

## **CGMA Exam – Examiner’s report**

**February 2017 exam session**

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

### **General comments**

This exam was based on a pre-seen scenario which described a company in the reality television 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 tasks to be completed. Each task was split into two or three specific elements. This is a very interesting industry. 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**

This case study was on the reality television industry. Most countries have reality television shows so it is a context that most candidates should have understood. Performance overall was reasonably good for many candidates, there were however some weak scripts. There were several weak areas which candidates must improve at in the future. Ethics was one poor area, another was governance which was surprising. It is very clear that candidates are becoming weaker at technical accounting questions and better at management questions which is not ideal. Candidates are much better at structuring their answers which is very good. It is much easier to mark scripts if they have a good structure and are well laid out.

The main problems were candidates failing to answer what was asked and writing everything they knew on the topic being asked about. There still seems to be a problem with a significant number of candidates presenting answers which lack sufficient depth and development.

### **Looking ahead to future examinations**

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

**Variant 1**

	<b>Designed to test ability to:</b>	<b>Competency being tested:</b>	<b>Syllabus lead learning outcome:</b>
<b>Section 1</b>	Evaluate risks of founder acting as CEO and Chairman	People skills	P3 B3a - evaluate the risks associated with poor governance structures
	Evaluate corporate strategy	Business skills	E3 B1a - evaluate the process of strategic analysis and strategic options generation
<b>Section 2</b>	Evaluate dividend policy	Technical skills	F3 B2b - recommend appropriate dividend policies.....
	Recommend KPIs for measuring CEO performance	Leadership skills	E3 D1b - recommend solutions to problems in strategic performance measurement
<b>Section 3</b>	Discuss implications of social responsibility report	Technical skills	F3 A1c - advise on the use of sustainability and integrated reporting to inform stakeholders.....
	Evaluate host government's concerns about company behaviour	People skills	P3 D2b - evaluate appropriate methods for the identification and management of financial risks associated with international operations
	Recommend approach to post implementation audit	Business skills	P3 E1c - evaluate the outcomes of projects post implementation and post completion
	Evaluate impact of change for share price	Leadership skills	F3 A1a - advise on the overall strategic financial and non-financial objectives of different types of entities

## Comments on performance

### Section 1

Overall this seemed to be answered well with students understanding the potential issues. Sometimes they left insufficient time for the second part of the question.

#### **Newspaper article highlighting potential issues with Denny White as CEO and Chairperson**

Candidates on the whole picked up many aspects of why this causes problems and most discussed that it should be avoided. However, relatively few gave a good balanced answer showing how the company had been built on his strengths and that he still wielded significant influence.

Where candidates stopped to consider the wider picture, they gave good answers. There are several advantages which come with Denny's experience which can be brought to the Board and is a strength of Evestar.

#### **Evestar's programmes in production**

Overall this was weakly answered. Some candidates had clearly spent more time answering part 1 but there seemed to be a lack of reflection on the pre-seen material or indeed from wider experience of programme scheduling.

The best answers focused on the fact that the formula is successful and focus should be put on future planning and development with close attention to audience figures and general feedback, rather than responding to an individual critic.

### Section 2

Candidates mostly understood the issues with the current dividend approach but often failed to give a balanced view with arguments for both sides.

KPIs were weaker and more briefly covered. Many candidates just listed KPIs with no qualification. Some listed irrelevant KPIs.

#### **Dividend policy and the need to reinvest profits**

Mostly candidates argued that dividends were too high but that shareholders were accustomed to this policy and the share price would suffer if changed. Many commented on the profit taking aspect of Denny's own shareholding being a large influence.

Some considered actual business needs in a low capital deployment industry and concluded that there was no issue.

The best candidates took a wider view and considered all the above plus a need to evolve programmes for the future.

### **CEO performance indicators**

There was a good wide range of KPIs put forward to assess CEO performance. These were often well stated and clearly defined. It would have been good to have had a little more follow through in many cases to argue why the KPI was relevant in the scenario. However, some candidates did this well and scored highly.

