

Examiner's report

P1 Governance, Risk and Ethics

March 2018

The ACCA logo consists of the letters 'ACCA' in a bold, white, sans-serif font, centered within a solid black square.

Introduction

The overall performance of candidates in this paper was good, with well-prepared candidates provided with the opportunity to score well. Indeed, there were several candidates who attained an exceptional mark above 80%. The overall pass rate was 51%, which is very much in line with all previous sittings of the exam.

General Comments

The examination consisted of the standard two sections. Section A contained one question for 50 marks and Section B contained three 25-mark questions, from which candidates had to answer two.

In general, most candidates scored equally well in both sections of the exam with the vast majority answering Section A first. The actual order of attempting questions is a choice for each candidate, however it is apparent that those who focussed on Section A first used the additional 15 minutes more productively, and so were less time pressured at the end of the exam. There appears to be some correlation between the order of questions attempted and the overall mark achieved.

It is also important to advise candidates that by writing far too much and extending this to several additional answer booklets does not necessarily guarantee success. The most successful candidates adopted an effective but concise answer approach, and simply addressed the question set rather than making irrelevant points. Another failing of candidates is writing more points than required for the marks available. Even if these points are highly relevant they will score no extra marks, but will use up valuable time that might have been better used on another requirement.

Candidates who are planning to sit the exam for the final time in June, are strongly advised to utilise the resources freely available to them on the ACCA website at:

www.accaglobal.com/uk/en/student/exam-support-resources/professional-exams-study-resources/p1.html.

This website provides a wealth of exam focused resources that will equally help to prepare the first-time candidate or the resitter. For this diet, the recently added article entitled "Organising transactions" would have given candidates a clear insight into how to apply Transaction Cost Theory in Q1. The articles "Corporate governance – from the inside out" and "CSR strategy and Strategic CSR" would have also helped to develop good answers to different parts of the compulsory question. The articles "Strategic and operational risks", "COSO's enterprise risk management framework", "Ethical decision making" and "Independence as a concept in corporate governance" were directly relevant to different parts of the questions set in Section B.

Similarly, candidates who performed well clearly demonstrated the points raised in the study videos: "Answering P1 questions on corporate governance", "Ethical theories kept simple", "Focus on risk" and "Professional marks – the difference between a pass and a fail". Please make full use of all these freely available resources that can make the difference between a pass and a fail.

Question One

The long case study for this diet concerned a government department responsible for the delivery of education services in a fictitious country. Apart from the obvious need to provide teaching resources and maintain high learning standards, the department also was committed to a broader social and environmental agenda whilst delivering value for money to taxpayers.

A recent change to the contracts of peripatetic [visiting] art and music teachers, made by the head

of the education department, meant that these teachers were now only paid when they actually taught in class, and not when traveling to and from schools or preparing for classes. The peripatetic teachers were also not entitled to sick pay or holiday pay, but they were expected to be on call to work as and when required, so their plight was taken up by a major newspaper. It was reported that many of these teachers in rural areas were struggling financially because they had no guarantee of work.

The justification for this policy, which if successful was planned to be rolled out to other subject areas, was to provide operational flexibility and save tax payers money. However, the teachers on the new contracts claimed that the education department was acting like a profit-making organisation and showed little or no social responsibility. Some teachers felt so aggrieved that they were considering taking legal action against the education department.

To add to the problem a recent internal audit report identified that substantial bonuses were paid to the head of the education department in return for the reducing operating costs and changing working methods. This bonus was negotiated as part of the head's remuneration package, but since its introduction there had been a reduction in art and music education performance across state schools.

Part (a) for 8 marks required the comparison and contrast of ownership and accountability in the education department to that of a listed company. This was a relatively straight forward question that stronger candidates scored well in as they identified the similarities and dissimilarities. The weaker candidates simply identified the owners of each organisation and what they wanted from it, which fell far short of the depth of answer expected.

Part (b) was concerned with how the concept of corporate social responsibility (CSR) is communicated to an organisation's stakeholders. This requirement was also worth 8 marks, but to achieve this a clear explanation of the different ethical stances that could be adopted by the education department and a profit-making organisation was required. Weaker students simply regurgitated the range of ethical stances described by Gray, Owen and Adams, with the stronger candidates understanding which of the 7 stances were more appropriate to the different needs of each organisation described in the scenario.

Part (c) was in two parts. The first part for 6 marks simply required an explanation of CSR strategy, and to recommend an approach for the education department to develop such a strategy. The stronger candidates suggested a structured and methodical approach to devising strategy in the context of a public-sector organisation, whereas the weaker students failed to address the second element of the requirement. Part (c)(ii) was only worth 4 marks and covered the regularly tested issue of embedding something into a culture, in this case it was CSR. This was surprisingly badly answered or omitted by many candidates, with the stronger ones merely applying common sense to the situation and thereby able to achieve all the allocated marks.

Part (d) required the candidate to draft a letter from the head of an audit team to central government. If the answer was correctly presented it earned the candidate professional marks for format, clarity, logical flow and persuasiveness. Most good answers scored 3 or 4 of these marks.

(d) (i) was on the subject of Transaction Cost Theory, and was worth 6 marks, but had not been tested in P1 for some time. However, a recent article published on the website would have provided candidates with the means to assess the behaviour of the education department head

when introducing the new contracts. Good candidates had evidently read the article and so introduced issues such as independence and bounded rationality into the substance of their answers. Weaker candidates had not studied this area of the syllabus and so made up answers that often scored no marks.

