Financial performance – advice on extended writing tasks

The Financial performance computer based assessment (CBA) includes two written tasks, in the form of emails or reports. Cliff Floyd, the Chief Examiner, offers some examples of good and poor answers.

The Financial performance assessment is in two sections. Section 2 contains two written tasks designed to test your application and communication skills. For both tasks you'll need to read and analyse a scenario. Task 2.1 covers standard costing and variance analysis. It usually provides some key variances and narrative, and you'll need to explain, analyse, give reasons and suggest improvements.

Task 2.2 will provide information on the financials of divisions, products or companies with key performance indicators. You'll need to explain, analyse and make recommendations. The product lifecycle could feature in this task, so you may need to analyse the income and costs for different stages of the cycle.

A typical example of a written task from Section 2 about standard costing
You have been provided with the following variances but your colleague has omitted the sign of some of them:

Variance	Amount
Direct material price variance	£20,000
Direct materials usage variance	£10,000
Direct labour rate variance	£3,000 F
Direct labour efficiency variance	£7,000 A
Fixed overhead expenditure variance	£9,000 A
Fixed overhead volume variance	£5,000
Budgeted production	50,000 units
Actual production	45,000 units

You have also been provided with the following additional information.

- The supplier of raw materials suggested an improved quality raw material, which should result in less wastage in production.
- A budgeted pay rise was not given to staff and this resulted in low morale.
- A machine broke down resulting in delayed production and increased maintenance costs.

Using this information, prepare a report to the Managing Director to cover an analysis of each variance by:

- identifying the sign of the variance where it is missing
- explaining what the variance means
- providing one possible reason for each variance
- explaining any links between the variances.

Here are four possible answers. Read them carefully and decide which answers the question more fully before viewing the feedback from the Chief Examiner.

Answer 1 – Direct material price variance

I suggest that the variance is favourable because the better quality material should result in less wastage and therefore less material needs to be purchased.

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Answer 2 – Direct material price variance

I suggest that the variance is adverse because a better quality of material has been bought.

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Answer 3 – Direct material price variance

I suggest that the variance is adverse because a better quality material was purchased which usually costs more than a lower quality material. An adverse variance means that the price paid was more than expected. This is likely to result in less wastage and therefore a favourable usage variance.

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Answer 4 – Direct material price variance

It has not been determined if this is an adverse or favourable variance. However, as a higher grade of material was purchased and used it is highly likely this variance was £20,000 adverse, as higher quality materials can usually be purchased at a higher price. This means a higher price was paid for materials compared to the standard.

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A typical example of a written task from Section 2 about key performance indicators
The following information has been provided for Companies A and B

Budgeted profit and loss account	Company A	Company B
Sales volume	50,000	75,000
	£	**£**
Sales price per unit	15	15
Total sales revenue	**750,000**	**1,125,000**
Materials costs	200,000	225,000
Labour costs	150,000	225,000
Fixed production costs	250,000	250,000
Total cost of sales	600,000	700,000
Gross profit	**150,000**	**425,000**
Key indicators		
Material cost per unit	4.00	3.00
Labour cost per unit	3.00	3.00
Fixed prod cost per unit	5.00	3.33
Gross profit margin	20.00%	37.78%
Net profit margin	6.67%	24.44%
Return on net assets	10.00%	12.00%

Draft a report covering the following:

(a) An explanation of why the gross profit margins are different, referring to the following:

- sales price
- sales volume
- materials
- labour
- fixed production costs.

Answer 1 – Sales price and volume

The sales price is constant for both companies and the volume is higher for company B. This will increase the revenue for company B and therefore increase the profit margin.

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Answer 2 – Sales price and volume

The sales price is constant for both companies which does not explain the different margins. The sales volume is higher which increases the margin if there are fixed costs.

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Answer 1 – Material cost

The material cost for company B is greater because more units are produced which will reduce the margin the company B2. The more a company produces the greater the cost and this cost is taken from the profit.

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Answer 2 – Material cost

The material cost for company A is £4 per unit and Company B is £3 per unit. Lower material cost per unit will result in a higher gross profit margin. Company B is achieving economies of scale.

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Answer 1 – Fixed production costs

The fixed production costs do not change. They are the same for both scenarios and therefore do not affect the gross profit.

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Answer 2 – Fixed production costs

The fixed production costs do not change but the fixed production cost per unit does. Because company B produces more units the overheads spread more and the cost reduces. This improves the margin for company B.

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