



# ROLE SIMULATION EXAMINATION

This paper consists of **two** tasks (100 marks).

1. Ensure your candidate details are on the front of your answer booklet. You will be given time to sign, date and print your name on the answer booklet, and to enter your candidate number on this question paper. You may not write anything else until the exam starts.
2. Ensure you have a copy of the Advance Information.
3. Answer each task in black ballpoint pen only.
4. 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.
5. 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.
6. The examiner will take account of the way in which answers are presented.
7. When the assessment is declared closed, you must stop writing immediately. If you continue to write (even completing your candidate details on a continuation booklet), it will be classed as misconduct.

## IMPORTANT

Question papers contain confidential information and must **not** be removed from the examination hall.

**DO NOT TURN OVER UNTIL YOU ARE INSTRUCTED TO BEGIN WORK**

You **must** enter your candidate number in this box.

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## Task 1

This task consists of **four** parts worth a total of 60 marks.

### Task 1.1

Otis Tilling, the finance director of Real Deal Productions Ltd (RDP), gives you some information about three matters that affect the financial statements for the year ended 31 October 2020:

- The market value of RDP's building following the fire in August 2020 (**Advance Information: Board meeting on 12 October 2020 and Appendix E**) is only £160,000. Annual depreciation of £30,000 and an impairment loss of £140,000 have been recognised in the year ended 31 October 2020. The value of the land is unaffected (**Advance Information: Operations**). Otis wants you to prepare notes to explain the situation with the building to the other directors.
- On 31 October 2020 RDP issued each of the four directors with one ordinary share for every five shares they held (**Advance Information: Appendix E**). The rights issue price was 70p per share. All the directors paid RDP for the shares on 31 October 2020. The rights issue has not yet been accounted for due to a bank error in processing the receipts.
- In order to obtain a commission from Semiotic for "Adventure Plus" (**Advance Information: Appendix E**), RDP started production of a pilot episode on 20 October 2020. The directors are confident that a commission will be agreed with Semiotic at RDP's usual 20% gross margin. At the end of October, payments of £197,000 in advance fees to external specialists working on the pilot were included in cost of sales. As this is a speculative programme, the policy for inventories in **Advance Information: Appendix C** must be applied.

### Requirements

- 1.1 (a) Prepare a briefing note for the directors which:
- explains the differences between impairment losses and annual depreciation charges; and
  - states the effect on RDP's profit of the impairment loss on the building.
- (5 marks)**
- 1.1 (b) Using **Advance Information: Appendix B**, calculate the number of ordinary shares issued to each director on 31 October 2020.
- (2 marks)**
- 1.1 (c) Prepare journals to record, in accordance with RDP's relevant accounting policies (**Advance Information: Appendix C**), the correct treatment as at 31 October 2020 for:
- the rights issue, and
  - the advance fees to specialists regarding "Adventure Plus".
- Include a narrative for each journal.
- (6 marks)**

**Total: 13 marks**

## Task 1.2

Otis has extracted the following list of balances as at 31 October 2020, which does **not** include the effect of the journals you prepared in **Task 1.1(c)**:

Balance	Debit £'000	Credit £'000
Land – cost	350	
Building – cost	600	
Building – accumulated depreciation as at 31 October 2020		300
Building – accumulated impairment losses as at 31 October 2020		140
Equipment – cost	400	
Equipment – accumulated depreciation as at 31 October 2020		240
Inventory	235	
Trade receivables	4,493	
Accrued income	2,419	
Bank	3,630	
Share capital – 50p ordinary shares		200
Retained earnings as at 1 November 2019		5,406
8% bank debentures		500
Trade payables		3,160
Deferred income		1,291
Tax payable		170

Otis tells you that RDP made a draft profit after tax for the year ended 31 October 2020 of £720,000.

Otis wants you to prepare a draft statement of financial position. He tells you that, in addition to adjusting the list of balances for the journals you prepared in **Task 1.1(c)**, the following information is relevant:

- 20% of the debentures are repayable to the bank on 31 October 2021.
- No debenture interest was paid or accrued in the year ended 31 October 2020.
- Equipment that cost £45,000 was destroyed in the fire. It was not insured. The equipment was purchased on 1 November 2017 and has been depreciated up to 31 October 2020 in accordance with RDP's policy, assuming a nil residual value.

### Requirement

With reference to **Advance Information: Appendices B and C** and the journals you prepared in **Task 1.1(c)**, prepare the draft statement of financial position for RDP Ltd as at 31 October 2020 in a format suitable for publication under IAS 1. Do not include comparative figures. Show your workings, including a full working for RDP's retained earnings as at 31 October 2020.

