

Examiner's report

F5 Performance Management

December 2010



General Comments

This was my first paper as the new examiner for F5 but the syllabus remained exactly the same as in previous sittings. The structure of the paper also remained the same – five questions worth 20 marks each – although, in this paper, there was a twenty mark discussion question. The purpose of this was to balance the paper; there was quite a lot of information to absorb in question 2 and there were quite a few calculations to perform in question 3, albeit basic ones. By the time candidates got to question five, it was felt that they would benefit from a chance to display their understanding of budgeting without having to absorb much information. As accountants, we often have to write reports that include little or no numerical analysis. This need for clarity of expression is explicitly required at the professional level papers, so it seems a good idea to start preparing candidates more for this now.

The pass rate on this paper saw a drop from previous recent sessions. I believe that the reason for this is primarily that candidates tried to question spot. So, for example, because linear programming came up in June 2010, the belief was that it would not come up again in December 2010. The lesson to be learnt is that you can't question spot in these exams. You have to make sure that you are comfortable with every area of the syllabus; otherwise you may be caught out. Anyone who watched the 'Examiners' Special' online in September would have got this message.

The paper was 54% computational and 46% narrative, since within question two there were a certain number of marks available for the calculations. On the whole, question four was the best answered, although there were still a surprising number of candidates uncomfortable with the area of activity based costing. In every question, the candidate had the opportunity to earn some easy marks quickly, and well prepared candidates attempted these parts first.

Specific Comments

Question One

This question covered the fundamental area of variance analysis. Part (a) started off with some basic calculations for sales variances and materials variances, followed by some more tricky calculations on labour variances. There were plenty of easy marks in this question, but if anyone didn't understand variances properly, they would have struggled with the labour variances, which required a little bit of thought. The sales and materials variance calculations were thankfully well performed by candidates, but the attempts at the labour variances were poor.

The question clearly stated that the labour variance related solely to the temporary workers. This meant that it was necessary to work out exactly how many hours the temporary workers had worked for. The calculation was not particularly difficult, but it did require an understanding of the scenario. Since permanent workers only had the capacity to work 2,200 hours and a total of 2,475 hours was needed for production, the initial calculation required was that there was a shortfall of 275 hours. However, the question stated that temporary workers took twice as long as permanent workers and therefore the temporary workers would be needed for 550 hours. Approximately one fifth of candidates worked this out and went on to calculate the variances correctly.

Part (b) was the written part of the question, asking for an explanation of the reasons why Carad Co would be interested in the material price planning and the material price operational variance. The most common error was that candidates didn't read the requirement properly. They expected it to be asking them how the manager had performed and this was what they wrote about. Every exam sitting, this proves a problem – candidates pre-empting the question and not reading it properly. It should not be assumed that every single variance question will give you some variances, maybe ask you to calculate some more, and then ask for a discussion of management's performance. Exam papers cannot be allowed to become that predictable as examinees would

then start to only partly prepare for them, on the basis that they know what will be examined, more or less. Candidates that did read the question, however, tended to make a reasonable attempt at this part.

Question Two

This was a typical performance measurement question. There was quite a lot of information to absorb but I strongly believe that, unless you are given plenty of information to work with, it is only possible to make very generalised, insipid comments. This is not what F5 is all about. I want candidates to be able to handle information and make some quality analysis about it. It requires common sense and ability to link information. This should not be too much to ask of a part-qualified accountant, who would have to exhibit these qualities in the workplace.

Needless to say, answers were poor. Anyone who had read my article on this area, or indeed my predecessor's article on this area, would know that insipid comments such as 'turnover decreased by 8.3%, which is poor' will score only a calculation mark, for working out the 8.3%. Is this decrease in turnover poor? Well, it depends on the market in which the company is operating. You have to read the scenario. When you take into account the fact that there has been a 20% decline in the demand for accountancy training, AT Co's 8.3% looks relatively good. You must link information; this is an essential skill for any accountant. Nothing is ever what it seems...ask any auditor!

Let me also take the opportunity to distinguish between an acceptable comment, which might earn one mark, compared to a good point, which might earn two marks. Cost of sales fell by \$10.014m in the year. Part of this reduction was down to a fall in freelance lecture costs. A good candidate would have commented that, whilst the company requested that freelance lecturers reduce their fees by 10%, the actual fee reduction gained was 15%, a strong performance. A comment such as this would have earned two marks. A less observant comment, earning one mark, would have been that the reduction in cost of sales was partly due to the fact that the company requested freelance lecturers to reduce their fees by 10%.

I hope that this question will serve as a good revision question to future examinees of F5. The information given is there to help you make worthwhile comments. It is not there to trip you up. When planning the question, you should annotate it carefully, cross-referencing different parts of the question, linking financial and non-financial information etc.

