



# *ROLE SIMULATION EXAMINATION*

## *ADVANCE INFORMATION*

This material is issued prior to the examination session.

Candidates **must** bring this material with them  
to the Examination Hall.

No copies will be provided.

## ADVANCE INFORMATION

This Advance Information is issued prior to the examination session to allow you to familiarise yourself with the information provided and to undertake any other appropriate research and analysis. The Advance Information is also published on the website: [www.icaew.com/students](http://www.icaew.com/students).

**You must bring this Advance Information with you to the Examination Hall**, annotated if you wish, together with any other notes of your preparatory work. You must carry out sufficient and appropriate analysis work **of your own** in order to have a detailed understanding of the Advance Information. You should also undertake any additional research and analysis you feel necessary to enhance your awareness of the industry and market context and to enable you to clarify any technical terms or other issues of vocabulary. You will need to be able to refer back quickly to the Advance Information and your notes during the examination; you are therefore unlikely to benefit from taking large quantities of additional material with you into the Examination Hall.

At the start of the examination you will receive some additional material which will complete the description of the role simulation scenario and state the role simulation requirements. Your answer must be submitted on the paper provided by ICAEW in the Examination Hall. Any pre-prepared papers, or papers comprising annotated exhibits from this Advance Information, included in your answer will not be marked.

The examination is based on the 2019 Learning Materials.

### Assessment of the Role Simulation Examination

The marks in the Role Simulation Examination are awarded for demonstration of competence in the knowledge, skills and behaviours set out in the Level 4 Accounting Technician assessment plan. The marks are allocated broadly as follows:

- Knowledge 30% - 40%
- Skills 30% - 40%
- Behaviours 30% - 40%

The knowledge, skills and behaviours will be assessed through a series of requirements in the Role Simulation Examination. Marks available for each requirement will be shown next to each requirement.

### Presentation of Answers

Answer each task in black ballpoint pen only.

Answers to each task must begin on a new page and must be clearly numbered. Use both sides of the paper in your answer booklet.

For multiple choice questions, you should clearly record the response you wish to select in your answer booklet. If the examiner is in any doubt as to which option you consider to be correct, you will receive no marks for that question.

The examiner will take account of the way in which answers are presented.

## Real Deal Productions Ltd

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**This document reflects information available as at 15 October 2020.**

## **Introduction: Real Deal Productions Ltd (RDP)**

Real Deal Productions Ltd (RDP) is an independent TV production company that specialises in making two types of reality TV programme:

- 'Fly-on-the-wall' documentaries – these follow people engaged in a profession or hobby during their day-to-day working and personal lives. Documentaries currently in production include "Police HQ", which follows police support staff as they ensure smooth operations at a major police headquarters over a six-month period.
- Competitions – these involve people participating in a contest which only one participant, or one team of participants, can win. Competitions currently in production include "The Mobile Kitchen", in which teams of professional chefs compete to set up the most successful mobile kitchen business in the UK.

Both types of reality TV programme have been popular with viewers for over 20 years and are in the maturity phase of their product lifecycle. During that time RDP has created and produced a range of innovative programmes which have won awards for quality. RDP is also renowned for its ethical approach to production.

## **Background on the TV industry**

The TV industry is divided into two main activities: production of programmes and delivery of programmes to viewers.

### Delivery

TV programmes are delivered to viewers in two ways:

- On-screen broadcasters, such as the BBC and ITV, deliver programmes in real time via terrestrial or cable TV channels, usually 24 hours a day. Viewers can also 'catch up' on broadcast programmes for a limited time after initial delivery.
- Video-on-demand (VOD) streaming services, such as Netflix and Amazon, allow viewers to stream or download content directly at any time via the internet.

### Production of programmes

Broadcasters and streaming services contract with TV production companies to produce TV programmes for them. These contracts are known as commissions.

Typically, a production company operates with a limited number of employees. It completes the process of production by contracting with a large number of external specialists in the different skills involved in programme production, such as directing, camera operation and sound recording.

In the UK there are several large, non-independent production companies owned by broadcasters or streaming services (eg ITV Studios). They produce many types of TV programme such as factual and drama as well as reality TV. There are also many small to medium-sized independent production companies, known as 'indies', which specialise in

producing particular types of programme such as fly-on-the-wall documentaries. Indies compete intensely with non-independent production companies for commissions and access to the best external specialists in programme production.

Relationships with the individuals who commission programmes at client broadcasters or streaming services are important for indies. The reputation of each indie is significantly influenced by the success of their most recent programme.

