's training needs, identifying the areas that needed improvements, etc. for which full marks were given. Some repeated the question i.e. performance appraisal is done to appraise the employees performance. Some have come up with remotely related objectives of PA. E.g. PA is done to motivate employees and to increase productivity.
- (b) Some have correctly identified that employee-training would pave the way for lowering cost, increasing productivity, minimizing accidents, creating healthy and safety environment, motivating employees, helping change management, etc. A few identified training employees will enhance the firm's goodwill and attract customers which was not directly related to the question.
- (c) Job rotation, temporary promotion, providing coaching & instructions, etc. are some methods of training. A few students incorrectly stated that 'probation period' is a training method.

Question 07

General comments

Performance of the candidates was good. The question carried 20 marks and required candidates, as per the given scenario, to;

- (a) Calculate market equilibrium price and quantity
- (b) Calculate the point price elasticity of demand
- (c)
 - (i) Explain the impact of increase in demand for laborers on the market for tea
 - (ii) Explain the impact of compromising the quality on the tea market
 - (iii) Explain the impact of price setting for USD 400 per Kg by the govt. on the tea market.
- (d) Explain the impact of establishing minimum daily wage for teapluckers on the labour market.
- (e) Explain the effect on total revenue of Highland Tea, if it charges a higher price for its products.
- (f) Discuss 3 key factors that the Company should look at, when undertaking a competitor analysis.

Specific comments

- (a) Almost all arrived at equilibrium price and quantity correctly as USD 100 and 200 MT, respectively. A few got incorrect answers due to calculation errors/application errors.
- (b) Only a few arrived at the point elasticity correctly. Some had cited correctly the formula but ended up with a wrong answer due to calculation errors whereas some seemed to have lack of knowledge on slope of the demand curve which was required to calculate the elasticity.
- (c) (i) Increase in demand for labour will increase the wages, cost of production. As a result, tea price would rise and quantity will fall. Some have drawn the diagram to show this outcome by correctly shifting the supply curve to the left. A few had totally misunderstood the question and concluded by shifting the demand curve to the right. Some explained the consequences correctly but could not draw the graph as expected by the examiner.
- (ii) When the government sets a price of USD 400, suppliers will be willing to supply at the higher price which is above the equilibrium market price. Some had explained this impact correctly but had not drawn the diagram to reflect the correct explanation, whereas some had drawn the diagram correctly but not explained it adequately. Some students could not arrive at the excess supply of 450 MT.
- (d) The establishment of minimum wages which is above the equilibrium market rate will help workers to be paid more. Possibility of lesser demand for labour cannot be ruled out. A fair number of candidates have drawn the diagram correctly but not described this in an acceptable manner. Only a few described the possibility of less demand for labour and some manufacturers may not be able to afford the pay hike. Some mentioned that due to increase of wages tea market will improve and the production possibility curve will shift to the right for which marks were not awarded.
- (e) If a higher price is charged, customers will shift to the other brands since the market is monopolistic competitive and as a result demand and income for Highland tea will be lower. Some have explained the effect as lower income for Highland Ltd. citing the elastic demand prevalent for Highland tea. But some were not sure whether demand for Highland tea was elastic or inelastic. Some explained that the income for Highland Company will rise since the demand for tea is inelastic.
- (f) Competitor's goals, assumption, current situations and strategies and competitor's capabilities are among others that need to be considered when competitor analysis is carried out. Some stated competitor's product and price need to be considered when the competitor analysis is made, which was not adequate.