

This document should be read in conjunction with the examiner’s suggested answers and marking guidance.

General comments

CGMA Exam – August 2016 – Rationale

This paper was based on a pre-seen scenario which described a company in the alternative energy industry. The scenario was made available in advance of the exam and a number of variant papers were set, each offering additional scenario-based information and each setting three sections to be completed. Each section was split into two or more specific elements. This is a very interesting industry which many candidates should understand. The pre-seen scenario was detailed and well prepared candidates should have been able to give good answers in the context of the industry. The unseen scenarios were interesting and presented some realistic questions on the industry.

Candidate performance

Performance overall was reasonably good for many candidates, there were however many weak scripts. There were several weak areas in which candidates struggled. For example, ethics; many candidates could not name the ethical principles, apply them or even recognise an ethical issue. Another poor area was finance where the lack of ability was surprising. It is clear that candidates are becoming weaker at technical accounting questions and better at management questions which is not ideal.

The main problems were candidates failing to address the specific task requirements and writing everything they knew on the topic being asked about. Many candidates did apply their answers to the industry which was good. However, some candidates did not appear to be familiar with the pre-seen material at all. Most candidates answering the variants attempted all three sections but some missed out some of the elements, e.g. they would write about risks but not mitigations. There still seems to be a problem with a significant number of candidates presenting answers which lack sufficient depth and development.

Some candidates had made good use of the pre-seen materials and showed an understanding of the alternative energy industry which was heartening. Some candidates, however, did not demonstrate much knowledge of the pre-seen material which was surprising; it was as if candidates did not realise it was important. It was also good to see most candidates tried to use relevant models and did not produce lists of inappropriate models.

In most of the questions it was hoped candidates would be able to use industry knowledge and knowledge of the company to help formulate answers, there was some evidence of this but some candidates did not know anything about the industry.

Variant 1

	Designed to test ability to:	Competency being tested:	Syllabus lead learning outcome:
Section 1	Evaluation of investment opportunity	Technical skills	F3 A1a - advise on the overall strategic financial and non-financial objectives of different types of entities
	Discussion of protecting intellectual property	Business skills	E3 A1d - recommend how to build and manage strategic relationships with stakeholders
Section 2	Advise on suppression of negative research study	People skills	P3 A3a - evaluate ethical, social and environmental issues arising from risk management
	Motivating stakeholders	Leadership skills	E3 C1b - evaluate the role of leadership in managing the change process and building and managing effective teams
Section 3	Advise on share valuation	Technical skills	F3 C2b - evaluate the validity of the valuation methods used and the results obtained in the context of a given scenario
	Advise on risk of losing staff	People skills	P3 A1c - recommend responses to identified risks
	Advise on presentation of study findings	Business skills	F3 A1c - advise on the use of sustainability and integrated reporting
	Discuss governance issues of share distribution	Leadership skills	P3 B3a - evaluate the risks associated with poor governance structures

Comments on performance

Section 1

Part 1 concerned a project evaluation for and against fit with strategic financial and non-financial objectives and was generally well answered. Candidates occasionally repeated the same points using up time that could have been better spent addressing the second part of the question which was often ignored completely.

Part 2 was about actions needed to protect rights under the terms of the arrangement should the study be successful. In the majority of cases Part 2 appeared to have been treated as an afterthought, perhaps candidates have no concept of securing commercial rights over research outcomes, or they are simply naive about commercial funding expectations but the vast majority failed to secure the situation commercially. Only a handful answered this well with hard facts. Those who offered a reasonable answer were mostly based on vague assertions that we should have a written agreement of some sort

Section 2

Part 1 - Whether or not to exercise the right to prevent publication. Candidates grasped the pros and cons of publishing / anonymity well but as with section 1 tended to either not leave enough time for the second part of the question, or alternatively did not realise the importance of the perspective of internal stakeholders. Quite a number of candidates did integrate their answers well in this part, inserting internal stakeholders as one of the interested parties in the general debate about whether or not to publish.

Part 2 - Implications of publishing or suppressing results from internal stakeholder's perspective. Most candidates failed to grasp the de-motivational aspects of not succeeding and failed to recognise that the ethos of AEN would be taking a knock back for all its good efforts. Those who did tended to pull through on both engineers and founder morale and scored well.

Section 3

Overall section 3 was the best answer for most students and on the whole was well answered.

Part 1 - Valuation of non-quoted stock, choice of FAIR model. Many candidates described the pros and cons of a number of different valuation models well.