Question Three

It was this question that was probably made students' downfall on F5 in December 2010. Why? Was it difficult? No. Was it time pressured? Perhaps a little, but the calculations were routine. Was it expected? No! It was obvious that many candidates hadn't even looked at this area at all. They took a gamble and it didn't pay off. Much of this question could have been examined at F2. Why then, was it in the F5 paper? It is becoming more and more apparent that the assumed F2 knowledge for F5 simply isn't there and it is therefore necessary to make candidates realise that it is examinable under F5 and that, if they don't know the subject matter, they need to go away and study it! Would it be possible to turn round to a manager at work and tell them that you can't do a particular piece of work for them because it is on an area you studied last year, not this year? I don't think so. In accountancy, you have to carry knowledge forward with you to use at later stages. You can't simply think that the exam is over, so you can forget it all now. If you have got an exemption from F2 but can't remember the subject, you've got some revision to do before you will be able to sit F5.

Those candidates who had revised this area made a decent attempt at this question, with many of them scoring full marks in part (a) at least. This is because the numbers involved were not particularly complicated. It is important, when answering a linear programming question like this, to set out your workings clearly, with a logical progression in steps from defining the variables and constraints, through to drawing the graph and finding the solution. This makes it easier to mark. The recommended approach is to use the iso-contribution line to find the optimum solution; it is the quickest way to do it. Candidates weren't penalised if they used the simultaneous

equations method, because they were not told which method to use, but they penalised themselves because it took them longer to do it.

It is essential to show all of your workings. So, for example, the iso-contribution line needs to be worked out and then drawn onto the graph. If you didn't show how you worked it out, you stood to lose some marks.

Where you are asked to work to 2 decimal places, you should do it. In this question, it was necessary in order to keep a level of accuracy required to answer part (b) as well. Whilst we gave follow on marks for part (b) wherever possible, if fundamental mistakes had been made in part (a) so that, for example, there was no slack for amino acids, it was hard to award marks.

Question Four

This was the best-answered question on the paper, with a significant number of candidates earning the full five marks available in part (a) for calculating the cost of each product using traditional absorption costing. Part (b), which required a costing of the products under activity based costing, produced more mixed results. Perhaps the most surprising outcome was that nearly all candidates mixed up the driver for machine set ups (which should have been the 36 machine set ups) with the driver for machine running costs (which should have been 32,100 machine hours.) We certainly saw far more of these answers than of correct answers. I'm not quite sure why there was such an incidence of error here, but fortunately most candidates went on to complete the calculations correctly and earn the appropriate follow-on marks.

In part (c), the requirement asked candidates to explain how activity based costing could help the company improve profitability, using the calculations performed in parts (a) and (b). Answers were very poor. The requirement was very specific about what should be talked about – ABC in relation to improving the profitability of this company, not in general. Candidates were expected to say that because, for example, 'product A required more set ups than products B and C, the set up costs were higher, meaning that A's profitability was far lower under ABC. The company could use this to identify how cost savings could then be made, by reducing the number of set ups. Alternatively, the company could consider whether it could charge a higher price for product A, thus improving profit by pushing up revenues'. The biggest problem with answers to part (c) was that candidates did not read it properly and simply started talking about the benefits of ABC in general. They scored poorly for this.

Question Five

This question may have been unexpected in that it was a pure discussion question but this should have helped candidates who were feeling bit pressed for time. Again, anyone who reads Student Accountant would have seen an article in this over the past year and a half on incremental vs. zero based budgeting. These articles are never meant as an indicator of what is going to be examined in a forthcoming session but should be seen as a useful resource, there to supplement the study materials being used. They are there to help broaden your knowledge; if you fail to prepare you prepare to fail.

Part (a) of question five asked candidates to discuss the difficulties encountered in budgeting in the public sector compared to the private sector, drawing comparisons between the two organisations. There were some reasonable attempts at this, although too many candidates simply compared the two types of organisation without relating it to budgeting. Similarly, a significant number of candidates were clearly confused about the difference between public sector organisations as opposed to publicly listed companies, and answered the question entirely incorrectly!

Part (b) asked for an explanation of the terms 'incremental budgeting' and 'zero based budgeting'. These were the easy marks in the question and most candidates got them. Part (c) asked for the key steps in zero based budgeting. These were also easy marks for those who had revised well; answers here were again quite good, with only a minority of candidates making no attempt.

Finally, part (d) asked for a consideration of the statement that there is no longer a place for incremental budgeting, particularly in the public sector. There were some reasonable attempts at this, although, as with part (a), some answers focused purely on the benefits and drawbacks of both methods without relating it back to the statement.

In summary, a mixed set of comments on the different questions. Question 2 was poor, with much improvement still needed in this area; question 3 was really disappointing, showing a lack of revision; and the other three questions were a mix of good and bad, but – for many – not good enough to make up for the difficulties encountered with the other two questions.