A common error committed by candidates when answering questions on the centralisation versus decentralisation debate is to conflate decentralisation with outsourcing. These are quite separate concepts by Tanya Matheson

The E1 paper may well be CIMA students’ first real insight into the opportunities and expectations that await them when they become fully qualified management accountants. Given that the syllabus serves as a mere introduction to the context of international business in the most significant functional areas (apart from finance, of course), E1 leaves one in no doubt that there’s far more to being a financial manager than merely dealing with numbers.

The syllabus, which covers a huge amount of ground, is divided into five main segments of equal weight:
- The global business environment.
- Information systems.
- Operations management.
- Marketing.
- Managing human capital.

In considering each of these, students can start to see the bigger picture of the management role and its impact on how businesses of all sizes and shapes are run.

Historically, the topic of centralisation versus decentralisation has been covered by the following learning outcome in the information systems segment: “Discuss ways of organising and managing information system activities in the context of the wider organisation.” But the debate on whether activities should be centralised or decentralised can be considered across many more functions, including finance, HR, legal and marketing.

The centralisation versus decentralisation debate boils down to where the decision-making power should lie. A centralised organisation is one in which this power resides at higher levels, such as among senior managers at head office. Once they have made their decisions, these are communicated down through the organisation to be enacted at lower levels. Where an organisation has several locations or units, it can become difficult to operate a truly centralised business, so most large companies will need to incorporate a degree of decentralisation. The issue then becomes more about independence: how much control and decision-making authority should the business units have?

A good example of a centralised business would be a multinational fast-
food chain such as McDonald’s or Burger King. A centralised structure enables control and consistency to be maintained across thousands of outlets, while saving on overheads such as local payroll and accounting functions through economies of scale. Franchising, a popular approach among fast-food retailers, has increased in popularity recently. It involves replicating another business’s successful practices at a local level. Crucially, this enables the operator to benefit (for a fee) from the franchisor’s centralised systems, supplies, advertising and branding.

In a business context, decentralisation is the delegation of decision-making authority to smaller local units at lower levels of the organisation. This takes some control away from the hub and will often result in an upward flow of information – the opposite of what happens in a centralised organisation. A good example of a decentralised business would be a large department-store chain such as John Lewis or Debenhams. Each store has a manager who is able to make certain decisions locally, such as which products to promote, whom to recruit and how to handle customer complaints.

The advantages of centralisation are as follows:
- The single point of control enables decisions to be made more quickly and easily, as senior managers will have a clearer picture of the whole organisation.
- Once decisions have been made, the top-down management style of a centralised organisation makes it easier for a standard practice to be implemented throughout the organisation.
- It helps the organisation to focus on its long-term goals, especially in instances where there is one individual leading the company.
- It makes the organisation easier to co-ordinate and control from the hub.
- It facilitates the concentration of skills, enabling specialists to be deployed efficiently across the organisation.
- Because all the information is stored in one place, it improves communication and reporting.
- It avoids the duplication of roles across the organisation, thereby saving costs.

The advantages of decentralisation are as follows:
- It can increase the organisation’s flexibility with regard to minor decisions. By allowing units to become more autonomous, it reduces bureaucracy.
- It enables local managers, who have a deeper knowledge of local situations, to make decisions and resolve conflicts.
- It means that decisions can be tailored more to local circumstances and consumers’ needs. This will help to improve customer service.
- It empowers people further down the hierarchy by encouraging them to innovate and use their initiative, which serves to boost morale and increase their job satisfaction.

In the exam you should concentrate on understanding the question requirements. Often the examiner’s comments in the post-exam guide indicate that many candidates answered the question they would prefer to have seen rather than the one actually asked.

The following tips will help to keep your mind focused when it comes to preparing for the exam:
- Answer the question asked, rather than the one you wanted to see. Candidates often mention outsourcing when answering questions relating to centralisation and decentralisation, but no marks will be awarded for this if the topic isn’t included in the requirement.
- Read every element of the question before starting to write your answer. Often a scenario will cover several issues, so separating your thoughts before putting pen to paper can help.
- Plan your answers, applying what you have learnt to the scenario. You will not gain maximum marks by simply regurgitating everything you know about the subject in question. The key to the answer lies in the scenario, so use the resources available to you. An answer plan will also help you to avoid getting your answers to sub-questions confused.
- Note the mark allocation. You would expect to write more for a 10-mark question than for a five-mark question, but the focus is definitely on quality over quantity. If a question offers 10 marks for the advantages of centralisation, expect to have to make five substantive points, with examples to support these, on – you’ve guessed it – the advantages of centralisation.

