



# Examiner's report

## P1 Professional Accountant

December 2009

### General Comments

December 2009 was the fifth P1 paper and I am happy to report another successful diet for the many candidates that passed. I would like to congratulate the successful candidates and their tutors and it is good to be able to recognise the hard work that many candidates put into their studies. As always, however, many candidates were unsuccessful and I hope that the following remarks will be helpful in explaining where they may have gone wrong.

Paper P1 contains four questions in two sections. Section A was compulsory and contained one extended question (Question 1) worth 50 marks. As in previous diets, Question 1 was a multi-part requirement covering a wide range of outcomes from the study guide. Section B contained three questions worth 25 marks and candidates were required to select two from those three. The section B questions tended to be located within one area of the study guide but, as in previous papers, also contained supporting requirements from other areas. All questions (in sections A and B) were based on case scenarios and marks were often awarded for application to the case material.

### Specific Comments

#### Question One

As in previous diets, the compulsory question was based on an extended case. In the December 2009 exam, the case concerned the sinking of a ship (the Mary Jane) and its owner, Sea Ships Company. The central event of the case was the loss of a ship, the Mary Jane, in a storm but the case explains that the ship sank because of a series of internal control failures both on board the ship itself whilst the company's future was threatened because of other internal control failures at the Sea Ships head office. Because of the loss of life on the Mary Jane, the government held an inquiry which identified and highlighted a range of failures leading to the loss. It was a scenario, drawn from a range of real maritime disasters, which shows the importance of risk management and internal controls in business operations. Lives can and do depend upon them and internal control failures can result in the loss of lives and threaten the viability of companies.

As in some earlier P1 exams, Question 1 contained an ethical reasoning task, this time using the 7-step American Accounting Association model (in Q1a). The company had evidence from an independent consultant that a range of structural changes to the Mary Jane would have prevented it from sinking but that the changes had not been carried out due to cost constraints. The task in Q1(a) was to use the AAA model to consider the ethical dilemma of whether or not to publicly disclose the fact that the report had been received but not acted upon. All of the information needed to conduct the analysis was in the case scenario. Candidates that could only recall some of the 7 steps did receive some recognition but it was disappointing to see some candidates reproduce the seven steps but then to either ignore or misinterpret the ethical dilemma. A careful reading of the question should have indicated exactly what the requirement was to consider 'whether or not to disclose this information [about the independent consultant's report on structural changes] publicly' but some failed to recognise that this was the dilemma to be considered and thereby did not achieve high marks for this part.

Part (b) was an 'identify and analyse' task where candidates had to study the case and draw out the internal control failure both at Sea Ships Company and on the Mary Jane itself. This required a careful reading of the case but the internal control failures were relatively clear to many candidates. Some candidates missed out on some of the internal control failures at the Sea Ships Company itself (such as the failure to ensure adequate insurance cover). This type of question, involving a careful analysis of case material to draw out relevant content, is one that tests both understanding (being able to identify the internal control failures) and analysis (being able to say why the identified issues are important IC failures and their implications) is a useful way to test candidates on a

range of topics on the P1 study guide. A similar approach was taken, using different verbs, in this paper in Q2(c) and Q3 (b). It is not possible to perform well on these questions without a careful scrutiny of the case scenario.

Part (c) asked how non-executive directors (NEDs) might have helped in improving the governance at Sea Ships Company. The issues highlighted by the government inquiry were useful starting points for this question. I was disappointed that many candidates automatically wrote about the four general roles of NEDs in this question as though this were an automatic response to all NED questions! Candidates that based their answers on the unique governance situation at Sea Ships were rewarded whilst those that reproduced an auto-response ('strategy, scrutiny, risk and people') tended to achieve few or no marks on this question. Again, it was important to analyse the case and read the question carefully. The question was not asking about the roles of NEDs but rather the contribution they (rather than executive directors) could make given the governance failures at Sea Ships Company.