**Total: 17 marks**

### Task 1.3

Hermione Letts, the Mocona engagement partner responsible for the external audit of RDP, has contacted Otis. Extracts from her email dated 8 December 2020 are as follows:

#### Extract 1

“As I mentioned in my email of 13 October (**Advance Information: Appendix F**), I must update our figure for materiality for the financial statements as a whole. We shall calculate the relevant percentages of revenue and total assets using RDP’s draft financial statements for the year ended 31 October 2020, then use the lower figure. This will then help us to establish the appropriate level of performance materiality for our testing. I understand that the draft revenue figure for the year ended 31 October 2020 is £17,280,000 and that your team are in the process of finalising the total assets figure in the draft statement of financial position.”

#### Extract 2

“To obtain sufficient, appropriate audit evidence we will carry out testing of invoices submitted by external specialists (**Advance Information: Production function**) that are included in the trade payables balance as at 31 October 2020. Toni Coleman, who is leading the audit, will organise the selection of a sample of invoices.

We will also perform substantive procedures in relation to the balances for accrued and deferred income (**Advance Information: Appendices C and D**). We will need access to commissioning contracts, sales invoices and cost reports for every programme in the course of production at the year end.”

Otis shares these email extracts with you and Celine Kandage, the junior assistant accountant. Celine has studied the accounting principle of materiality, but she asks you to clarify how the auditor uses the concept of materiality during the final audit.

### Requirements

- 1.3 (a) Identify and explain which one of the two fundamental qualitative characteristics of financial information, as set out in the IFRS Conceptual Framework, is affected by the accounting principle of materiality. **(2 marks)**
- 1.3 (b) With reference to your answer to **Task 1.2** and the information above, calculate the figure that Mocona will use as materiality for the financial statements as a whole in the final audit of the year ended 31 October 2020 (rounded to the nearest £1,000). **(3 marks)**
- 1.3 (c) Prepare an email to Celine Kandage which explains, in relation to the final audit:
- the relationship between materiality for the financial statements as a whole and performance materiality; and
  - how the level of performance materiality, once established by Mocona, will affect the auditor’s decisions about audit testing.

**(6 marks)**

- 1.3 (d) Describe the following sample selection methods and explain how Toni Coleman could use each method to audit RDP's trade payables in relation to external specialists:
- random selection,
  - systematic selection.
- (4 marks)**
- 1.3 (e) Explain **two** substantive procedures that Mocona should undertake as part of the audit of accrued and deferred income. **(4 marks)**

**Total: 19 marks**

## Task 1.4

The programme idea for “A Wild Career” (**Advance Information: Appendix E**) has been developed further by Alina Oh, who recently joined RDP as a creative assistant. The programme specification requires participants aged between 17 and 19. They will live 24/7 at the wildlife park for up to one month during the competition, without contact with the outside world. They will be encouraged to form close bonds with the animals in their care. The production team will decide, based on how entertaining the participants are, who will be removed from the park at the end of each episode. Participants will be removed without warning and with no opportunity to say goodbye. Similar programmes, made by RDP’s competitors, involved adults who found the experience, and the media coverage the programme attracts, psychologically damaging.

Izzy Gratz, the creative director, wants to co-produce the programme with another indie, Swerve Co, which has in-house experience in making programmes involving animals. Alina has had long conversations with the creative team at Swerve Co so they already know the details of the programme idea.

During a recent conversation, however, Otis expressed his continuing doubts to Josh Penfold, the CEO:

‘I don’t think the content of and process for making “A Wild Career” will allow us to remain compliant with either Ofcom rules or our own statement on business ethics (**Advance Information: Background on the TV industry and Appendix A**).

‘Also, the questionable behaviour of Sammy Rayner, the CEO at Swerve Co, is well-known throughout the TV production industry. It makes me particularly uncomfortable given that, like myself, Sammy is an ICAEW Chartered Accountant.

‘It’s unfortunate that Swerve Co now know so much about “A Wild Career” as this may limit our ability to co-produce the programme with alternative indies.

‘Having said all that, Swerve Co is the best in the business for this sort of programme and we will maximise the commission price from a client if we co-produce with Swerve Co.’

Josh responded that, at the next board meeting, he requires Otis to ignore his doubts and vote in favour of seeking a commission for “A Wild Career” based on it being co-produced with Swerve Co.

### Requirements

- 1.4 (a) Explain **three** ways in which the plan for “A Wild Career” fails to comply with RDP’s statement on business ethics. **(6 marks)**
- 1.4 (b) Explain the issues of professional ethics that should determine whether Otis, as an ICAEW Chartered Accountant, votes in favour of RDP co-producing the programme with Swerve Co. **(5 marks)**

**Total: 11 marks**

**PLEASE TURN OVER**

## Task 2

This task consists of **three** parts worth 40 marks.

### Task 2.1

Otis asks you to help with some management information in respect of two programmes, “HighSchoolSports” and “The Mobile Kitchen” (**Advance Information: Appendix E**).