Tanya Matheson is a marker for E1 and a freelance tutor.
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If you are in full-time work and have precious little time to devote to your studies, you would be well advised to use your daily experiences to help you consider how the CIMA syllabus applies in the real world.

By Steve Crossman

My students often tell me that they lead such busy lives that they are forced to leave their studies until the very last minute, cramming for their exams and hoping for a pass, rather than expecting one. I tell them that our everyday activities can all link into the syllabus so that, as we go about our business, we can be applying or consolidating what we’ve learnt. For example, our experiences may provide opportunities to think about the product life-cycle or elements of the marketing mix.

Let’s consider a “typical” day. You’re just about to wake up and are perhaps coming to the end of a rather pleasant dream about how you met one of the examiners, fell in love and just happened to stumble across the question papers for the next sitting… Unfortunately, your alarm goes off and ruins the moment. While many of you will have an alarm clock, my guess is that a significant number of you use a mobile phone for this purpose. As your hand emerges from underneath the duvet and scrabbles for your phone, what is going through your mind? “Oh, bother. I can’t believe it’s time to get up already,” perhaps? Or maybe you’re thinking: “Ah, that has reminded me of a great link to the product life-cycle.”

I very much doubt it’s the latter, but it is a concept that’s worthy of consideration. The mobile phone has not only revolutionised telecommunications; it has also had a dramatic impact on many other products and services. For example, if I ask my students what the time is, few refer to their wristwatches; most look at their phones. This is not great news for watch manufacturers, since, from a purely functional point of view, wristwatches are at the maturity/decline stage of the product life-cycle in the same way that the products they succeeded, pocket watches, were a century earlier.

Let’s look in a little detail at the product life-cycle – ie, the period between the launch of a product and its withdrawal from the market.

The length of this life-cycle will vary from product to product, of course. Consider the duration of a tablet PC’s life-cycle compared with that of the new Airbus A350, for example. The former could be a few months while the latter should be several decades.

The product life-cycle typically has four stages: introduction, growth, maturity and decline. At each of these, the manufacturer could try a number of things. At the introduction stage, for example, it could adopt penetration pricing (using a low price in order to build market share quickly) or, at the other extreme, price-skimming (setting a high price to “skim off” customers who are willing and able to pay a higher price). One key factor in determining price at this stage is the amount of competition – a product with...
very few rivals would lend itself nicely to price-skimming, for instance.

At the growth stage, the production volume will increase and associated economies of scale should emerge. If prices can be maintained, these lower costs could result in higher profits or enable the release of funds to reinvest in marketing campaigns.

The maturity stage comes when the product’s sales slow down and the manufacturer’s focus turns to maintaining market share.

Since wristwatches are arguably in the decline stage, how might watch manufacturers try to decelerate the process? Can they extend the tail of the life-cycle? The classic approach is to adjust various components of the marketing mix – for example, reducing the price or increasing the number of distribution outlets. In this case, it probably wouldn’t work: if people use their mobile phones as a timepiece, then it doesn’t matter how cheap a watch is or how many locations it can be bought from. They are unlikely to buy a wristwatch purely to tell the time.

But there are still plenty of stylish and expensive watches for sale, as manufacturers have found a way to extend the tail by focusing on the jewellery value of the watch and its ability to make a “lifestyle statement”. Today’s watches are positioned as fashion accessories rather than functional timepieces. They are bought because they look good rather than because they tell the time. From a marketing point of view, watch manufacturers have looked at the needs of their various customer groups (eg, the desire to be perceived as a rugged outdoor type) and developed watches with appropriate features (eg, a timepiece that’s waterproof at a depth of 200m and has a compass built in).

Let’s consider a product at the other end of the life-cycle. The Harry Potter series of books was one of the most successful pieces of literature in history, providing a great example of how the marketing mix changes over time. You may remember the crowds of fans queuing up to buy the latest book just after midnight on its day of publication. This was truly a product at the introduction stage. How was the marketing mix of the Harry Potter books structured at this point? If we look at the product, the narrative itself would remain the same during all the stages of the life-cycle, but what about the packaging? When a book was first published it was made available in hardback only. This enabled a premium price to be charged – ie, a price-skimming strategy. If you’re a keen muggle desperate to read the latest adventures of the boy wizard, then price isn’t the most important thing to you.