Part (d) contained two requirements which were linked and were required to be answered within the same 'flow' of narrative. As in previous P1 papers, four professional marks were available for the correct presentation of the answer. These two requirements (part (b) i and ii) were poorly done overall with some candidates refusing to attempt them at all. Both areas asked about were well covered in the study texts so I was surprised and disappointed that some candidates did so poorly. Again, in both cases, I suspect that a reason for poor performance was an inadequate reading of what the question was actually asking for.

Part (d)(i) asked candidates to assess the importance of information on controls and risks. The range of answers I saw on this suggested that some candidates misinterpreted its meaning. The key words in the question were 'importance of information' or, in other words, why does the board of Sea Ships need information on controls and risks? The importance of information is covered in the P1 study guide section B4a but this subject is also covered in other ACCA papers so candidates should have been aware of this area.

Part (d)(ii) was also done poorly overall but was also relatively straightforward in what it was asking. Following on from the importance of information, this part asked about the nature of the information itself. A good answer explained that good information was reliable, relevant, understandable and complete although markers accepted other relevant qualitative characteristics as equally valid. The six marks in Q1(d)(ii) should have been relatively straightforward to achieve so it was disappointing that many candidates failed to see what the question was asking them to write about. Again, I would reiterate and emphasise the point that a careful reading of each question is crucial.

One of the most disappointing things to report on Question 1 was the poor attempts to gain the professional marks in Q1(d). I have highlighted this as an issue in past exam reports and there was a useful article on professional marks for P1 in a recent edition of Student Accountant. The question required the answers to Q1(d) (i) and (ii) to be in the form of a memo. This was worth 4 marks and it was disappointing that so few managed to gain high professional marks. I have made the point before that the various forms of narrative communication should be taught to and learned by P1 candidates and I repeat this point in this report. It was evident that many candidates were unsure of how to frame and draft a memo to management and this was reflected in the professional marks awarded. A common error was to write the answer in the form of a letter.

## **Question Two**

The question was set in the context of a newly appointed director at Ding Company. Drawing on themes in the core of the corporate governance sections of the P1 study guide, this question examined director's induction,

unitary vs. two tier boards and the roles of a non executive chairman. It was necessary to study the case in detail in order to gain high marks on the three requirements.

Part (a) had two tasks: to explain the content of a director's induction programme and to assess the advantages of an induction programme for Sam Mesentery, the new director who was the subject of the case. In most cases, the first task was done better than the second. The marks for 'explain the content' were mainly bookwork but it was necessary to study the problems with Sam Mesentery to gain the 'assess the advantages' marks. Again, I would remind candidates that they must be prepared to closely examine the text of case scenarios as answers often require the placing of case evidence into a theoretical context.

Parts (b) and (c) were less well done overall than part (a). Both required level 3 intellectual levels and a very careful analysis of the case. Candidates who did not answer at that level did not achieve a high score on this task. Part (b) required a knowledge of unitary and two-tier boards in order to critically evaluate Annette Hora's belief. She believed that companies in turbulent environments, i.e. in which environmental factors are highly changeable, should have two-tier boards. The task in part (b) was to provide arguments for and against this belief. This, then, was not just about the pros and cons of one type of board structure over another, but rather about their suitability in different environmental conditions, therefore this was an application question. Candidates had to take what they knew about unitary and two tier boards and apply that knowledge to something they may not have considered before – how different environments might favour different types of board.

There was evidence of candidates not adequately reading the question in part (c). In the case, the non-exec company chairman, Arif Zaman, made a number of remarks about his job. The task was to assess his (Arif's) understanding of his role based on the remarks he had made. It was necessary to know what the roles of a non-executive chairman are in order to compare Arif's views with those roles. The question was not asking what the roles of a non-executive chairman are. The most common error in answering this question was listing the roles of the chairman and failing to analyse what Arif had actually said.

### **Question Three**

This was a question about an irregular transfer of company funds for private use which gave rise to an ethical dilemma for John Wang, the training manager of the company's auditor. It raised issues of professional relationships, the role of auditors, and personal loyalties and friendships. The transfer of \$100,000 for a security system of a company manager's holiday home was highly irregular and the behaviour of Potto Sinter, the engagement partner was wrong in several respects.