(d) (ii), also for 6 marks, tended to be well answered by most candidate as it was on the popular subject of stakeholder claims. Provided the candidate correctly explained the term and then provided an assessment of claims from both the teachers and government perspectives they scored well.

(d) (iii) drew the letter to an end by assessing how the bonus earned has affected the behaviour of the education department head, as well as providing a case for a more ethical bonus structure. Good candidates broke the requirement down into its two constituent parts and addressed each in turn, whereas weaker answers tended to ramble and lack structure.

Question Two

The first optional question in Section B was the most popular of all the optional questions. The scenario was concerned with pressure that was being exerted on a qualified accountant who was leading an audit team examining the ongoing feasibility of a project. The main source of the pressure came from the accountant's girlfriend who happened to be the project manager, but their personal relationship remained a secret at work. The audit report, to be presented to the audit committee, suggested that the project no longer represented value for money so should be cancelled. However, this would mean his girlfriend, and many other colleagues, could lose their jobs. Therefore, the essence of the question was about the expected ethical and professional behaviour from the accountant.

Part (a) was worth 8 marks and required an explanation of professionalism for an accountant, and how this should influence the behaviour of the accountant/audit team leader in the situation described in the scenario. Weaker candidates simply listed the IFAC five fundamental ethical principles without any attempt to apply them to the scenario, which helped in part to explain professionalism but could not secure a pass mark. Stronger candidates carefully selected the principles that applied in the situation described and from that were able to provide a clear and accurate answer. Future candidates must try to think about how to use their knowledge to address the specific requirement.

Part (b) required an evaluation of the ethical threats posed to the accountant from the situation as well discussing safeguards that would be appropriate in these circumstances. Weaker candidates simply listed the threats to independence that they had previously studied in paper F8 but did not show how they could be prevented. This meant that they only scored 3 of the 9 marks available. The stronger candidates focussed their attention on how to build structural and organisational safeguards to reduce the risk of unethical and unprofessional behaviour at the company.

Part (c) tended to be very well answered by most candidates as it required the application of the American Accounting Association model of ethical decision making to the dilemma faced by the accountant. Provided the candidates knew the 7 steps to the model and applied the information provided in the scenario to make the right decision they secured all 8 marks available. Weaker candidates should not have selected this question because they simply did not know the model and so scored no marks.

Question Three

This was the least popular of the three optional questions and was concerned with a diversified company that operated a portfolio of leisure-related businesses. The most profitable individual business was a network of 10 theme parks well dispersed around the country that are popular with young people. A recent accident occurred on the most popular ride at one of the theme parks that caused serious injuries to several paying visitors. An internal investigation identified internal control failings as the cause of the accident, and so this ride was closed at all 10 parks. The aftermath of the incident was recorded by a TV crew, which potentially caused huge damage to the company's image and reputation. This is likely to further exacerbated by criminal and civil court action that is probably to follow the accident.

Part (a) required the identification and analysis of both the generic risks to the company and specific risks to the theme park following the accident for 7 marks. Weaker candidates identified a whole range of risks that could be applicable, but often included risks that were irrelevant. This showed a lack of understanding as to what the question was asking. Stronger candidates were more selective and carefully analysed the risks within the context of the scenario.

Part (b) was only worth 4 marks and simply required the concepts of severity and probability to explained and illustrated using the theme park accident. It was quite disappointing that many candidates tackled this requirement badly, as they did not understand the fundamental concept of risk assessment. Future candidates must be able to assess any risk presented to them so that they can decide on the most appropriate methods of mitigation.

Part (c) for 6 marks required candidates to describe the core elements of a suitable internal control system. Weaker candidates tended to produce a generic list of the characteristics of an internal control system and not its elements. Stronger candidates scored very highly on this part, provided they were able to draw on knowledge of the COSO framework to generate and structure their answers.

Part (d) required recommended improvements to the control systems at the theme park to avoid a recurrence of the accident for 8 marks. Good answers were from those candidates who provided a set of sensible and practical measures that would have been appropriate, thereby justifying their inclusion as a control. Weak candidates provided generic controls that were often irrelevant to the situation described in the question.

Question Four

The final optional question of this diet concerned a listed sports equipment retailer that had enjoyed substantial growth and profitable performance over its 25-year existence. The company operated in a highly competitive market place but was able to sustain its success by operating a low-price business model. Recent political events mean that a decision to leave a customs union will potentially inhibit trade in neighbouring countries and could impact unfavourably on currency exchange rates. To deal with these changing events the company, and more specifically the CEO, has decided to set up a risk committee as it has not been considered necessary to formally manage risk strategically until now.

In part (a) 6 marks were available for an explanation of the risk attitude and assessing how it has been influenced in this particular company. Strong candidates produced relevant and specific

points taken from the scenario for a well- developed answer. Whereas the weaker candidates simply discussed the terms risk seeking and risk aversion.

Part (b) for 9 marks required candidates to explain the dynamic nature of risk assessment, and not risk dynamism which was a common mistake from weaker candidates. However, to secure a pass mark it was necessary to advise the company how they could respond to the political and economic aspects of risk facing the company. Stronger candidates used the structure of the question to generate enough points to score most of the marks available, as the scenario has enough detail to expand on these. This is a good technique for candidates to use in the final P1 exam and also in Strategic Business Leader in the future.

Part (c) for 10 marks was well answered by most candidates. The first sub-requirement was to explain the role and responsibilities of a risk committee. The second element required a discussion of how non-executive directors on a risk committee improve the effectiveness of corporate governance. The main difference between weak and stronger candidates was how both parts of this requirement was applied to the situation described in the scenario, rather than providing a purely textbook answer.