Part 2 on risk evaluation and HR response in secondary resignations was well received with better candidates opening the discussion quickly into culture health and open organisation feedback; quite a number scored well here by differentiating between immediate and more remote colleagues of Gita and her likely degree of influence. Many grasped the fact that speedy communication and feedback was essential to gauge what might be brewing with several looking to re-engage Gita if possible through negotiation, rather than have her locally set up with competition or in a new venture with associates potentially drawn from similarly disillusioned colleagues from AEN.

Part 3 was a little vague and waffly, there were very few strong answers to this part.

Part 4, with regard to governance risks, many candidates understood the requirement and answered it competently. Candidates who appreciated more than agency theory gained better marks as they recognised that boards need to represent all ownership elements, the need to have more breadth of experience on the board and possible employee/shareholder representation.

Variant 2

	Designed to test ability to:	Competency being tested:	Syllabus lead learning outcome:
Section 1	Advise on exploitation of intellectual property	Business skills	E3 B1a - evaluate the process of strategic analysis and strategic options generation
	Recommend financing strategy	Technical skills	F3 B1a - evaluate the impact of changes in capital structure for an incorporated entity on shareholders and other stakeholders
Section 2	Advise on ethical risks	People skills	P3 A3a - evaluate ethical, social and environmental issues arising from risk management
	Discuss appointment and management of external lobbyists	Leadership skills	E3 A1b - recommend approaches to business/government relations and to relations with society
Section 3	Advise of identification of stakeholders	People skills	F3 A1c - advise on the use of sustainability and integrated reporting to inform stakeholders of relevant information concerning the interaction of a business with society and the natural environment
	Recommend content for sustainability report	Leadership skills	F3 A1a - advise on the overall strategic financial and non-financial objectives of different types of entities
	Discuss internal audit approach	Business skills	P3 C2a - evaluate the essential features of internal control systems for identifying, assessing and managing risks
	Discuss checks on report content	Technical skills	P3 C3a - evaluate the effective planning and management of internal audit and internal audit investigations)

Comments on performance

Section 1

Section 1 firstly required candidates to consider whether AEN should build the biodigester itself or sell the intellectual property. Secondly candidates were asked to consider whether to fund the potential investment with debt or equity and the issues involved with the selected financing method.

Part 1- Build the biodigester or sell the intellectual property. This question was answered well by most candidates. Many answers were well constructed and covered advantages and disadvantages of both potential strategies. A significant number of candidates used the SAF approach to structure their answers to this question, which was useful and appropriate.

Some candidates did not perform well on this question because they only considered the biodigester as a potential strategic option and failed to consider the selling of the intellectual property at all. Also, some candidates provided very thin answers, which failed to consider a significant range of strategic issues.

Part 2 - Equity or Debt funding decision. Candidates performed reasonably well on this part of section 1. Most candidates considered a range of positive and negative factors associated with both debt and equity financing. Those candidates who did not answer this question well were those who only considered debt or equity as a financing option and therefore failed to cover a sufficient range of issues.

Overall, section 1 was answered reasonably well by most candidates.

Section 2

Section 2 covered two separate issues. Firstly, candidates were asked to consider the ethical issues related to lobbying the government to announce grants for the biodigester quickly and secondly, to discuss the approach that should be taken to select and manage an external lobbying company.

Part 1 - Ethical issues relating to lobbying the government. This part of the section was not well answered by most candidates. Some candidates did correctly identify the ethical dilemma involved in asking the government to announce the grants quickly and also used the correct aspects of the ethical code to evaluate the dilemma. However, these answers were few and far between. It was extremely disappointing that a significant number of candidates who, firstly, did not correctly identify any real ethical issue and then, secondly, presented a mere description of the ethical principles, with little or no direct application to the scenario.

Part 2 - Approach to selecting and managing an external lobbying company. This part of the task was again, disappointingly answered. Many candidates' answers went little further than discussing the advantages and disadvantages of external lobbying companies. This is not what was asked for. Some candidates who did perform well on this part of the task did so because they considered the approaches required to select and manage an external lobbying company, considering the issues specific to AEN. However, few candidates adequately considered both the selection and management issues.

Overall, section 2 was not answered well by most candidates. Many answers were thin and very poorly applied to AEN.

Section 3

Issues relating to GRI Reporting Principles

Part 1- Identification of stakeholders. This task was not answered well. Far too many candidates merely applied Mendelow's matrix to AEN's stakeholders, identifying their levels of power and interest, but ignoring completely the impact that this would have on AEN's GRI Reporting. Many candidates ignored this completely.