A balanced scorecard in itself is a wrapper for industry-relevant KPIs, the details need to be given as to the elements and the purpose of those elements.

Many extraneous or irrelevant KPIs were also given, usually with no justification. This approach did not gain marks.

### **Section 3**

Comments on the environment report and dealing with the minister were good. The Post Implementation Audit response was very mixed.

### **Environmental reporting**

Many commented on general aspects of the environmental report. However relatively few drew out the nuance of the effort and timing of the report and as to whether it was already drawn up. Many more commented on the issues raised under the protesters and what would be good ways to address them.

### **Liaison with foreign government Minister of Tourism**

Candidates raised a wide range of measures for addressing the concerns made about Evestar's activity reassuring the Minister for Tourism, mostly based on publicity gained for the local area and environment for encouraging additional tourism, plus benefits for revenue generated by having production crews staying for extended periods.

### **Implementation review**

Candidates were often confused here about the purpose and process of setting up a team, rather than holding a post implementation review/audit. Likewise there were interpretation errors in looking at the review of an ongoing project whereas the question explicitly directed them to a completed phase to review.

### **Strategic Board position change affecting share price**

Many candidates confused this with a process required to persuade Denny to step down as CEO. Rather than reading the question details: **"Whether"** persuading Denny to step down as CEO could have a positive impact on Evestar's share price. This was quite a widespread error.

Those who read the question correctly were able to answer well, giving details of sounding out the industry analysts to interpret their reactions and interpret whether Denny's step down would enhance the market perception and valuation of Evestar or not.

**Variant 2**

	<b>Designed to test ability to:</b>	<b>Competency being tested:</b>	<b>Syllabus lead learning outcome:</b>
<b>Section 1</b>	Evaluate strategic benefits and risks	Business skills	F3 C1a - evaluate the financial and strategic implications of proposals for an acquisition, merger or divestment
	Discuss ethical implications of refusing to discuss a takeover offer	Leadership skills	E3 A2a - evaluate ethical issues and their resolution within a range of strategic organisational contexts
<b>Section 2</b>	Evaluate risks associated with a breach of confidence	People skills	P3 A1a - identify the types of risk facing an organisation
	Evaluate takeover offer	Technical skills	F3 C3a - evaluate alternative pricing structures and bid process
<b>Section 3</b>	Recommend response to criticism concerning programmes	Business skills	E3 B2b - recommend how to manage the product portfolio of an organisation to support the organisation's strategic goals
	Recommend response to concerns about new legislation	People skills	P3 A1c - recommend responses to identified risks
	Recommend approach to performance measurement	Leadership skills	E3 D1a - evaluate alternative models of performance measurement in a range of business contexts
	Recommend approach to reassure customers	Technical skills	P3 C1a - evaluate the appropriateness of control systems for the management of an organisation

## Comments on performance

### Section 1

Section 1 firstly required candidates to evaluate the strategic benefits and risks to IndTV of acquiring Evestar. Secondly candidates were asked to consider the ethical implications of the Board rejecting the offer before hearing the full details of the proposal.

#### **Strategic benefits and risks to IndTV of acquiring Evestar**

This question was answered well by most candidates. Most candidates were able to present a wide range of well-argued and applied benefits and risks to IndTV of acquiring Evestar. It was pleasing to see the range of answers provided and the level of direct application to the scenario. However, there were some candidates who approached the question incorrectly as they considered the risks and benefits from the perspective of Evestar and not IndTV. Candidates are reminded to read the question requirements carefully.

#### **The ethical implications of rejecting IndTV's offer**

This requirement was answered reasonably well, although most answers were rather thin and lacked real application to the scenario. Some candidates provided only theoretical answers, outlining the ethical principles, which clearly was not sufficient. Many candidates did correctly identify the main ethical principles challenged by the Board's rejection of the offer, in particular the threat posed by their own personal interest in the decision.

Candidates would have performed better on this requirement had they focused their answers on the main ethical principles challenged, rather than trying to apply all of the ethical principles to the decision. Candidates must learn when to apply a particular area of knowledge and not to waste time on unnecessary theory.