The cost of producing a book in hardback is significantly less than the extra revenue that can be generated by price-skimming. If the book had been launched with a paperback cover, it would have been hard to charge a high price. But, as the product moved through its life-cycle, a paperback version was introduced with a correspondingly lower price. Then there is growth in popularity of e-books as an alternative medium, with electronic versions replacing traditional print. Again, the story didn’t change, but altering the packaging – and the price accordingly – made the book available to a bigger market.

New “collectors’ editions” have since been introduced. Has the story changed?

No, but the packaging has changed, again: the books now have embossed leather covers. It’s another example of tweaking the product to extend its life.

In the maturity/decline stage, excess copies are cleared from the shelves and stocks are pulped at a loss. An example of this is the pulping of a large number of copies of the 50 Shades trilogy as the result of over-stocking.

We’ve seen that prices can change at different stages of the life-cycle. Further details on the different types of pricing methods can be seen in the table above.

If simply switching off your alarm in the morning can illustrate the product life-cycle for you, what else might be in store when you go for a cup of coffee or catch a bus to work?

Steve Crossman is CEO of the ExP Group. More than 25,000 people worldwide subscribe to his weekly “business exam success blog” newsletter. ExP provides free online CIM courses. Details of these and the blog can be found at www.theexpgroup.com.
T4 part B

Test of Professional Competence in Management Accounting

Hold on to your hat for the concluding episode of ‘High noon in the boardroom’ – a dramatic re-imagining of May 2013’s BVS case study in two acts, the first of which was published in FM’s October issue

By Ian Herbert, FCMA, CGMA

This is the second of two articles focusing on the recent BVS case. Before reading it, you should review the case and the model answer, both of which can be found on the CIMA website at bit.ly/T4resources.

When the board meeting resumed, Toby Baum told his colleagues: “I appreciate that we have been trying to do a lot and maybe we’ve been flying by the seat of our pants lately instead of being as analytical as we might have been. But we are where we are. Annika will now outline the priorities as she sees them and recommend a cohesive plan. I accept that this will involve some compromises and I am happy for there to be a discussion afterwards, but my top priority is for us to proceed as a team.”

Annika Larsen opened her slide deck and started what she knew was a make-or-break performance for her career at the company.

“I propose that we adopt a plan based upon the following order of priorities,” she said. “First and foremost is the need to rebid on the government contract. I propose that we bid at minus 7.8 per cent to give us a little room to negotiate down to minus 8 per cent if necessary. If we’d had more time to prepare, perhaps we could have stood our ground, but for now the profitability of this contract is 9.5 per cent. So, even with the reduction, we’d still make a small profit and, perhaps more crucially, avoid losing the significant contribution to our fixed costs and having to pay our contractors €1 per hour more. The impact on profitability would be minus €4,435,000 if we were to lose this contract right now.

“While the bid instructions make the price non-negotiable in essence, we might be able to draw on our record of high-quality service to negotiate a two- or even three-year contract. Perhaps we might even be able to do less routine servicing or subcontract some of this work, since that part of the contract is much less profitable than our ad hoc repairs and tyre replacements.

“I don’t expect any of us to be happy about this, but I’ve made some projections of the estimated share price at flotation in figure 1 on the next slide and you will see that the overall return is extremely healthy relative to the buy-out share price of €5. But you’ll also notice that, without the government contract, the projection is worse than it would be if we were to retain that business, even at the lower price.

“This brings me to the second priority: customer profitability analysis. Leo is right that we are accepting any business at present and we simply cannot be sure exactly which customers are profitable to us. The signs from the new analysis are that we’re actually making a net loss of 3.3 per cent on small customers and we need to be much more proactive in chasing debts outstanding with them. While we make net profits of 5.7 per cent and 4.9 per cent from large and medium-sized customers respectively, there’s no significant difference between the three categories’ contributions to fixed costs. We need all three types at the moment and I would add two further points here: first, we aren’t the only new business to focus on grabbing market share at any cost; second, our flotation valuation will be based on growth, profit and perceived risk. A balanced portfolio of customers will assure investors that we are not unduly reliant on one or two big players.