Josh is seeking a commission of £250,000 per episode for the six episodes of “HighSchoolSports”. He wants to identify the total cost budget for all six episodes that would achieve a 20% gross margin for RDP (**Advance Information: Appendix D**).

Selma Farouk, the production director, tells you that the final episode of “The Mobile Kitchen” will involve the remaining two teams in the competition providing dinner for prestigious functions at two hotels. Additional cast members will be present as guests and staff at the hotels. Catering, supplied by an external contractor, is required for all cast and crew members. Otis recognises that the cost budget of £23,000 for catering for the final episode is too low. 2,000 meals are expected to be served to cast and crew during production of the final episode. Catering costs are semi-variable as they include fixed costs plus the cost per meal served.

You are given the following actual catering costs for the first three episodes:

Episode	Catering cost £	Number of meals served
1	22,500	1,785
2	24,000	1,935
3	23,600	1,820

### Requirements

- 2.1 (a) The approach to costing that is taken by RDP in relation to “HighSchoolSports” is termed:
- A Lifecycle costing
  - B Target costing
  - C Process costing
- (1 mark)**
- 2.1 (b) Calculate the total cost budget for all six “HighSchoolSports” episodes.
- (2 marks)**
- 2.1 (c) In relation to the “The Mobile Kitchen”, calculate:
- the fixed and variable elements of catering costs, using the high-low method; and



- the forecast overrun for catering costs for the final episode.

**(7 marks)**

2.1 (d) Explain:

- **one** action that RDP could take immediately to avoid the forecast catering cost overrun for the final episode of “The Mobile Kitchen”; and
- **one** other action that RDP could take to increase RDP’s total profit on the programme as a whole.

**(4 marks)**

**Total: 14 marks**

## Task 2.2

Following the board discussion on 12 October 2020 about obtaining commissions from streaming services (**Advance Information: Appendices E and G**), Otis has established that:

- data is collected by streaming services continuously and in huge quantities from a great many sources, including social media
- much of the data is collected then used in real time
- some of the data is derived from the internet of things, so it is generally judged to be reliable, but it requires the application of data analytics before it can be used.

The sporting event on which the documentary “Cheer Me On” is based (**Advance Information: Appendix E**) was cancelled in November, before any recording of the programme started. RDP wrote to the relevant external specialists to terminate their contracts due to frustration of contract. One specialist wrote back claiming redundancy, another wrote back claiming damages for breach of contract and a third wrote back seeking reimbursement of expenses.

Otis knows that you have studied these topics recently. He asks you to explain some of the data issues involved in more detail, and also RDP’s legal position in light of the contracts in place with external specialists for “Cheer Me On” (**Advance Information: Production function**).

### Requirements

2.2 (a) Explain:

- whether the data captured by streaming services demonstrates the four Vs characteristics of big data; and
- how data analytics allows big data to be used for decision-making by streaming services.

**(6 marks)**

2.2 (b) Explain, in relation to the “Cheer Me On” programme:

- whether RDP is correct in stating that termination of the contracts was caused by frustration of contract;
- whether RDP’s contracts with external specialists can give rise to redundancy claims; and
- whether RDP is liable to pay damages or to reimburse expenses.

**(6 marks)**

**Total: 12 marks**

## Task 2.3

At the end of November 2020:

- TVStandard told Josh that it would not be commissioning the production of “Work Gym” (**Advance Information: Appendix E**) with RDP because it has chosen a new indie which has a younger production team.
- Josh received notice from a client that Ofcom may impose a financial penalty due to a breach of its rules in a TV programme that RDP made for the client in the summer of 2020. The amount of the penalty has not yet been quantified but the publicity surrounding it will be damaging for RDP’s reputation.

The directors had not been expecting either of these events, and they are concerned that RDP’s scale of activities will now start to contract as a result. They have revived the ideas discussed at the October board meeting, of:

- raising long-term finance to acquire new premises, expand RDP’s types of programme beyond reality TV and extend its client range to include streaming services; and
- drafting a mission statement.

The directors could approach a known group of business angels or RDP’s bank for some new finance. In addition, they were approached some time ago by advisers who want to help RDP achieve an AIM listing. Otis asks you to prepare some explanations for the board in relation to these matters.

The directors have decided to review RDP’s strategy, starting with a SWOT analysis. Otis has prepared an analysis of RDP’s strengths and opportunities. He asks you to add to it in relation to current weaknesses and threats.

### Requirements

- 2.3 (a) Briefly explain whether it is appropriate for RDP to seek the required long-term finance from each of the following sources:
- business angels
  - an AIM listing
  - additional debentures.
- (6 marks)**
- 2.3 (b) Explain the purpose and benefits of a mission statement for RDP. **(4 marks)**
- 2.3 (c) Explain **two** weaknesses and **two** threats that are relevant for RDP as at today’s date. **(4 marks)**

**Total: 14 marks**