Part (a) should have been relatively straightforward. It asked for an explanation of 'integrity' and then an explanation of its importance in professional relationships. In context, this referred to the professional relationships between the actors in the scenario although explanations concerning other professional relationships were also rewarded by markers. Most candidates that attempted this question were able to define integrity but fewer were able to apply that knowledge to the case. Accordingly, some did not gain the marks for applying integrity to professional relationships.

Parts (b) and (c) were less well done overall. Both employed level three verbs and required a careful analysis of the case. In part (b), candidates were invited to criticise Potto Sinter's ethical and professional behaviour. There were, in fact, five clear ethical and professional 'issues' in the case attributed to Mr Sinter and it should have been straightforward for candidates to pick these out. When I use 'criticise' in a P1 question, such as in Q3(b), the challenge is to carefully scrutinise the case, identify the behaviour which is wrong or inappropriate, and to

discuss why the behaviour is wrong. Of course in order to do this, it is necessary to know what right and wrong behaviour is, hence the need to understand before the application of knowledge can be made. In this case, it should have been straightforward to identify Mr Sinter's shortcomings. This question was not done well overall, perhaps because candidates felt too time-pressured to spend time reading the case in detail and yet this was necessary to answer the question correctly. Where case analysis is essential for gaining marks, it is better to invest time studying the case to the required level rather than writing a long but unfocussed answer that fails to address the question.

The same point can be made in respect of part (c). It was necessary to know what John Wang's alternatives were before they can be evaluated. A dilemma, by definition, is a choice between two options (in the same way that a trilemma would have three choices) so there were two main options to be considered. In recognising that some other options were theoretically possible (such as consulting a third party for advice), markers allowed some latitude in the options that candidates discussed. Confronting Potto Sinter with his ethical and professional failures was the correct option in context and it was disappointing to note that some candidates failed to recognise this.

#### **Question Four**

This question was mainly about risk and, like the other questions in section B, contained three requirements. The notion of 'embedding' risk in organisations is an important one in risk management and is examined in two requirements of this question. Part (a) asked candidates to describe what it is whilst part (b) required an analysis of the case study to assess how easy it would be to embed risk management into the company in the case (Saltoc).

Part (a) was not just asking for a description of embeddedness, however. The question specifically mentioned 'with reference to Saltoc Company'. This required the candidate to describe the term and then give examples of how it could be implemented in Saltoc. The first part was generally done quite well but many candidates failed to gain the application marks. I would again emphasise the importance of carefully reading the question. The 'with reference to Saltoc' indicated that some marks were reserved for this and so it was not possible to get a high mark in part (a) without this.

The case about Saltoc included some descriptions of key personnel and issues with the corporate culture. It was necessary to draw on these to answer part (b). The requirement was to assess the ability of the Saltoc culture to implement embedded risk systems. In order to answer this, it was obviously necessary to study the culture using evidence from the case. Again, time spent studying and scrutinising the case usually resulted in better answers. It was not possible to gain a high mark without a careful study of the Saltoc culture based on the evidence of the case. Some candidates attempted a general discussion either about culture in general or about the importance of risk embeddedness but neither of these were well rewarded.

The third requirement (part c) was worth 11 marks was about external risk auditing. I wrote an article about this in *Student Accountant* and so candidates should have been aware of the essentials. There were two tasks in Part (c): to explain what risk auditing contains and to construct the case for external (rather than internal) risk auditing at Saltoc. Many candidates were able to get the 'contains' marks but then did less well on making the case for risk auditing at Saltoc. Given that I had written an article on this, I was surprised and disappointed that some candidates were unable to recall the four stages in risk auditing. But the level 3 intellectual level task in this requirement was to construct the case for an external risk audit. This meant that candidates had to study the case in order to place themselves in a position to make a convincing argument for external risk auditing. So, again, a detailed analysis of the case was necessary to gain the highest marks.