“Customer profitability analysis takes time and money. To do it as an ongoing exercise rather than as a one-off will require new IT and administrative systems. But we must proceed with the right pricing model. We need to renegotiate prices in cases where existing accounts aren’t appropriately profitable. Moreover, Philip’s sales team will need to be motivated by a mix of price, volume and cash flow – and for retaining, as well as gaining, business. Again, this will take time and entail a change of culture. We may even have to renegotiate some employment contracts.

“The third priority is the proposal for the pressure-checking service for tyres. This seems to be a profitable venture, with a net present value over three years of €611,000. It represents the sort of value-added service that complements what we already provide and it matches our stance on environmental issues. But it’s for the medium term, as it will take time to recruit staff and engage customers. And there is always the risk that, as we prove the savings, some customers may instruct their drivers to make the checks and maybe pay them a little extra for this, instead of paying us.

“Having said that, we might accelerate this plan instead of making some redundancies if we were to lose the government contract. I propose that we start a pilot scheme with a customer that’s relatively geographically constrained – a local authority, for example – so that we’d need to involve only one depot. This should enable us to gain valuable experience in case we need to...”
The situation might be different if more utable ups and downs along the way. from our long-term strategy by the inev - are achievable. We must not be deflected "We all stand to gain or lose by the even she said, looking straight at Jonas Kral. I see this as a real option for mitigating expand the operation quickly. I’ll pre - aspect, because apprentices have been There may also be a health and safety pany policy and for parts not to be paid for. is not ethical for managers to ignore com This is not something we should allow. It There may also be a health and safety aspect, because apprentices have been fixing their own cars, even though we’d never allow them to work unsupervised on commercial vehicles. But I am acutely aware that the situation is not straight- forward. We’ve known about this practice for some time and have done nothing to address it. Claiming that we never knew it was going on would never wash if it came to an industrial dispute or a negligence case. And we need to show that we are sensitive. Carmen will bring an end to the practice by the end of the month, but she will do so in consultation with the relevant managers and technicians. “That’s it. Any questions?” Bauml responded before anyone could raise an objection. “Thank you, Annika. That was an excellent summary of the situation and our priorities,” he said. “I suggest that we break for refreshments before we discuss how we are going to implement her recommendations.” Larsen tried not to show how relieved she was that he looked pleased and had cleverly taken the sting out of any chal- enging that might have been coming.

Ian Herbert is a senior lecturer in ac - counting and financial management and deputy director of the Centre for Global Sourcing and Services at Loughborough University’s School of Business and Economics.

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Paper F2
Financial Management

F2 candidates often score poorly on the very last question because they fail to relate their discussion or explanation closely enough to the given scenario. Try to stay focused on the business and its particular situation.

By the examiner and a marker for F2

The closing question of the F2 paper requires candidates to analyse and interpret financial information about a business. This may be for the benefit of a potential investor or a bank considering a loan application. The first part of the question often offers 20 marks for some ratio calculations and a discussion of the firm's performance and financial position. The last part, usually offering five marks, tends to ask about the benefits and limitations of the analysis or the extra information needed in order to make a good decision. This is often not answered well.

When tackling such questions, you would be well advised to do the following:

- Observe the verb in the requirement. If an explanation is needed, write a full sentence for each point you make. Don’t provide a list of one-word responses.
- Make a brief plan. Scoring five marks will entail making three to five good points, so think about these before putting pen to paper. Students who don’t do this will often repeat a point simply using different words. The markers do notice this.
- Avoid listing generic points regurgitated from the textbook, since not all of these are likely to apply. Use the relevant information from the scenario.
- Make your points relevant to your audience – is it a potential investor or a lender?

With these principles in mind, let’s review question 7(c) of November 2012’s F2 paper. It requires candidates to “explain the limitations of using the financial ratios above as a means to compare X and Y”.

The scenario concerns a firm considering the acquisition of one of its suppliers – i.e., a potential investment. X and Y are the potential targets. High-scoring candidates would have identified that they operate in different nations. This gave the opportunity to discuss different economic climates, different accounting standards, the age of the information provided and the accounting policies used by each firm.