Part 2 - Matters to report on to present contribution to sustainability. This second part of the task was answered well by most candidates. Most focused correctly on AEN's transparency in the reporting of its emissions and impact on the environment and also the work that they are doing to reduce this. Most also considered a wider range of issues, such as research and development activities and its philanthropic activities.

Part 3 - How internal audit should evaluate the reliability of disclosures. Candidates did not perform well on this aspect of the section. Many answers were very thin and in fact, a significant number of candidates did not make a serious attempt at this requirement of the task. Most answers were merely descriptions of internal audit activities, such as sampling and testing and very few answers correctly focused on the reliability of the disclosures in the GRI Report.

Part 4 - How should internal audit ensure the report is balanced. This part of the task was answered poorly. Once again, most answers were very thin and a significant proportion of candidates did not make a serious attempt at this part of the task. The only point that was made consistently by candidates was that the report should contain both positive and negative aspects of AEN's performance. Apart from this, candidates had little more to say on this requirement.

Overall, Task 3 was answered poorly by most candidates.

Variant 3

	Designed to test ability to:	Competency being tested:	Syllabus lead learning outcome:
Section 1	Advise on costs and benefits of a listing	People skills	E3 A1d - recommend how to build and manage strategic relationships with stakeholders
	Determine issue price	Technical skills	F3 C2a - calculate the value of a whole entity
Section 2	Evaluate potential non-executive board appointment	Leadership skills	P3 B3a - evaluate the risks associated with poor governance structures
	Discuss the ethical implications of publishing facts that are accurate but misleading	Business skills	E3 A2a - evaluate ethical issues and their resolution within a range of organisational contexts
Section 3	Discuss implications of employees' inability to diversify	Technical skills	F3 C2a - Calculate the value of a whole entity
	Motivational effects of employees owning shares	Leadership skills	F3 A2a - evaluate the interrelationship between investment, financing and dividend decisions for an incorporated entity
	Share price implications of employee share trading	People skills	P3 A1a - identify the types of risks facing an organisation
	Discuss importance of share price volatility	Business skills	P3 A1b - evaluate the organisation's ability to bear identified risks

Comments on performance

Section 1

The first part raised the question of the merits of seeking a stock market quotation, albeit on a small company market.

Candidates were generally aware that AEN is a relatively small company that is closely held. Answers took the nature of the business and the interests of the present owners into account.

The second part addressed the question of valuing shares for the purposes of the listing. Answers were generally valid, although many candidates took the indirect approach of describing every valuation model they could think of and rejecting those that seemed irrelevant. Even those answers reflected an understanding of the business problem.

Section 2

The first part asked for an evaluation of the merits of appointing James Whittaker as a non-executive. Answers to this were generally very well written. Candidates clearly know the role of the non-executive and were able to apply that knowledge to the potential appointee's CV. For example, most candidates picked up the need for a fresh look at the company and questioned the merits of adding yet another engineer to the board.

The second part dealt with the publication of a forecast profit figure. Extrapolation of recent trends would give a defensible figure that would attract shareholders. However the directors are aware that the forecast would be misleading because an extrapolation ignores recent changes. Would publication be ethical? Candidates offered good arguments concerning the need to produce a more realistic estimate.

Section 3

The first part dealt with the problems faced by employees who receive shares as part of their remuneration package. Such an investment is very unlikely to be properly diversified and so the return will be inadequate to compensate for the risks. Candidates answered this part of the question quite badly. There were very few answers that picked up the difficulties of ensuring an acceptable rate of return.

Answers to the second part were a little better, although some of the arguments were a little naive. Arguably, this issue is one where both sides of the argument have to be presented because the granting of shares to employees probably would enhance motivation to some extent, but may not be as significant as one would hope.

Most candidates picked up the possibility that an efficient market would interpret a sale of shares by an employee as a signal that business was bad. Some candidates answered the question on the basis that the markets might be affected by the granting of shares. Such answers were not particularly relevant and tended to repeat points made earlier in the question.

Answers to this part varied in quality. Many candidates argued well that higher volatility would increase the cost of equity and so might affect the appraisal of projects. Other candidates wrote very short answers that did not really address the question.

