

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

General comments

This paper was based on a pre-seen scenario which described a company in the computer hardware manufacturing industry. The scenario was made available in advance of the exam and five variant papers were set, each presenting additional scenario-based information and setting four tasks to be completed. Each task was split into two or three specific elements.

The industry is interesting and information on this industry is widely available.

Overall, the standard of answer presented was similar to the May 2016 case study; there were many very short and incomplete solutions. As with previous case studies, the strongest answers were properly applied to the scenario. The main difference is that candidates appear to be getting weaker in technical accounting and stronger in general management. Candidates must be better prepared in technical accounting areas in the future.

There were some very short answers to the case study and some candidates did not seem to know much about the industry or the company. Given that the pre-seen material had been available for several weeks prior to the exam, this was disappointing. There were also answers which had been learned and even though the question was different just wrote a prepared answer which was not related to the unseen case at all.

Some candidates demonstrated an alarmingly poor understanding of several important syllabus areas, such as the accounting standards, transfer pricing, ethics, rights issues and even NPV. This was clearly very disappointing. There were also some very good solutions where candidates were well-prepared and made excellent attempts at answering what was asked.

Summary

The standard of scripts varied widely in this session. There were some reasonably good scripts submitted by candidates who had clearly prepared well, made good use of the pre-seen material and were technically competent. At the other end of the spectrum were some very poor papers, where candidates had written very little, and did not always demonstrate understanding of the requirements. Many did not demonstrate adequate understanding of technical accounting issues. Some weaker candidates had clearly revised specific topics and were determined to work them into their answers despite the fact that they were really not relevant.

Variant 1

	Designed to test ability to:	Competency being tested:	Syllabus lead learning outcome:
Task 1	Discuss key cost questions	Technical skills	P2 (A1c) Discuss techniques for enhancing long-term profits.
	Discuss relationships with existing vendors	People skills	E2 (A1b) Compare and contrast alternative approaches to strategy development.
Task 2	Discuss risks arising from health and safety	Business skills	P2 (D2a) Discuss risk management.
	Evaluate impact of cultural values	Leadership skills	E2 (B2b) Explain the importance of organisational culture.
Task 3	Discuss issues associated with transfer prices	People/Leadership skills	P2 (B3b) Discuss transfer pricing systems.
	Recommend accounting treatment	Technical skills	F2 (B1a) Produce primary financial statements for a group of entities in accordance with relevant international accounting standards.
Task 4	Discuss potential share price impact	Technical skills	F2 (A2a) Calculate the cost of equity for an incorporated entity using the dividend valuation model. F2 (B4a) Produce the disclosures for earnings per share.
	Evaluate SWOT analysis	Business skills	E2 (A2a) Distinguish between different aspects of the global business environment, including the competitive environment.

Comments on performance

Task 1

Candidates were asked first to discuss key cost questions. A good answer should have brought out the estimates and assumptions that LMC has made in setting its selling price. Its prices are likely to be determined by sales volumes, which will have implications for bulk discounts from parts manufacturers and economies of scale in spreading fixed overheads. There will be other assumptions too. This question attracted a range of differing arguments, which was good to see, but many of the answers missed the main issues. Many candidates failed to discuss whether LMC allowed for the costs of shipping to a single major customer in Westland or to discuss volumes at all.

Candidates were next asked to make a realistic assessment of the need to maintain a good and steady relationship with vendors. It was crucial here for answers to reflect the nature of the business. SparkSpace owes no particular loyalty to any given vendor and the products themselves are generic. Competition means that vendors cannot really afford to turn away customers. Very few candidates answered these issues well. Many gave very generic answers which did not reflect the nature of the business at all. They just discussed how to keep good relationships in a general business sense.

Task 2

Candidates were asked first to discuss risks arising from health and safety. These risks should have been evaluated in terms of likelihood and impact. The suggested answer offers some scenarios, but candidates could have approached the problem in different ways provided they demonstrated some logic. Some candidates answered this well and discussed sensible risks, their likelihood and their impact. Others discussed obscure risks instead of the obvious ones and did not gain high marks. A significant number of candidates failed to discuss damage to reputation which should have been quite obvious.