Low-scoring candidates would have discussed the fact that X and Y may have varying depreciation methods and different policies for the revaluation of non-current assets, thinking that each was worth a mark. This is one point: they have different accounting policies. Many also mentioned that the accounts could have been manipulated. Really? If they were published, they would have been audited. Ensure that your suggestions are valid and reasonable.

Question 7(c) of May 2013’s F2 paper requires students to “discuss what additional information your client could obtain in order to help him arrive at a decision about whether or not to invest”. The scenario is about a potential investor in a group of firms that organises music festivals and provides security for such events. A lawsuit is outstanding at year end and, if the business were to lose this, it would have to pay a substantial sum in damages. The question states that this was disclosed in the accounts as a contingent liability.

You need to put yourself in the investor’s shoes here. It’s about to put a lot of money in a firm that may not be a going concern if it loses the case. It would want to know how the lawsuit is progressing after the end of the year. Where will this information be found? Interim financial statements and recent press releases would be worth reviewing. Also look at the movements in its share price to see how the market has been rating its performance.

The following are suggested information sources that scored no marks:

- Budgets and forecasts. It would be lovely to review these, but no ethical employee would leak them to an outsider.
- Historical trends. What use are these when the main issue is cash flow if the business loses the court case?
- Industry averages. These would be useful only if you had a firm that didn’t have a big problem in its accounts and could therefore be compared against the mean.
- Economic factors – e.g., tax. Why would this make any difference unless we were comparing firms in different jurisdictions?
- Accounting policies. Would a potential investor really be interested in whether the firm uses a straight-line or a reducing-balance method of depreciation when it is facing a serious cash flow problem?
- Narrative information. This is produced at the time of the accounts. It is forward-looking, but not certain.

The main insight to take away from these examples is that candidates must not simply set out a list of points learnt from their study text. Look at the scenario carefully and remember: the final part of the final question may be worth only a few marks, but these could be the difference between a pass and a fail.
Paper P2 Performance Management

Time and again in the P2 exam, candidates provide information that’s not asked for by the questions. If you don’t want to waste time and marks, you’d be well advised to focus on the verbs in the requirement

By Tim Thompson and the examiner for P2

In the preceding article in this series, published in October’s Velocity (www.cimaglobal.com/velocity), we gave a sample scenario that might appear as the preamble to the requirements of an exam question. We also provided an initial sample requirement, based on the scenario, using the verb “explain”.

In this article, the second of three, we will provide two further sample requirements, using the verbs “calculate” and “discuss”. These are also based on the scenario given in the first article. As before, we will suggest a solution.

Sample requirement two is as follows: “Calculate the currently expected actual total cost of manufacturing the 1,000 units of product Q (four marks).”

“Calculate” is a level-three verb that’s concerned with application. It means “ascertain or reckon mathematically”. You must ensure that the workings you present are detailed and clear. Minor calculation errors aren’t penalised heavily, providing that the marker can see that your approach is clear and correct. Even if you make a mistake early in the calculation that makes the rest of the numbers wrong, they will be treated as correct as long as you have used the right method.

Note that the following suggested solution calculates only the total cost. It does not go on to discuss the significance of the figure, for example, because no marks are offered for doing so.

Suggested solution to requirement two

\[ \begin{align*}
  y &= ax^b \\
  y &= 10 \times 1,000^{0.152} \\
  y &= 3.5 \text{ hours} \\
\end{align*} \]

The expected actual total cost of manufacturing 1,000 units of Q is therefore:

\[ \begin{align*}
  (1,000 \times (3.5 \times 7 + 30)) + 10,000 &= $64,500 \\
\end{align*} \]

Sample requirement three is as follows: “Discuss the potential viability of three actions that XZP might consider taking to attempt to improve the profitability of product Q over its life (six marks).”

“Discuss” is a level-four verb that means “examine in detail by argument”. It is concerned with the learning objective of analysis.

To start with, you’ll need to identify three ideas for action that might reasonably be suggested as ways to improve profitability. “Identify” is actually one of CIMA’s recognised verbs from level two. The question isn’t specifically asking you to identify three ideas – the expectation is implied, because you cannot answer the question without doing so. After identifying your three ideas, you’ll need to explain how each of these could improve profitability. Once again, the requirement contains an implied subordinate verb: “explain” (also from level two).