Production of TV programmes in terms of staging, filming and special effects etc has become increasingly digitalised. Production companies must take account of the different IT platforms used by broadcasters and streaming services when delivering content to the public via TVs and other devices such as smartphones.

### Regulation

Ofcom is the independent regulator and competition authority for UK communications industries. Its responsibilities include supervising the delivery of TV programmes by broadcasters and streaming services, which have the final editorial responsibility for their content. Ofcom has the power to issue financial penalties for breaches of its rules on, for example, protecting under-18s.

### Latest trends

The TV industry is large and growing in the UK and globally. However, the ongoing changes in how programmes are delivered to viewers mean that the industry is fragmenting. Average audiences for broadcast as opposed to streamed programmes in the UK are falling year-on-year. As this affects advertising revenue, many broadcasters are diversifying into subscription-only video-on-demand (SVOD) so they are not reliant on advertising revenues only.

In terms of the content of reality TV programmes, trends include:

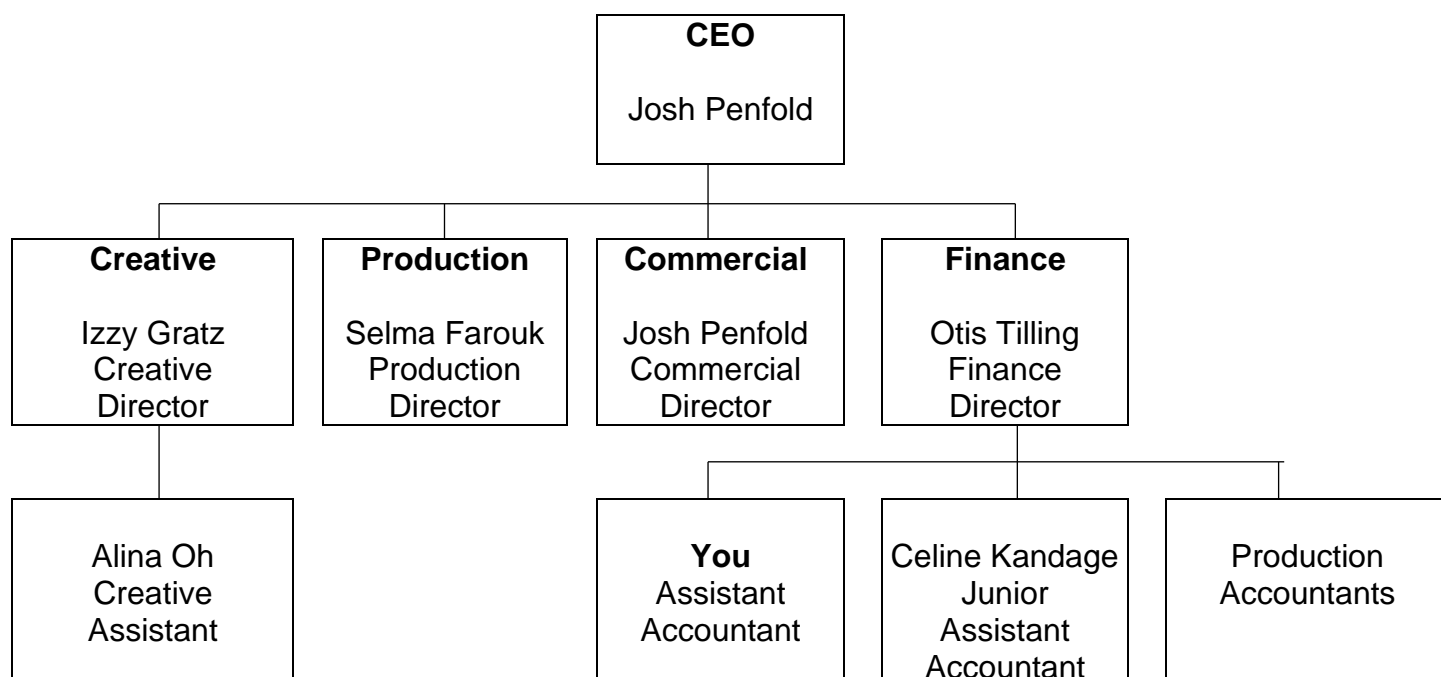
- viewers moving away from some types of reality TV following public scandals about their effects on presenters and participants, and on viewers aged under 18
- augmented reality programmes with multiple storylines, in which a viewer reaches a junction, chooses an option and goes down that pathway. The result is that few viewers have the same experience by the end of their path.