Candidates were next asked to evaluate the impact of cultural values. The most likely argument is that imposing cultures and values will prove to be a costly failure. Candidates were, however, free to argue the opposite if they wish. Generally this part was answered well with candidates providing high-quality discussion of business culture.

Task 3

Transfer pricing is an important part of the syllabus and a topical area in practice. In this case, candidates should bear in mind that the transfer prices will affect the profitability of SDC, which is only partially owned by SparkSpace. The relationship between the three parties to this venture may determine some of the issues associated with transfer prices. Candidates demonstrated very poor

understanding of the detail of transfer pricing: the candidates appear to be much better at less technical management issues than the technical accounting areas of the syllabus. Many candidates failed to discuss arms-length pricing at all.

In the second part of this task, candidates were required to recommend an accounting treatment and should have justified their recommendation. It would probably be a joint arrangement, although alternative treatments may be justified and marks were awarded accordingly. Candidates should have explained how their chosen treatment will be reflected in the financial statements. This section of the variant was done very badly with few candidates realising it was a joint arrangement. They did get some marks for discussing the treatment is the investment even if they had made a wrong decision in the first section. Candidates demonstrated very poor F2 technical ability.

Task 4

Candidates were first asked to discuss the potential share price impact and should have been capable of explaining the relevance of each of the facts provided in the scenario. Answers should have focussed on the logic behind the models implied by the figures. Once again candidates demonstrated very little technical ability. The answers on rights issues and dividend growth in many cases were very poor. Few candidates discussed the main issue such as whether the shareholders would be happy with the rights issue and related that to the return which was expected. Candidates' discussions on NPV and share price were also weak.

The second part of this task – the SWOT analysis – should have covered each of the four elements in roughly equal depth. The candidates found it difficult to think of many strengths or weaknesses, which was surprising. Again the answers were fairly weak and very short. This seems to again show a lack of technical accounting knowledge and a lack of ability to apply that knowledge to practical issues.

Variant 2

	Designed to test ability to:	Competency being tested:	Syllabus lead learning outcome:
Task 1	Discuss commercial implications	Business skills	E2 (A1c) Explain the approaches to achieving sustainable competitive advantage.
	Discuss cost of quality	Technical skills	P2 (A1b) Evaluate total quality management (TQM) techniques.
Task 2	Discuss learning curve	People skills	P2 (A1d) Apply learning curves to estimate time and cost for activities, products and services.
	Evaluate performance	Leadership skills	E2 (B2a) Discuss behavioural aspects of management control.
Task 3	Discuss commercial risks	Technical skills	P2 (D2a) Discuss risk management.
	Evaluate impact on accounting ratios	Business skills	F2 (C1b) Evaluate the financial performance, financial position and financial adaptability of an entity based on the information contained in the financial statements provided.
Task 4	Account for warranty provision	Technical skills	F2 (B1c) Discuss the provisions of relevant international accounting standards in respect of the recognition and measurement of revenue, leases, financial instruments, provisions, share-based payments and deferred taxation.
	Advise on negotiation	People/Leadership skills	E2 (C2a) Discuss the roles of communication, negotiation, influence and persuasion in the management process.

Comments on performance

Task 1

Candidates were asked to address the competitive advantage which this proposal could offer SparkSpace. They were also asked to comment on the implications of this proposal from the perspective of SparkSpace's cost of quality. Many candidates addressed the first element of this task well, addressing wider issues in addition to the price advantage. Some produced quite generic answers, discussing competitive advantage generally – for example using Porter's five forces model – without relating their discussion to the specific issues raised by the case study.

Better candidates also attempted the second section well, with many using an appropriate structure of prevention, appraisal, internal and external failure costs. However, relatively few recognised the impact of the manufacture being carried out by a third party. Some weaker candidates produced general answers which talked about cost of quality but did not refer to the case study scenario.

Task 2

Candidates were required to advise on how best to determine the learning curve for test engineers for the new Powerblade, then to discuss the difficulties of establishing objectives for the new Powerblade quality control department and the impact on the subsequent performance of its manager.

For the first element, many candidates provided a general discussion on how to determine learning curves, with better attempts also discussing how field testing could help. Relatively few suggested discussions with the senior quality engineer.