Variant 4

	Designed to test ability to:	Competency being tested:	Syllabus lead learning outcome:
Section 1	Evaluate risks associated with bad publicity	Business skills	P3 A1b - evaluate the organisation's ability to bear identified risks
	Evaluate problems associated with environmental reporting	Leadership skills	F3 A1c - advise on the use of sustainability and integrated reporting to inform stakeholders of relevant information concerning the interaction of a business with society and the natural environment
Section 2	Advise on promotion of investment opportunity	Technical skills	P3 E1a - evaluate investment projects
	Evaluate ethical implications of presenting environmental argument for investment	People skills	E3 A2a - evaluate ethical issues and their resolution within a range of organisational contexts
Section 3	Recommend critical success factors	Business skills	E3 D1b - recommend solutions to problems in strategic performance measurement
	Recommend KPIs	Leadership skills	E3 D1b - recommend solutions to problems in strategic performance measurement
	Evaluate impact of hedge accounting	Technical skills	F3 A2c - evaluate the impact of the adoption of hedge accounting and disclosure of financial risk on financial statements and stakeholder assessment
	Evaluate effects of hedge accounting on reported profit	People skills	F3 A2c - evaluate the impact of the adoption of hedge accounting and disclosure of financial risk on financial statements and stakeholder assessment

Comments on performance

Overall

Once again the standard of scripts was reasonable, with relatively few very weak or incomplete scripts. Most candidates attempted all three sections. Better candidates tended to provide responses with a structure, using headings based on the requirements of the exam. Stronger candidates also managed their time well and put appropriate effort into each section.

One issue was candidates not answering the questions presented. Some seemed to have prepared solutions to questions which were not those asked, or had not read the requirements carefully enough.

The level of technical knowledge, particularly of financial reporting was generally very disappointing.

Section 1

Section 1 asked the candidate to address problems arising on a wind farm site, the Black Ridge wind farm. The first part was to explain the risks to AEN of acting for Black Ridge and manage the response to the disaster. The second was to explain the dangers associated with AEN publishing its wildlife risk assessment and how these might be overcome.

Part 1 – Risks. Most candidates successfully identified risks although some talked at length about how a strategic plan should be prepared which would involve identifying the risks which meant that the focus of their answer was at a tangent to what was required. Very few identified the upside risk of the scenario. Some used models such as the TARA framework.

Part 2 - Wildlife risk assessment. Some candidates dealt with this section very briefly by saying that publishing the risk assessment was dangerous and so AEN should not publish. This approach showed poor exam technique. Most identified the dangers of activists focussing on the information published, but did less well at suggesting how those dangers could be overcome.

Section 2

Section 2 presented candidates with the development of a beacon which could deter birds from flying too close to wind turbines. They were asked to discuss whether potential buyers could be persuaded to purchase the beacon because this would reduce the

risk of running a wind farm, despite the high cost of the beacon. They were also asked to explore the ethical implications of publicising the beacon.

Part 1 - Beacon proposal. Better candidates provided a rounded discussion of whether the proposed approach would convince potential buyers, and what other arguments could be brought to bear. Some candidates misinterpreted the question and discussed the risks of AEN manufacturing the beacon. Others decided that buyers were unlikely to buy the beacon and quickly dismissed the proposal, an approach which did not maximise marks scored.

Part 2 - Ethical issues. Candidates were asked about whether publicising the beacon caused ethical issues. This was often not well addressed, with some candidates either stating that there was no ethical dimension, or that the ethical problems were so serious that the project should be abandoned. Brief answers like this did not give a full exploration of the issues.

Section 3

Candidates were asked to address four separate issues:

Part 1 - To identify and justify two important CSFs. Some candidates addressed this requirement well, and identified appropriate CSFs. Weaker candidates did not appear to know what a CSF is.

Part 2 - To identify the KPIs which could be used to measure progress to each of the CSFs. Generally speaking those candidates who identified appropriate CSFs also suggested appropriate KPIs to measure them.

Part 3 - To explain how hedge accounting could protect against currency risks in financial reporting. This section was extremely poorly attempted. Very few candidates understood the concept of hedge accounting. They often explained transaction translation and economic risk, which is not what was asked for.

Part 4 - To explain whether hedging would make AEN look more profitable. This was marginally better attempted than part 3 but was still generally poor, with many candidates discussed in depth the methods of hedging (options, futures etc.) rather than answering the question as required.