At this point we have a solid foundation for our answer, but to raise it to a discussion we must address the viability of each idea, which is clear in the requirement. (This is a useful reminder to ensure that you read the question carefully so that you’re clear about what the examiner wants.) The first idea in the following suggested solution – to raise the selling price – shows how this can be done. The explanation is that, if all other factors were to remain unchanged, the total revenue and profit would increase. The discussion is completed by challenging the assumption that sales volume would remain unchanged and concluding that this idea is probably not viable.

Suggested solution to requirement three

- Idea one: increase the selling price. If XZP were to set it above the planned $77 per unit, then, if all other factors were to remain unchanged, the total revenue and hence the total profit would increase. This works mathematically, but is unlikely to work in practice. That’s because it’s clear in the scenario that the selling price of Q is expected to be determined by the market. Any attempt to push it above $77 would probably mean that the product wouldn’t sell.

- Idea two: improve the rate of learning. If it could be improved to less than 90 per cent, then the total time taken to make 1,000 units of Q would be shorter, which would in turn cut the total labour cost. Extra training, or the recruitment of more skilled employees, would be potential ways to improve the rate of learning. For this to be viable, the benefit of the improved rate would need to exceed the cost incurred in achieving it.

- Idea three: reduce “other” variable costs. These will include the cost of the raw materials used to make Q. If XZP has not already done so, it could contact a range of suppliers to determine whether or not any materials could be obtained more cheaply. But it is important that any use of cheaper materials does not reduce the quality of the product.

The three verbs we have covered so far in this series have been “explain”, “calculate” and “discuss”, all of which appear frequently in the P2 paper. In the third and final article, we will focus on another of the verbs that the examiner might use. You will find it on the P2 exam preparation resources area of the CIMA website (bit.ly/P2StudyNotesPart3).

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Exam notice
Visit www.cimaglobal.com regularly for updates

November 2013 main exams
The exams will be held on 19, 20 and 21 November. The deadline for entries has passed, so applications will be accepted only in exceptional circumstances.

Cancellations and changes
CIMA does not accept cancellations and will not refund fees. The standard closing date for changing papers or exam centres was 19 September.

Attendance advice letters
You must print off your admission advice online by logging into your “My CIMA” account. This shows the exact details of your exam centre and the papers you are sitting. You must take the admission advice with you to the exams and keep it safely afterwards, as it contains your candidate number(s).

Exam rules
You must download the exam rules and regulations from the CIMA website and read these when you download your admission advice.

Going to the exams
As well as your admission advice you will need to bring another means of identification to the exam hall showing your photo, name and signature – eg, a passport or driving licence.

Pre-seen material for papers at Strategic level and T4 part B
The pre-seen material for November’s T4 part B case study can now be downloaded from www.cimaglobal.com/t4preseen. An article analysing the pre-seen material is also available there.

The pre-seen material applying to all three Strategic level papers for the November 2013 exams is available from www.cimaglobal.com/strategicpreseen. It’s your responsibility to download this material and familiarise yourself with it.

A “clean” copy of the pre-seen material and further unseen material will be provided in the exams. You cannot take any notes with you into the exam hall.

Tax rules for papers F1 and F2
Information on the relevant tax rules and examinable standards for the Financial Operations and Financial Management exams is available to download from the “Study resources” page for each paper on the CIMA website.

Absences from any of the Strategic level exams
You should apply to the examinations and assessment oversight panel if you have missed one or more of your Strategic level exams on the first sitting because of illness or any other mitigating factor. For details, visit the “After the exams” section at www.cimaglobal.com/Students/Exams.

Past exam papers and model answers
Past question papers and model answers are available to download from the relevant “Study resources” pages on CIMA’s website at www.cimaglobal.com/Students/Exam-preparation. Further model answers can be found in Velocity (www.cimaglobal.com/velocity).

Post-exam guides
Post-exam guides are available to download from the relevant “Study resources” pages at www.cimaglobal.com/Students/Exam-preparation. These are essential reading for unsuccessful candidates and those studying new papers.

They contain:
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The results of November’s T4 on PC exam will be released on 12 December. All other November results will be released on 14 January 2014. Log into your “My CIMA” account to register to receive your results by email.

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Queries
Visit www.cimaglobal.com/exams to see whether your question is answered there, or get in touch with CIMA Contact (cima.contact@cimaglobal.com) or your local office (see panel, page 7).

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