The second element was generally well addressed, although there was again an issue with some candidates producing very generic answers about how performance can be evaluated without reference to the information presented in the case study.

Task 3

The third section of this variant asked candidates to produce a report on the major risks associated with tendering for contract to build a backup server for air traffic control using the Powerblade, then to identify and explain the likely impact on key accounting ratios.

Most candidates identified some appropriate risks, although many did not recognise that the client was air traffic control and that therefore an aviation accident was an important consideration.

Discussion of ratios was very disappointing; many identified ratios but did not explain the likely impact on them. Whilst comments on working capital ratios were generally sensible, many showed a lack of understanding of profitability ratios.

Task 4

The final section required candidates to discuss whether or not a provision should be created for future costs to be incurred under warranties, then to discuss how the negotiations with SparkSpace's auditors should be structured and what the ethical implications would be of threatening to replace the firm of auditors if the matter remained unresolved.

Whilst better candidates tackled the first requirement well, many showed a lack of financial reporting knowledge and failed to demonstrate knowledge of the relevant IFRS. Many did not explain how and why the provisions applied to this case, merely stating that SparkSpace should, or should not, make a provision.

Discussion of how negotiations should be conducted was sometimes very generic, explaining the process of negotiation without reference to the scenario presented. Some candidates saw no ethical barrier to threatening the auditor, but most recognised that this would breach the CIMA Code of Ethics.

Variant 3

	Designed to test ability to:	Competency being tested:	Syllabus lead learning outcome:
Task 1	Discuss criteria for optimisation	Technical skills	P2 (B1a) Discuss the information needed for decision making in different organisational structures.
	Discuss bargaining positions	People skills	E2 (C2a) Discuss the roles of communication, negotiation, influence and persuasion in the management process.
Task 2	Discuss ethical stance	Business skills	P2 (D2a) Discuss risk management.
	Discuss issues associated with corporate culture	People/Leadership skills	E2 (B2b) Explain the importance of organisational culture.
Task 3	Discuss implications of granting executive share options	Leadership skills	E2 (B2a) Discuss behavioural aspects of management control.
	Discuss impact of granting options for financial statements	Technical skills	F2 (B1c) Discuss the provisions of relevant international accounting standards in respect of the recognition and measurement of revenue, leases, financial instruments, provisions, share-based payments and deferred taxation.
Task 4	Discuss relevance of planning variances	Technical skills	P2 (B2a) Prepare performance reports for the evaluation of projected and actual performance.
	Discuss WACC	Business skills	F2 (A2c) Calculate the weighted average cost of capital (WACC) for an incorporated entity.

Comments on performance

Task 1

Candidates were asked to propose criteria for making optimal use of the few vital components available to Sparkspace, who had agreed to build eight large systems. The key to this question is that there is not a single criterion that can be used to resolve this dilemma. A significant minority of candidates suggested a simple analysis of contribution per component and maximising the total contribution. That approach rather misses the point that it will be possible to build all eight systems eventually. The key question is in terms of ranking priorities in a manner that optimises Sparkspace's position.

There were some basic and obvious points that were frequently overlooked. For example, if Sparkspace has insufficient parts to complete a large contract then there is little point in proceeding with that contract. There would be some merit in establishing the various permutations and combinations of contracts that could be completed. There were further commercial issues that could have been explored but the basic problem was that answers tended to oversimplify the optimisation exercise.

Task 2

Answers to this task were generally better, with a more realistic response to the requirement. Candidates were asked to respond to the argument that the board had acted unethically in permitting the company to become entirely dependent on a single supplier. This allegation could be supported by arguing that there had been a lack of competence. Most candidates were able to make a realistic case for Sparkspace's willingness to rely on this one supplier and that was the key to answering this question.

Some candidates argued that the board had been reckless, which was also acceptable provided the basis for this claim was logical. Perhaps Sparkspace should not be in this market because it is so difficult to guarantee the completion of projects due to the excessive reliance on a single supplier. Conversely, arguments that an alternative supplier should have been found were not particularly relevant to the question because it is clear that there were none.

The discussion of the task culture was generally well informed with respect to the benefits of task cultures, but said relatively little about the implications of that culture to Sparkspace.