### **RDP**

RDP was founded as an indie in 1999 by Izzy Gratz, Selma Farouk and Josh Penfold, who formerly worked together at the BBC. All three founders are still fully involved in the business as directors and they collaborate well together. Otis Tilling, the finance director, is the only other member of the board of directors. Each director holds 25% of RDP's ordinary share capital.

You are an assistant accountant within RDP's finance function. You are training to become an ICAEW Chartered Accountant. You report to Otis Tilling, the finance director, who is an ICAEW Chartered Accountant.

This is an extract from RDP's organisation chart:



Your colleague, Celine Kandage, has just been appointed. She has not yet received professional training except for an introductory course on accounting principles, including materiality. There are also several production accountants who work on individual programmes while they are being made. Production accounting at RDP is described further in **Appendix D**.

## Operations

RDP's activities are based in Manchester. On 1 November 2010 RDP bought a small freehold building in Manchester for a total of £950,000 (this included £350,000 for land).

Each RDP programme takes the form of a series comprising up to eight episodes. Many of RDP's programmes are now in their second or subsequent series because they have been re-commissioned by the client. Production of each series takes six to nine months from commission to delivery. **Appendix A** sets out the operational process for commissioning and producing programmes, and includes RDP's statement of business ethics.

RDP's clients are UK broadcasters. RDP is not currently in a position to market effectively to streaming services. RDP does not seek commissions from outside the UK to make original programmes.

Very occasionally RDP commences speculative production of a programme, before a commission from a client has been agreed, in the expectation that a commission will be achieved at a later date. Sometimes RDP produces programmes in conjunction with other indies. These programmes are known as co-productions.

## Production function

RDP's production function has a reputation for high quality processes and outputs. It comprises a small number of employed staff who contract with a wide range of external

specialists. These specialists are issued with separate contracts to supply services for each programme they work on. They provide RDP with their services as independent contractors, not employees, so under law they have no employment rights such as entitlement to sick pay.

RDP's standard contract with external specialists includes payment of an advance fee when the specialist agrees to supply their services for a programme over a prolonged period of time. There are no explicit terms relating to frustration or force majeure in the standard contract.

## **Commercial function**

RDP's commercial function negotiates each commissioning contract with a client based on a detailed specification for the programme. RDP and the client then agree a fixed price which falls within a range that is standard in the industry. The total amount of the fixed price is driven by the number of episodes and how much the client believes the programme will generate in terms of advertising and/or subscription revenue.

Broadcasters and streaming services rely on advertising and/or subscription revenue to different degrees. They make estimates of their potential revenue based on the vast amounts of data they collect about the behaviours of the viewing public (see **Appendix G**).

RDP aims to achieve a gross margin of 20% on each programme. The commercial function therefore draws heavily on the production accounting skills of the finance function to prepare a final cost budget for the programme that is complete and achievable, given the fixed price and specification agreed (see **Appendix D**).

The commissioning contract usually states that, if the client changes the agreed specification during production, any additional costs will be passed on to the client by RDP at a 20% margin. However, if RDP incurs costs in excess of the estimated amounts included in the final cost budget – known as 'cost overruns' – these cannot usually be passed on. The risk of cost overruns remains with RDP.

## **Recent performance**

RDP typically has between seven and nine programmes in production at any one time. Despite its reputation for quality, RDP has recently lost potential reality TV commissions to smaller indies which have more innovative programme ideas and production techniques. Like all indies, in the last 18 months RDP has experienced falling prices from broadcasters. In addition, broadcasters are increasingly resistant to RDP passing on additional costs caused by changes to programme specifications.

**Appendix B** contains extracts from RDP's financial statements for the year ended 31 October 2019. **Appendix C** contains relevant accounting policies.

## **Board meeting on 12 October 2020**

RDP's directors are aware that profits have fallen in the reporting period which will end on 31 October 2020. This is partly due to a fire at the RDP building in August 2020, which increased administrative expenses because RDP subsequently had to rent temporary accommodation.

Recent longer-term forecasts show that, based on the number of commissioned programmes now in development or production, RDP's profits will gradually continue to fall. The directors fear that the size of the business will contract unless they develop expertise in producing different types of TV programme and adopt a more effective approach to marketing to streaming services.

The directors discussed these and a range of other issues at a board meeting on 12 October 2020. **Appendix E** contains extracts from the minutes of the meeting.