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 risks to Evestar and its shareholders of a breach of confidence over the acquisition discussions. The second aspect of this task required candidates to consider how Evestar could tell if IndTV was offering a good deal once its acquisition terms were announced.

### **Risks of a breach of confidence**

This part of the section was reasonably well answered although most answers focused largely on risks to Evestar as a business rather than its shareholders. Most candidates discussed a range of relevant risks to Evestar, including the impact on its share price, the risks to the bid overall and the impact on staff. However, few candidates considered in detail the impact on the shareholders in terms of share price fluctuations, uncertainty in the market and the impact of shareholder confidence in the Board. However, overall most candidates provided a reasonable range of risks which were well applied to Evestar.

### **How can Evestar tell if IndTV is offering a good deal**

This requirement was not well answered. Most candidates seemed to have difficulty interpreting what was required. Most candidates correctly attempted to present a combined value of the business and a calculation of Evestar's percentage ownership of this combined entity. However, the majority of candidates then went on to present a detailed description of a range of valuation methods such as Price Earning, Dividend Valuation and NPV. Although some marks were awarded for these, this is not what the requirement asked for. Many answers were theoretical and descriptive rather than evaluating the deal being offered by IndTV. However, most candidates did recognise the need to consider synergy when combining the two entities.

Overall Section 2 was not answered well by most candidates.

### **Section 3**

Section 3 required candidates to respond to comments made on a shareholder blog site.

Section 3 had four main sub-tasks. Firstly, candidates were asked how to respond to allegations that all of Evestar's programmes are the same. Secondly, candidates had to present advice on the threat that the government may introduce more regulation in the making of reality TV programmes. Thirdly, if Evestar were to be taken over by IndTV, how would it go about measuring Evestar's performance. Finally, candidates were asked to make recommendations for safeguards for Evestar's programme buyers to overcome fears that the link to IndTV may cause them harm.

### **Allegations that all of Evestar's programmes are the same**

This part was not well answered. Many candidates merely refuted the claim by listing out all of the current programmes and highlighting the differences between them. This was a very narrow approach and did not take into account the need to show a measured and balanced approach to the allegation. Candidates should have also taken into consideration the concerns of the blogger and made it clear that Evestar would take into account these allegations and respond positively if there was a genuine concern. Candidates must make sure they provide a balanced answer, particularly when responding to stakeholders.



### **Threat of more government regulation of reality television**

This second requirement was answered well by most candidates. Most answers covered a range of points to address this risk, such as working with the government, being proactive and ensuring full compliance with government regulations, enhancing Evestar's own risk management policies and updating the risk register in relation to safeguarding contestants' welfare. Overall, answers were well considered and addressed the requirement in this part of the task.

### **How would IndTV measure Evestar's performance if it was a subsidiary**

This requirement was answered reasonably well. Most candidates used the balanced scorecard to structure their answer which was appropriate. Most candidates also presented a reasonable range of applied performance measures including advertising revenues, viewing figures and new programmes developed. However, weaker answers were those that presented unexplained lists of performance measures and those which were largely generic measures not directly applied to measuring the performance of Evestar. However, overall most candidates did present a reasonable range of suitable performance measures.

### **Safeguards to reassure potential programme buyers of Evestar's relationship with IndTV**

This part of the task was not well answered. Most candidates presented very thin answers which said little more than setting out strict contract terms and confidentiality agreements. As is often the case, candidates seemed to 'run out of steam' by the time they reached this final requirement of the examination and answers were often very thin and not well explained. Candidates must remain focused and put in as much effort on this final requirement as with all of the other requirements attempted.

Overall, section 3 was answered reasonably well but few answers were good across all four tasks.