Task 3

This task focussed on the question of executive stock options, with a suggestion being made that the board should be required to accept options in place of a portion of salary.

The first requirement dealt with the question of the motivational effect of stock options. Answers here were generally weak, with relatively little thought being applied to the situation. Many candidates asserted that options would align the board's interests with those of the shareholders, but did not elaborate further. There were, for example, issues associated with whether it would truly benefit the shareholders to expose the directors to risks such as the unforeseen events arising from the fire. There were further issues associated with the need to make the options a significant part of the remuneration package and whether or not the directors would tolerate such a scheme.

The second part of this task required a fairly generic discussion of the accounting treatment of stock options; unfortunately this was also answered poorly. Candidates wrote very little about how the options would be accounted for and were, therefore, struggling to explain how the use of options would affect the financial statements. Many candidates showed a complete lack of technical skill relating to F2.

Task 4

This task dealt with the ongoing management of Sparkspace in the aftermath of the fire, both from the perspective of management and the shareholders.

The first part of the task dealt with planning vs. operational variances by offering a report that made no attempt to filter out the impact of the fire. Very few candidates discussed the possibility that the variances were difficult to interpret unless the effects of the fire were isolated. For example, the so-called favourable underspend on parts was attributable to a failure to complete contracts.

By this stage of their studies, candidates should be prepared to identify the shortcomings of reports and the threats that they may be misleading.

The second part of this task, dealing with the possible shareholder concerns about ongoing reliance on a single supplier, generated some better answers, however some candidates omitted to discuss the implications of an increase in cost of capital.

Variant 4

	Designed to test ability to:	Competency being tested:	Syllabus lead learning outcome:
Task 1	Apply target costing	Technical skills	P2 (A1c) Discuss techniques for enhancing long-term profits.
	Advise on team membership	People/Leadership skills	E2 (C1a) Evaluate the issues associated with building, leading and managing effective teams. E2 (B2a) Discuss behavioural aspects of management control.
Task 2	Account for intangible assets	Technical skills	F2 (C1b) Evaluate the financial performance, financial position and financial adaptability of an entity based on the information contained in the financial statements provided.
	Communicate with shareholders	Business skills	E2 (A1c) Explain the approaches to achieving sustainable competitive advantage.
Task 3	Advise on consolidation of foreign subsidiary	Technical skills	F2 (B2b) Demonstrate the impact on the group financial statements of consolidating a foreign subsidiary.
	Discuss impact of foreign currency on transfer pricing	Leadership skills	P2 (B3b) Discuss transfer pricing systems.
Task 4	Discuss ethical stance	People skills	E2 (C2b) Discuss approaches to managing conflict.
	Discuss commercial risks	Business skills	P2 (D2b) Discuss the risks associated with the collection and use of information.

Comments on performance

Task 1

This task focussed on setting up new plant and production line for manufacture of Graphmark Blade server.

Candidates were first asked to comment on the problems and opportunities presented in applying target costing and this was generally well-answered. A number of candidates gave good answers highlighting trimmed design before production is commenced and indicating that there may be a significant trade off with subsequent quality. However a significant number displayed a lack of understanding of the finite floor costing of products involving raw material input and thought that sourcing cheaper raw materials is the only answer rather than simplifying design and automating parts of the assembly or build.

Candidates were then asked to recommend the composition of a team and basis for their evaluation. This generated some very mixed responses. Many candidates thought that this would be a good training ground for new starts, which was incorrect. Many candidates quoted Belbin roles rather than practical issues. Again most students went down the balanced scorecard route without too much practical knowledge of the component elements relative to this scenario.

Task

2

This task focussed on the board's assessment of Graphmark's projected production costs and criteria for shareholder communication.

Candidates were first asked to consider the impact of the outlay on final development work and investment in PPE. The more capable candidates immediately grasped the requirements to differentiate capital vs. expense, though many glibly capitalised expense prior to the board decision! Very few gave any real thought to the source of funds nor the lag before revenues flow, so there would be some potential start up disasters. However, the stronger students recognised the delay before funds flow and the need to divert cash from somewhere, probably shareholders.