### **External audit**

RDP's external auditor is Mocona LLP (Mocona). The engagement partner, Hermione Letts, emailed Otis Tilling with some expectations regarding the final audit of RDP's financial statements for the year ending 31 October 2020 (**Appendix F**).



## Appendix A – RDP’s operational process and Statement of business ethics

### RDP’s operational process

RDP first develops an idea for a TV programme into a proposal for a potential client. Proposals include a programme specification plus photographs, a screen-test or a sample film.

In summary, RDP’s process for each programme is as follows:

Programme	RDP functions involved
<p><b>Develop proposal</b></p> <p>Conceive programme idea and obtain an expression of interest from a client</p> <p>Develop programme specification and prepare proposal for the client</p> <p>Obtain commission from the client: agree on fixed price, finalise contract terms, prepare a final cost budget and sign contract</p>	<p>Creative</p> <p>Creative, Commercial and Finance</p> <p>Commercial and Finance</p>
<p><b>Produce programme</b></p> <p><u>Set-up</u>: obtain resources (participants, external specialists, equipment, locations, props etc)</p> <p><u>Recording</u>: record each episode (images and sound) in accordance with programme specification</p> <p><u>Editing</u>: edit recorded programme, add computer graphics, music and titles, and meet relevant IT platform requirements</p>	<p>Production</p>
<p><b>Close</b></p> <p>Client accepts all episodes of the finished programme</p>	<p>Production</p>
<p><b>Follow-up</b></p> <p>Explore opportunities for re-commissions of programme by client</p>	<p>Commercial</p>

### Statement of business ethics

RDP has the following statement of business ethics which it publicises both inside and outside the organisation:

“At RDP we aim to produce entertaining programmes in an ethical manner based on our core values of fairness and kindness. The TV industry is regulated by Ofcom, so we comply in full with relevant regulatory requirements in relation to the physical and psychological welfare of all programme participants. We pay close attention to the age of programme participants and any vulnerabilities they may have. We partner with ethically-aware external specialists and co-producers.”

## Appendix B – Financial statements for the year ended 31 October 2019 (extracts)

RDP prepares its financial statements under International Financial Reporting Standards (IFRSs).

### Real Deal Productions Ltd: Statement of profit or loss for the year ended 31 October 2019

	£'000
Revenue	18,036
Cost of sales	<u>(14,401)</u>
Gross profit	3,635
Administrative expenses and distribution costs	<u>(2,704)</u>
Profit from operations	931
Finance costs	<u>(40)</u>
Profit before tax	891
Income tax expense	<u>(178)</u>
Profit for the period	<u>713</u>

### Real Deal Productions Ltd: Statement of financial position as at 31 October 2019

	£'000	£'000
<b>ASSETS</b>		
<b>Non-current assets</b>		
Property, plant and equipment		920
<b>Current assets</b>		
Inventories	262	
Trade and other receivables	7,213	
Cash and cash equivalents	<u>2,485</u>	
		<u>9,960</u>
<b>Total assets</b>		<u>10,880</u>
<b>EQUITY AND LIABILITIES</b>		
<b>Equity</b>		
Ordinary share capital (50p shares)		200
Retained earnings		<u>5,406</u>
<b>Total equity</b>		5,606
<b>Non-current liabilities</b>		
Borrowings (8% bank debentures)		500
<b>Current liabilities</b>		
Trade and other payables	4,596	
Income tax payable	<u>178</u>	
		<u>4,774</u>
<b>Total equity and liabilities</b>		<u>10,880</u>

## **Appendix C – Accounting policies (extracts)**

### Property, plant and equipment (PPE)

PPE (land and building plus equipment) is recognised in the statement of financial position at cost less accumulated depreciation and impairment losses. Depreciation is charged on a straight-line basis over the useful life of each class of asset (20 years for the building and five years for equipment), taking residual value into account. A whole year's depreciation is charged in the year of disposal. Depreciation and impairment losses are presented in administrative expenses.

### Cost of sales and inventories

Costs incurred on commissioned programmes in the course of production are recognised immediately in cost of sales. Costs incurred on speculative programmes, for which a commission has not yet been received, are recognised at the end of the reporting period as inventories (work-in-progress) at the lower of cost and net realisable value.

### Revenue, accrued income and deferred income

Revenue for a commissioned programme is recognised as production progresses.

Any difference at the end of the reporting period between the revenue recognised and the amounts invoiced to the client (see **Appendix D**) is recognised in the statement of financial position in trade and other receivables as accrued income, or in trade and other payables as deferred income, as appropriate.