**Variant 3**

	<b>Designed to test ability to:</b>	<b>Competency being tested:</b>	<b>Syllabus lead learning outcome:</b>
<b>Section 1</b>	Evaluate ethical dilemma	Leadership skills	E3 A2a - evaluate ethical issues and their resolution within a range of organisational contexts
	Evaluate relevance of portfolio theory to shareholders	Technical skills	F3 C2a – calculate the value of a whole entity (quoted or unquoted), a subsidiary entity or division using a range of methods
<b>Section 2</b>	Recommend approach to exploiting data set using Big Data	People skills	E3 E2b - Evaluate the strategic and competitive impact of information systems, including the potential contribution of Big Data
	Recommend approach to an internal audit investigation	Business skills	P3 C3a - evaluate the effective planning and management of internal audit and internal audit investigations
<b>Section 3</b>	Evaluate concerns over the founder being both CEO and Chairman	Leadership skills	P3 B3a - Evaluate the risks associated with poor governance structures
	Evaluate proposal to have that individual step down from one of those roles	People skills	P3 B3a - Evaluate the risks associated with poor governance structures
	Evaluate benefit to the company of the CEO/Chairman's involvement in an outside company	Business skills	F3 A1a - Advise on the overall strategic financial and non-financial objectives of different types of entities
	Evaluate information concerning share price movements	Technical skills	F3 C2b - Evaluate the validity of the valuation methods used and the results obtained in the context of a given scenario

## Comments on performance

### Section 1

#### Ethical issues

Most candidates did quite well on the first requirement, with the better candidates taking a methodical approach and commenting on each of the relevant ethical points in turn and in some cases providing the counter argument about the perceived problem arising from the nature of game shows themselves.

#### Risks

The second requirement was less well done, with many candidates confusing systematic and unsystematic risks. Most candidates recognised that the assertion concerning unsystematic risks was incorrect, but many of those failed to offer a logical argument to support that position.

### Section 2

#### Potential benefits of using Big Data

Generally candidates recognised the value of Big Data and made appropriate comment on a number of different elements of the data. Stronger answers developed the points raised to evaluate the benefits to How Music in terms of increased revenues and the identification of acts that should be promoted in response to their potential popularity.

#### Key areas for Audit investigation

Answers to the second requirement often stated audit tests, without explaining how they might address the problems in the scenario. Stronger answers identified the concerns and explained how they could be used to enable the Board to respond to the allegations that the voting system was inaccurate.

### Section 3

Overall, this section was well done with most candidates making appropriate and relevant comments in respect of each element of the question.

### **Defence of apparent breach of Teeland's Code of Corporate Governance**

Candidates often argued that it was undesirable for the same person to be both CEO and Chairman. While that is generally the case, stronger answers also identified the benefits enjoyed by Evestar due to Denny's involvement in both roles. While there will always be concerns when a single individual is both CEO and Chairman, this is an unusual situation because of Denny's background and reputation.

### **Stepping down from one role only**

The question of Denny stepping down from just one role was generally answered in a realistic manner, with candidates understanding that such a move would probably be artificial.

### **Shareholder benefit**

Candidates appreciated that Denny's work with other companies that are not formally part of Evestar may have assisted in the development of the company's programming.

### **Lack of effect on share price**

Finally, the interpretation of the market's weak response to the suggestion of Denny's departure was generally realistic and demonstrated an understanding of the concept of market efficiency. Some candidates did offer an unduly detailed summary of the different forms of efficiency that could be inferred from the efficient markets hypothesis.

**Variant 4**

	<b>Designed to test ability to:</b>	<b>Competency being tested:</b>	<b>Syllabus lead learning outcome:</b>
<b>Section 1</b>	Evaluate capabilities required to implement strategy	People skills	E3 B2a - evaluate strategic analysis tools
	Evaluate currency risks associated with overseas investment	Technical skills	P3 D1a - evaluate financial risks facing an organisation
<b>Section 2</b>	Evaluate the use of debt finance for a project	Business skills	F3 B1b - evaluate and compare alternative methods of raising long-term debt finance
	Evaluate alternative approaches to managing performance of an SBU	Leadership skills	E3 D1a - evaluate alternative models of strategic performance measurement in a range of business contexts
<b>Section 3</b>	Evaluate ethical behaviour associated with creating a programme	People skills	P3 A3a - evaluate ethical, social and environmental issues arising from risk management
	Recommending approach to managing welfare of employees	Leadership skills	P3 A2a - recommend techniques that will enable the board to discharge its responsibilities with regard to managing risks
	Recommend approach to valuation of business entity	Technical skills	F3 C2a - calculate the value of a whole entity (quoted or unquoted), a subsidiary entity or division using a range of methods
	Evaluate potential market reaction to a proposed divestment	Business skills	F3 C1a - evaluate the financial and strategic implications of a proposal for an acquisition, merger or divestment

