



How to pass the exams!

Sample marking exercise

CT2 April 2005 question 2: Sample solution with comments

- (i) Price/ earnings ratio = P/E ratio
= market value of ord shares / earnings per share

Value of company
= P & L profit x P/E ratio
so is good indication of value of company

Net assets figure
= all assets – all liabilities
taken from balance sheet
so is what company is worth as it stands
but may be distorted because of accounting practices **(1)** and this could be true for the other measure too **(1)** which takes an ongoing view.

Comment

Too much bookwork knowledge which is not directly answering question; poor/ no planning; time wasted on bookwork; some good points identified but not expanded; some terms unclear. Just not enough information here for the marks.

How to improve

Don't just regurgitate the bookwork. Answer the specific question so here the student must explain the relevance of the two methods, not just write down a formula saying what they are.

Write points clearly so the examiner can see you understand what you are saying.

Make sure you have written enough for the marks on offer. Write too much and you use up time – not enough and you lose marks.

- (ii) First measure gives a much higher valuation **(1)**.

Comment

Only part of question answered; not very clear

How to improve

Keep points clear, so instead of “the first measure” say “The P/E ratio model” to be absolutely clear what you’re referring to.

Answer the whole question – it said “indicate, with reasons”, so you need to give reasons for your choice.

- (iii) The financial statements are made up of:
- A balance sheet showing the financial position on the last day of the company's financial year
 - A profit and loss account for the financial year
 - Detailed disclosures which are normally presented as a series of notes to the accounts
 - A directors' report
 - An auditor's report

These must give a true and fair view (**equivalent 1**) and be signed off by an auditor and follow accounting standards and use lots of accounting concepts eg cost concept, money measurement concept, going concern concept.

If the auditor does not agree he will issue a qualified opinion – an adverse opinion is issued if the auditor does not feel that the accounts give a true and fair view. He may issue a disclaimer of opinion if he cannot obtain sufficient information.

Ran out of time

Comment

Bad use of time; again more bookwork which is not directly answering question; poor/ no planning; wasted time; auditing point is quite a good one – equivalent to one mark

How to improve

The question asked for an explanation as to whether the information in the statements would be reliable for a valuation. To do well here the student needed to cover reasons why the information may be reliable and reasons why it may not. A simple list of what is in the accounts, as given above, does not achieve this.

Before the exam make sure you have completed your revision and can answer questions in good time. In the exam itself, have a time plan and stick to it. Don't spend too long on questions – you are better off moving onto the next one and coming back if you have time spare at the end.

- (iv) Financial statements have four groups of users:
- Equity investors
 - Loan creditors
 - Employees
 - Business contacts

There are also other reasons why a company prepares financial statements eg

- i. For stock exchange requirements
- ii. For tax (**1**)
- iii. So that investment analysts can form a view
- iv. For shareholders (**½**)

- v. It is important that all companies show the same amount of information so that the financial markets can proceed in an orderly fashion and that they can be regulated properly.

Comment

Again more bookwork which does not answer the question; misread question (unquoted); again no or poor planning

How to improve

As before, don't just regurgitate the bookwork.

Make sure you answer the right question – read it carefully! The question was about an unquoted company yet the answer here included points about the stock exchange (ie relevant to quoted companies). The answer here lists the groups of users of financial statements but does not always clearly explain why unquoted companies should prepare statements.

Marks awarded:

- (i)** 2
- (ii)** 1
- (iii)** 1 (for auditing aspect gaining an equivalent mark)
- (iv)** 1½

TOTAL 5½