## Appendix D – Production accounting at RDP

Once the specification and price for a commissioned programme are agreed, RDP can calculate the amount available to spend on its production. The budgeted level of total costs in the final cost budget is determined as the fixed contract price less a budgeted 20% gross margin.

The production accountant for a programme regularly prepares cost reports to indicate the actual costs incurred to date and forecast costs to completion. These reports, prepared monthly during the programme's production, are an important way of controlling total costs against the original budget.

Many of the costs involved in production are semi-variable, so RDP often uses the high-low method to forecast costs for episodes of a programme that are still to be completed.

At the end of a reporting period, cost reports are used to determine the percentage completion of the production and the revenue to be recognised in the year. The revenue recognised may be greater than or less than the amounts invoiced to the client in the year, resulting in balances for accrued and deferred income (see **Appendix C**).

The commissioning contract determines when RDP can invoice the client as production progresses. For example, the contract for a programme that is planned to take eight months in production typically specifies the following schedule for invoicing:

Schedule	Amounts invoiced to client
End of development	25% of contract price on signature of contract
During production	25% of contract price at end of Month 3 25% of contract price at end of Month 6
Close	25% of contract price on acceptance of finished programme by client

Costs related to changes made by the client to the specification after the fixed price has been agreed are identified and invoiced separately by RDP to the client at RDP's gross margin of 20%.

A small proportion of commissioning contracts provide for cost overruns to be passed on to the client at cost only.

## **Appendix E – Board meeting on 12 October 2020 (extracts from minutes)**

### **Fire at RDP’s building**

Otis Tilling, the finance director, confirmed that the fire in August 2020 impaired the building’s value and, while the building was insured, some of the equipment was not. The board agreed that RDP’s temporary rented accommodation is inadequate and new permanent premises are needed urgently.

### **Programme ideas in development**

The directors discussed their fears that the size of the business will contract unless they develop expertise in producing different types of TV programme. Subsequently, reports were received on five programme ideas in development:

#### 1 Adventure Plus

Izzy Gratz, the creative director, presented an idea for an augmented reality programme called “Adventure Plus”. All the directors are keen to develop the idea into a speculative proposal, but accept there is a significant risk that it may never be commissioned by any client. Otis is reluctant for RDP to commit cash from existing operations to developing the proposal so alternative funding is required.

#### 2 A Wild Career

Izzy also presented an idea for a new competition programme, provisionally entitled “A Wild Career”, the winner of which will be given the role of apprentice zookeeper at a wildlife park. Izzy potentially wants to co-produce this with another indie called Swerve Co. However, Otis expressed doubts based on what he knows about Swerve Co’s CEO, Sammy Rayner. Sammy persuades clients to sign commissioning contracts by including a clause that cost savings made by Swerve Co on the agreed specifications will be passed back to the client. Sammy then manipulates production quality and costs so substantial savings are made on the final cost budget, but he passes none of these savings back to the client. He also invoices clients for cost overruns which have not actually occurred.

#### 3 High School Sports

Josh Penfold, the commercial director, reported on the “High School Sports” proposal which RDP is developing to present to one of its main clients. It is a fly-on-the-wall documentary following teachers in the sports department of a secondary school during the academic year. Josh hopes to secure a fixed price for the commission which is at the top end of the range that is normally seen for such a programme. He is concerned, however, about whether production costs can be controlled enough to preserve the usual 20% gross margin.

#### 4 Climate Clash

Izzy has been approached by Ralph Hewson, an external specialist who is one of the most established programme directors in the TV production industry. Ralph wants to work with RDP to develop an idea called “Climate Clash”, an educational documentary about the effect of specific industries on climate change. This is not a reality TV programme, so the venture would be a move away from RDP’s two current styles of programme. However, the recent appointment of new employees in the creative and production functions give RDP scope to

make this move. The potential clients for RDP's educational documentaries are likely to be streaming services.

## 5 Work Gym

Josh said that he expected TVStandard, one of RDP's most established broadcaster clients, would soon commission "Work Gym", a new programme proposed by RDP.

### **Current activities**

Selma Farouk, the production director, reported on two RDP programmes that are in production:

#### 1 The Mobile Kitchen

Production of "The Mobile Kitchen" competition is nearing completion by Selma's team. Actual costs to date show that some of the figures in the final cost budget for the programme are too low.