## Comments on performance

### Section 1

#### **Capabilities that Evestar will have to possess or acquire in terms of managing the project and working with foreign television companies**

A wide range of capabilities could be identified here and many candidates answered this section extremely well, scoring high marks. Some weaker answers were focussed on whether or not the project should go ahead, which is not what was asked. These answers tended to drift into the advantages and disadvantages of the proposal rather than the capabilities needed. Some also used the suitability, feasibility, acceptability model which was not really a good fit for this requirement and tended to lead candidates to discussing topics which were not really relevant here, rather than identifying the capabilities as they were asked to do.

#### **Whether Evestar can mitigate the currency risks associated with the new venture by working in T\$ wherever possible**

Answers to this section tended to be much briefer than those for the first requirement, either because of poor time management or because candidates found this topic harder to discuss. Better candidates correctly identified, for example, that this approach would pass the currency risk on to the buyers, who might well be unwilling to accept it. Some candidates produced lists of potential methods for hedging currency risks without relating these to the specific scenario.

### Section 2

In Section 2 candidates were asked to discuss funding for the project, as the Board had decided not to raise any additional equity. They were also asked to explain the issues associated with evaluating the performance of the Marooned SBU and its management.

#### **Implications of seeking to fund the project by raising a secured loan of T\$70m**

This section was generally reasonably well attempted, with candidates discussing the impact on Evestar's gearing, the availability of appropriate security and the cost of the debt. Many made good use of the pre-seen material and illustrated their answers with gearing percentages and finance charges.

#### **Evaluating the performance of the SBU and its management**

Again, this was generally well answered, although candidates tended to put most emphasis on evaluating the performance of the management, with many ignoring the SBU. Some drifted away from the requirements by discussing change management issues, team building etc.

### **Section 3**

Candidates were asked to address four separate issues:

#### **Whether the board could be accused of acting unethically**

A wide range of points were possible here and many candidates provided good answers to this.

#### **Controls that could have been put in place to have prevented the abuse**

Again, this section was often well answered although some candidates made suggestions which could not really be defined as controls.

#### **How Evestar could go about valuing Marooned as a business entity**

Whilst there were many good answers to this section, some candidates provided “textbook” lists of possible valuation methods without applying them to the scenario or demonstrating an understanding of which methods would actually be appropriate here.

#### **How shareholders would respond if the divestment were to go ahead**

Some answers to this were very brief but many provided good balanced discussions of the possible reactions by shareholders.

**Variant 5**

	<b>Designed to test ability to:</b>	<b>Competency being tested:</b>	<b>Syllabus lead learning outcome:</b>
<b>Section 1</b>	Evaluate strategic benefits of acquiring another company	Business skills	E3 A1d - recommend how to build and manage strategic relationships with stakeholders
	Recommend approach to financing acquisition	Technical skills	F3 C3a - evaluate alternative pricing structures and bid process
<b>Section 2</b>	Recommend approach to setting strategic targets for senior manager	Leadership skills	E3 D1b - recommend solutions to problems in strategic performance measurement
	Evaluate governance issues associated with public profile of CEO/Chairman	People skills	P3 B3a - evaluate the risks associated with poor governance structures
<b>Section 3</b>	Recommend approach to the valuation of an entity	Technical skills	F3 C2a - calculate the value of a whole entity (quoted or unquoted), a subsidiary entity or division using a range of methods
	Evaluate potential synergies of acquisition	Business skills	F3 C3b - evaluate post-transaction issues
	Evaluate relevance of control environment	People skills	P3 A2a - recommend techniques that will enable the board to discharge its responsibilities with regard to managing risks
	Recommend approach to an internal audit investigation	Leadership skills	P3 C3a - evaluate the effective planning and management of internal audit and internal audit investigations



## Comments on performance

### Section 1

#### Risks and benefits

This was relatively well done with most of the main points being covered - there was a reasonable grasp of the implications of buying a new station and the understanding of the various financing methods was also acceptable.