In the second part of this task (factors to communicate to shareholders on Graphmark and its potential for the future profitability of Sparkspace), candidates usually grasped the need to inform the shareholders in view of future profits although few highlighted the immediate funds flow issues and the fact that these should not be problematic. Better candidates highlighted Apple's lack of dividends in favour of share appreciation. Overall there were a disappointingly low number of good answers. Very few capitalised on the differentiation afforded by Graphmark and the exclusivity in the market.

Task 3

In this task, candidates were asked to consider the impact of the decision to outsource production of Graphmark.

The first part, where candidates were asked to comment on the potential impact of currency movements on consolidated financial statements, was very poorly answered. The better students gave a good account of goodwill, net assets and profit and the timings of translation and position on the financial statements. However, the majority of students failed to give more than a scant account of some of these elements. Many candidates failed to mention goodwill or the ongoing translation required every year with changes being posted as currency gains or losses, although most grasped profit taken as an average through the year.

The second part of this task (transfer price considerations, impact on motivation and decisions on assembly location) was rather better-answered; the simple calculations showed predominantly that it was better to import than make at home but many chose to appease Westland management by making them there. However, there was reasonable treatment of alternative transfer price considerations and the relative effect on morale on both parties.

Task 4

The final task of variant 4 focussed introduced an ethical dilemma regarding the potential misuse of advanced technology in the case of Graphmark for facial recognition. Candidates were first asked to respond to the ethical dilemma of selling equipment capable of being put to immoral use. There were many reasonable answers pointing out that it is not the sale of the equipment which is the problem but the uncontrolled use to which it is put that is at fault here. The better candidates then drew comparisons with other products which are controlled or sold with safeguard warnings. Some excellent answers drew on wide ranging precautions, highlighting proper actions to be taken by Sparkspace, including consulting with government security to create a more controlled environment. Many candidates highlighted the ethical dilemmas faced by the football club mentioned in the article and questioned their right to publish and name without explicit permission. This is a wide-ranging ethical dilemma in the digital age and on the whole there was a pleasingly encouraging understanding of the position.

The second part of this task (a discussion of the risks arising from sale of the product) was not so eloquently argued, many candidates adopted a knee-jerk reaction and took draconian measures or insisted on impossible checks on intended future use highlighting that sales would be adversely affected. Most saw the need to create a distance between the sale and the improper use. There was a very wide range of ideas as to how this might be achieved.

The better candidates saw the opportunity for free marketing and publicity which if coupled with sensitive addressing of the potential down side could be used to create real opportunity.

Variant 5

	Designed to test ability to:	Competency being tested:	Syllabus lead learning outcome:
Task 1	Discuss commercial implications of no-profit contract	Business skills	E2 (A1c) Explain the approaches to achieving sustainable competitive advantage.
	Discuss dysfunctional behaviour	Technical skills	P2 (B1a) Discuss the information needed for decision making in different organisational structures.
Task 2	Discuss shareholders' perceptions	People skills	F2 (A1b) Discuss the markets for and methods of raising long-term finance.
	Discuss proposal for motivation of sales staff	Leadership skills	P2 (B3a) Discuss the likely behavioural consequences of performance measurement within an organisation.
Task 3	Discuss potential benefits of merger	Business skills	E2 (A2b) Discuss the approaches to competitor analysis including the collection and interpretation of trend data.
	Discuss goodwill valuation	Technical skills	F2 (B1a) Produce primary financial statements for a group of entities in accordance with relevant international accounting standards.
Task 4	Discuss business risks	Technical skills	P2 (D1b) Analyse risk and uncertainty.
	Discuss change management	People/Leadership skills	E2 (D1a) Discuss the concept of organisational change. E2 (D1b) Recommend techniques to manage resistance to change.

Comments on performance

Task 1

Candidates were asked to discuss commercial reasons for bidding on a contract which would make zero profit. This seemed to be a straightforward and clear question but many candidates seemed to misinterpret the question and answered a different question.

Where candidates did understand the requirement there were many very good responses, often discussing five or six benefits, whereas weaker candidates would only mention a couple which would usually be either something to do with reputation or branding and being able to either get further contracts with the customer or supplying maintenance (at a higher margin). Also with weaker candidates the points made were often too brief so they were not able to access higher marks.