#### 2 Cheer Me On

Selma reported that production is in the set-up stage for a commissioned fly-on-the-wall documentary, "Cheer Me On", which is based on a group's preparation for a sporting event. RDP has issued contracts to external specialists for their services between certain dates, but Selma has heard rumours that the underlying sporting event may be cancelled. She is unsure how this may affect RDP's contracts with the specialists and RDP's legal obligations to them.

### **Obtaining commissions from streaming services**

The board discussed the need to grow the business by developing RDP's ability to gain access to streaming services as new clients. RDP has never actively marketed its services beyond personal selling and word-of-mouth recommendation. However, a new generation of decision-makers in streaming services want a different approach, including:

- a mission statement from each indie when it makes proposals
- an awareness among indies of the use by streaming services of the different characteristics of big data to inform their commissioning decisions.

The directors agreed that more awareness of the uses of big data and data analytics would help them to plan their strategy regarding clients and types of programme. They reviewed some information on this topic in **Appendix G**.

The directors also agreed the "Climate Clash" idea, which will appeal to streaming services, may help RDP address its forecast reduction in commissions and level of activity.

### **Finance**

The directors affirmed their belief in Izzy's creative vision in relation to "Adventure Plus". They therefore agreed to make a small increase in their personal investment in RDP via a rights issue of shares on 31 October 2020. This will raise funds specifically for developing the "Adventure Plus" proposal to present to Semiotic, one of RDP's most established broadcaster clients.

RDP has sufficient cash to develop innovative reality TV ideas, produce sample programmes, fund current and planned productions and market to current clients. However, some new finance will be required for:

- acquiring new premises;
- undertaking research and development with a view to expanding RDP's programme types beyond reality TV to educational documentaries like "Climate Clash"; and
- extending RDP's client range to include streaming services.

The board discussed a range of possible sources of long-term finance, including business angels and a listing on the Alternative Investment Market (AIM). Otis suggested that preparing a mission statement for RDP may help with raising finance.



## **Appendix F – Email from external auditor**

Otis Tilling received the following email from Hermione Letts, the engagement partner at Mocona LLP:

Date: 13 October 2020  
From: hletts@mocona.com  
To: Otis Tilling  
Re: RDP audit

Hello Otis,

I confirm that the audit team from Mocona, led by Toni Coleman, will start the 2020 final audit on 7 December 2020. I expect to complete the audit within four weeks.

### **Materiality**

We have calculated materiality for the financial statements as a whole as £180,000, basing the calculation on the lower of 1% of revenue and 2% of total assets in the financial statements for the year ended 31 October 2019. This materiality figure will be revised, using the same percentages, once you provide us with figures for revenue and total assets from the draft financial statements for the year ending 31 October 2020. The revised figure for materiality for the financial statements as a whole will give us a starting point for establishing performance materiality.

### **Audit testing**

We completed our interim audit during September 2020, after the fire that damaged RDP's building.

We identified that RDP has problems in identifying, recording and controlling amounts owed to external specialists who have worked on programmes in production. In addition, from our experience in previous years we anticipate spending significant time auditing accrued and deferred income at the year end.

As a result, we have identified a high risk of material misstatement in relation to trade and other receivables and trade and other payables. We will be carrying out substantive procedures on these balances, on a sample basis, to address the assessed risks of material misstatement at the assertion level.

Please do not hesitate to contact me if you have any queries.

Kind regards

Hermione Letts  
Engagement partner, Mocona LLP

## **Appendix G – Use of data by broadcasters and streaming services**

Broadcasters split each 24-hour daily schedule into 15-minute time slots. They identify which programmes will be available to viewers during each slot, depending on the time of day or night, the type of viewer expected for that slot and the type of programme (eg reality TV) expected by that viewer.

Broadcasters aim to make programmes available which appeal to the type of viewer watching each slot in real time, so they can compete with other channels broadcasting programmes at the same time. This allows them to seek out contracts with advertisers to screen relevant advertisements between each slot. Historically, most broadcasters have depended on advertising revenue for survival.

Data on how many people in the UK viewed each programme in each slot (in real time or via catch-up services) establishes a programme's rating, which is the key indicator of how successful it has been. Strong ratings for programmes in key, prime-time slots are crucial in the fiercely competitive battle among broadcasters for viewers.

Streaming services are increasingly popular with viewers. They are not tied to time slots because viewers can access programmes at any time. Many streaming services are subscription-only so revenue comes directly from viewers, though advertising is also an important revenue stream. Streaming services collect a great deal of data and use it to determine which programmes to make available and how much to charge for them.

Much of the data collected and used by the TV industry meets the 4Vs criteria of big data: volume, velocity, variety and veracity.