Variant 5

	Designed to test ability to:	Competency being tested:	Syllabus lead learning outcome:
Section 1	Evaluate implications of reporting departmental profitability	Business skills	E3 B1a - evaluate the processes of strategic analysis and strategic options generation
	Discuss reporting period	Leadership skills	P3 C1a - evaluate the appropriateness of control systems for the management of an organisation
Section 2	Evaluate social responsibility	People skills	F3 A1a - advise on the overall strategic financial and non-financial objectives of different types of entities
	Discuss key risks	Technical skills	P3 A1a - identify the types of risk facing an organisation
Section 3	Recommend approach to business valuation	Business skills	F3 C2a - calculate the value of a whole entity
	Recommend dividend strategy	Technical skills	F3 B2b - recommend appropriate dividend policies
	Discuss challenges of creating new PR department	Leadership skills	E3 C2a - evaluate tools, techniques, and strategies for managing and leading the change process
	Evaluate merits of contracting out client business	People skills	E3 C3a - evaluate the role of the change leader in supporting strategy implementation

Comments on performance

Section 1

Part 1 - Analyse profits. Candidates were free to address these issues in any manner that they deem appropriate. They should have considered both the impact on management decisions and the additional insights that such an analysis might offer.

The main points which were done well by candidates in this section were that many candidates highlighted the interrelationships and the dysfunctional aspects of this scenario and discussed in detail the problems of apportioning costs to division - the average candidate however failed to develop the interrelationships and dysfunctions in any depth or sophistication.

Part 2 - Monthly figures. Candidates should have used whatever arguments they deemed appropriate, but the basic issue is that this is a business that operates fairly long term contracts and so a monthly reporting cycle is too short to be of any real use.

This element of monthly reporting was less well done with candidates failing to appreciate the difficulties of analysing projects which are long term and fail to fit a monthly expense/income pattern - the responses tended to be very brief with little consideration given to alternative methods of recording, reporting and control, the marks were low for this part of section 1.

Section 2

Part 1 - Social responsibility. This requirement addresses the basic argument that purely “technical” decisions are free of ethical values while more “social” activities are not.

Candidates should offer reasoned arguments for and against the position that Legal and PR are harmful.

This was the least well performed part of the exam. Very few candidates set out a basis for evaluation. The main failing in the first part was the inability of candidates to evaluate the wide reaching nature of social responsibility and the fact that it concerns many more groups than local resident and protestors.

Part 2 - Key risks. This requirement develops the theme that Legal and PR are effectively operating in opposition to interested parties who would wish to block AEN’s clients. In this section a majority of candidates discussed risk but failed to be systematic in the layout of the various risks involved with very few categorising risks into "business risk", "reputational risk", financial risk" etc. which tended to lead to rambling and ill structured discussion. Because of this, few candidates achieved a high mark. It helps if the solutions are well structured.

Section 3

Part 1 – Valuation. Any basis is acceptable provided it relates to a business in the service industry. In this case, dividend models are unlikely to be suitable, so profit-based models are probably required. This was by far the best answered section with many candidates using 4 valuation methods and analysing their usefulness in the given circumstances - the application of numbers was not handled as well with few attempting to apply any numbers or calculations to this section.

Part 2 – Dividend. Answers should focus on the position that AEN finds itself in, including mention of the block of shares held by the founders. The candidates were appreciating the need to hold back funds and not declare a huge dividend but few appreciated that the main shareholders were the directors and the fact that a large initial outgoing of cash to fund a new PR division was unlikely - more of a long-term commitment. Candidates did not achieve high marks in this section.

Part 3 - New department and outsourcing. Candidates should focus on the specific needs of AEN, drawing on the pre-seen material. The challenges were reasonably well done but there was little initiative shown in how to overcome these aspects. The answers to advantages and disadvantages seemed to mainly revolve around the fact that the new company would know AEN's systems and would be a relatively seamless fit whilst disadvantages were mainly limited to costs and conflicts between the two companies. There were some very good answers to this part but some very weak ones as well.

Tips for future candidates

It is obvious that candidates must read the questions carefully and answer what is asked. Candidates should read the pre-seen material carefully and come into the examination understanding the industry and the company which will be the focus of the exam. This will help candidates formulate good answers that relate to the questions.

Candidates are noticeably weak in technical accounting areas of the syllabus, this must be addressed by candidates or they will fail the case study exams.

Candidates must manage their time well and make sure they do not run out of time on parts they know well.

A good level of knowledge of the three strategic syllabi is necessary in order to do well in the exams, it is not enough to have knowledge of topics. Candidates must be able to apply their knowledge to a variety of situations and show they have an in depth knowledge of the subject matter.