Candidates should have recognised that Evestar produces only a very limited range of programmes. It is debateable whether it is capable of filling a full broadcasting schedule, which makes the identification of risks and benefits rather more challenging.

A good answer reflected the nature of the industry and Evestar's position.

#### Shares v cash

Candidates recognised that the target company is very much smaller than Evestar, but it does have a valuable asset in the form of broadcasting rights.

A good answer would have explored the merits of using both shares and cash and should have justified the selection of one or the other. Candidates were free to select either, with the credit being offered for the arguments in support rather than the conclusion in and of itself. Many candidates did make reasonable arguments for using a mixture of shares and cash which was excellent.

### Section 2

#### Targets

This was less well done with hardly any mention of stretch targets and most candidates simply stating that Balanced scorecard was the preferred approach outlining the basic features of the model with little analysis of targets and KPI's that would be useful in this scenario.

Candidates should have justified their suggestions for targets. The new Head of Advertising has to be challenged so that she is motivated to perform well, without any dysfunctional behaviour on her part.

Good answers should have recognised that this is a transition phase for the new line of business and so the focus should be on developing opportunities rather than necessarily delivering short-term revenues. There were few really good answers to this task. Most candidates ignored the issue of stretch targets altogether.

### **Stepping down as judge**

The second element of Section 2 was again only partially covered with very little thought being given to the Governance elements obvious in the task outline.

Candidates should have thought widely about the factors that might be used to evaluate the performance of the CEO. This required some consideration of the CEO's role and so they should have focussed on performance indicators that offered some insight into the strategic management offered by the CEO. Very few candidates discussed the governance aspects of Denny stepping down as a judge, which was disappointing. This meant that candidates received very poor marks as they failed to answer what was asked.

Any indicators that were justified by the candidate were accepted. There were some sensible indicators suggested by many candidates which was very good.

### **Section 3**

This task is essentially two pairs of linked requirements. They are presented as four separate requirements.

#### **Valuation**

The project could only proceed if Evestar can buy Teeland Fishing and that required a realistic valuation, otherwise the purchase will either fail or Evestar will overpay. The company's present business model probably restricts its value as a going concern, but its present shareholders will also be aware of the potential to broadcast more popular programmes. Valuation may have to allow for the value of the broadcasting rights. There were significant gaps in this section with no consideration given to the selling company's views on valuation. Candidates were able to discuss various valuation methods but with almost no thought of the context of the case study. Limited marks were available for this discussion unless applied to the case.

#### **Synergies**

Candidates should have been realistic about the nature of the synergies that are on offer. The key synergy will be obtained from Evestar's ability to broadcast programmes. Provided the acquisition proceeds, there will be very little to interfere with that occurring. A good answer should have reflected the nature of what is being acquired and the fact that Evestar was not looking for anything that is at risk because of problems of integrating the two businesses. This part was answered quite well with candidates talking about the different viewers interests briefly and then discussing the broadcasting.

#### **Control environments**

Good answers should have reflected the different sizes of the two companies, the fact that one was quoted and the other was not and the fact that one is almost a "hobby" business for its founders whereas the other was clearly a commercial enterprise. This

question and the next one on audit were not answered very well. Candidates did not seem to come up with any ideas on the differences between the two companies and how this could have affected the control environment.

### **Audit**

Candidates had to recognise the features of the control environment so that they could recommend the approach that the internal auditor should take to documenting it. Good answers would have suggested ways to determine whether Teeland Fishing has a satisfactory control environment and would have gone beyond merely documenting the control environment. This was also answered badly with candidates not really thinking about the control environment and how it could be documented and therefore failing to explain how the audit should be planned and what areas to focus on.

There were some very poor answers to this section.