

INSTITUTE OF CHARTERED ACCOUNTANTS OF PAKISTAN

EXAMINERS' COMMENTS

SUBJECT	SESSION
Cost and Management Accounting	Certificate in Accounting and Finance – Autumn 2014

General:

It was a balanced paper with a good mix of easy, moderate and difficult questions. However, the overall performance in the paper was about average. This was probably because of the fact that one of the easiest questions on job order costing was poorly attempted.

Question-wise comments:

Question 1

This question required preparation of process account of Cooking Department of a food processing company. As is usual, the key issue was to calculate the process loss and bifurcation thereof between normal and abnormal loss. In the given situation, the normal loss required further bifurcation between loss due to cooking and loss due to rejection.

The performance was just about average as majority of the students seemed familiar with the overall process but made various mistakes in the calculation and treatment of process losses. Some of the frequent mistakes are enumerated below:

- Total loss was calculated on the material input during the month only. Since opening work in process was only 50% complete as regards conversion and the inspection takes place when it is 80% complete, hence, loss should have been calculated on the opening work in process as well. Further, no loss should have been computed on the closing stock as it was only 65% complete.
- Normal loss was not bifurcated between weight and rejection losses and in most such cases, disposal of rejected nuggets was ignored.
- Normal loss was also included in equivalent production.
- In arriving at the equivalent production, the fact that abnormal loss quantity was only 80% complete as regards conversion was ignored and entire quantity of abnormal loss was included in equivalent production as regards conversion cost also.
- Inventory was valued using FIFO method instead of average cost.
- Some students ignored the applied overheads.

Question 2

This was a straightforward question in which existing break-even sales, margin of safety and contribution margin percentage were given. The question also provided information about certain proposed measures and the impact thereof on the financial performance of the company during the next period. The requirement was to:

- (a) Prepare profit statements under current and proposed scenarios and;
- (b) Compute break-even sales and margin of safety as a result of taking the proposed measures.

Overall performance in this question was average. For the existing situation, most of the students computed the sales correctly by adding the breakeven sales and the margin of safety. Almost all students correctly calculated the variable costs as 80% of sales and the fixed costs by multiplying the break-even sales with contribution margin percentage.

However, various errors were noted in calculating the figures for the next period. Some of these are enumerated below:

- Impact of 5% decline in sales price was determined by dividing the sales under existing scenario by 1.05 instead of multiplying it by 0.95.
- Only about half the candidates were able to compute the variable costs correctly as the remaining candidates calculated it by multiplying the sale with 70%. The students need to understand the difference between 10% decline in variable cost percentage and 10 % decline in cost per unit.
- A significant number of candidates did not take into account the interest on loan, in the computation of break-even sales.

Question 3

A poor performance was witnessed in this question which required computation of NPV of a project. A number of errors were observed. The most common among them are as follows:

- Majority of the students ignored the fact that installation of plant was to be completed in one year and hence the cash flows were to be computed for Year 0 to 6. Instead, they determined cash flows for Year 0 to 5.
- A significant number of candidates did not understand the concept of Year 0 and took outflows pertaining to Year 0 in Year 1.
- Instead of its market value, cost of land was taken as outflow.
- Market value of land at the end of the period of five years was ignored.

Question 4

This question on variances was straightforward and most of the students attempted it well. Some of the common errors are as follows:

- Many students could not compute the actual material cost correctly as they deducted the unfavourable variances from the standard cost instead of adding them. Some students did not attempt it altogether.
- Many students could not correctly bifurcate the total overhead rate per labour hour into fixed and variable portions and consequently, made errors in the computation of variances.

Question 5 (a)

A mixed response was seen in this 3 mark theory question. A large number of students scored full marks whereas few students did not attempt it altogether. However, it was noted that those who secured full marks in this part, performed much better in the second part as well.

Question 5(b)

This was a difficult question and required good understanding of the concept involved in make or buy decisions as well as in determining the optimum production plan in a situation where production capacity is limited and each product can be produced as well as purchased from outside suppliers.

The answer involved the following key steps:

- Determining the variable cost of production of each product.
- Dividing the difference between the discounted cost of imports and the variable cost of production by number of production hours to determine the order of ranking. (The same result could have been obtained by dividing the difference between the contribution margin of own produced and imported units by the number of production hours but it was a slightly lengthy method)
- Preparing optimum production plan from the available production hours based on the order of ranking.

Most of the students performed poorly in this question as they started making calculations without a proper plan. As could be seen from the steps described above, the key step was to determine the ranking and that is where most students erred as they failed to use the appropriate basis for the ranking. A large number of students used the following basis for the purpose of ranking:

- Discount offered.
- Discount offered divided by production hours per unit.
- Import price after discount or import price after discount divided by production hours per unit.
- Contribution margin on internally produced goods divided by production hours per unit.

Question 6

It was a simple question requiring journal entries based on job order costing. Probably because such questions are not tested frequently, the performance was much below the expected level. The basic entries for charging materials, labour and overhead costs to WIP of respective jobs were correct in majority of the answers. However, majority of the students made errors in the entries related to closure of applied FOH, recording of damaged goods and consequential loss and transfer of WIP to finished goods.

Some students prepared t-accounts which were not required.

Question 7(a)

This part required brief description of some of the very elementary cost accounting concepts but was not very well-answered. Almost 50% of the students gave incorrect examples.

Question 7(b)

This was the easiest question of this paper. It required calculation of absorption rate. Cost was to be allocated to all departments based on relevant drivers and thereafter, service departments' cost was to be allocated to the products.

Most of the students performed well in this question. However, some of the common mistakes are mentioned below:

- Many students did not allocate the service departments' costs to the products.
- A significant number of students did not understand the repeated distribution method and allocated the service departments cost in one step i.e. to the products only.
- Many students included the direct material and direct labour costs in the overheads.

THE END