Candidates were next required to discuss if having a narrow performance indicator on revenue for the sales department was appropriate. Most candidates seeing the word 'performance' moved the answer as quickly as possible to a discussion of KPIs and the need for a balanced scorecard approach with financial and non-financial indicators. There were very few good answers to this part as candidates often did not answer what was asked.

Task 2

Candidates seemed to be a little confused over the question asked in the first part of this task, which was to explain whether or not the low profit margins would be of concern to shareholders. Weaker candidates tended not to discuss shareholders at all but simply provided ideas of how margins could be improved: TQM/JIT, value analysis etc were discussed. While this did get some credit, ignoring the part about shareholders meant that students could not access those marks at all. There were also some excellent responses that discussed the fact that low margins were the norm for this type of industry and so there should be an expectation of this from the shareholders, which would be built into the share price. Some candidates also discussed Mendelow's matrix and the importance of communication but they often gave details of all stakeholders when the question was clearly geared to shareholders only so too much time was spent here giving irrelevant details.

In the second part of this task, candidates had to evaluate the suggestion to make sales staff redundant. Many candidates did not seem to understand the word 'evaluate', so all they did was discuss the disadvantages of making staff redundant.

Additionally, many candidates discussed things that were not really so relevant such as strike issues, unions, when staff could be made redundant, consulting staff, involving HR and acting ethically so there was too much on the process of making people redundant rather than evaluating the suggestion.

Task 3

Candidates were asked here to discuss the advantages and disadvantages of investing in Techrunn. The requirement was clearly set out and candidates did provide both advantages and disadvantages and tended to score highly for this section. The difference between scripts was really down to the quality of the discussions and quantity of advantages and disadvantages given.

The second part of this task (identification of the main challenges associated with the calculation of goodwill on the acquisition of Techrunn and suggestions about how those might be overcome) was generally very poorly answered, with many candidates just explaining what goodwill was (in terms of difference between consideration NCI and assets) and that assets would be difficult to value without any explanation. Again, candidates did very badly on the F2 content of the case study, giving very weak answers.

Task 4

Candidates were asked to discuss how the use of expected value did not fully consider the options available, and why it should be ignored. Candidates were reluctant to give any theory about expected value except to state that it was the NPV multiplied by the probabilities and that non-cash items were excluded from the NPV – for many weaker candidates, this then formed the basis for their discussion as to why the expected value should be ignored, as they felt that the figures would be severely understated due to not including depreciation on what would presumably be a large value of assets. The very weak candidates did little more than just list the NPV for each level of demand and each option, adding nothing to the discussion other than what was in the exam question.

Better candidates then also provided a broader look at the problems of keeping both plants open or relocating in terms of practical issues so expanded the discussion away from just the expected values. Some of these were very good, with candidates discussing issues with different work cultures, capacity problems, etc.

Candidates were finally asked to discuss change management issues, which most scored fairly well at. Where candidates differed in the marks achieved was due to a lack of explanation provided, with some candidates stating that staff would be resistant to change without giving any further elaboration, which wasn't really evaluating the problem.

The majority of candidates also only considered change management in terms of the staff (although there were plenty of high marks available for candidates just focusing on staff), so it was good to see the better candidates also discussing the problems of relocating the equipment too as part of the process.

Tips for future candidates

There are a number of key points to take into account when preparing for future management level case study examinations, as follows:

- Candidates must be able to demonstrate their technical accounting skills. Many candidates appeared weak in this area, especially in F2.
- Candidates must make better use of the opportunity to gain familiarity with the pre-seen material. It is not necessary to memorise the material or to become an expert in the industry, but candidates should develop an understanding of the business.
- Questions give explicit instructions as to what is required and marks will not be awarded for anything that has not been requested. In particular, essays on the theory underlying the problem at hand are unlikely to score well if the question asks for a response to a particular issue arising from a scenario.
- Candidates should remember that all sections of tasks are equally weighted.
- With the time constraints in place, candidates can only spend a limited amount of time on each task. Therefore it is essential that candidates focus on making the points that they are most confident of before they run out of time.