



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.

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.

The exam will contain questions with additional information which will complete the description of the Role Simulation scenario and state the Role Simulation requirements.

The examination is based on the 2021 Role Simulation Workbook and the 2020 Certificate 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.

Preparing your answers in the exam

You will need to refer to your copy of the Advance Information during the exam.

Respond directly to the exam question requirements. Do not include any content or opinion of a personal nature, this includes your name or any other identifying content.

You may use a pen and paper for draft workings. Any information you write on paper will not be read or marked.

The examiner will take account of the way in which your answers are structured. You must make sure your answers and workings are clearly visible in the word processing area when you submit your exam. Only your answer in the word processing area will be marked. **You must copy over any data from the spreadsheet area to the word processing area for marking.** The examiner will **not** be able to expand rows or columns where content is not visible.

Carmenta Ltd

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This document reflects information available as at 12 January 2021.

Introduction: Carmenta Ltd

'In order to be irreplaceable one must always be different.'

Coco Chanel

Carmenta Ltd (Carmenta) is a UK-based company which manufactures and sells visually striking, high quality personal accessories, such as purses, keyrings and notebooks. Carmenta operates as a differentiator in its markets.

Accessories industry information

In the UK accessories industry, fashionable personal items are sold at all levels of quality and price. Market stalls, supermarkets and large retail chains sell bags, notebooks, diaries, purses and wallets cheaply and in large quantities. Higher quality, higher priced accessories, like those produced by Carmenta, tend to be sold by department stores and by upmarket small retailers. Online sales are increasingly important. Luxury fashion designers have their own ranges of exclusive accessories, such as bespoke handbags, that can sell for thousands of pounds.

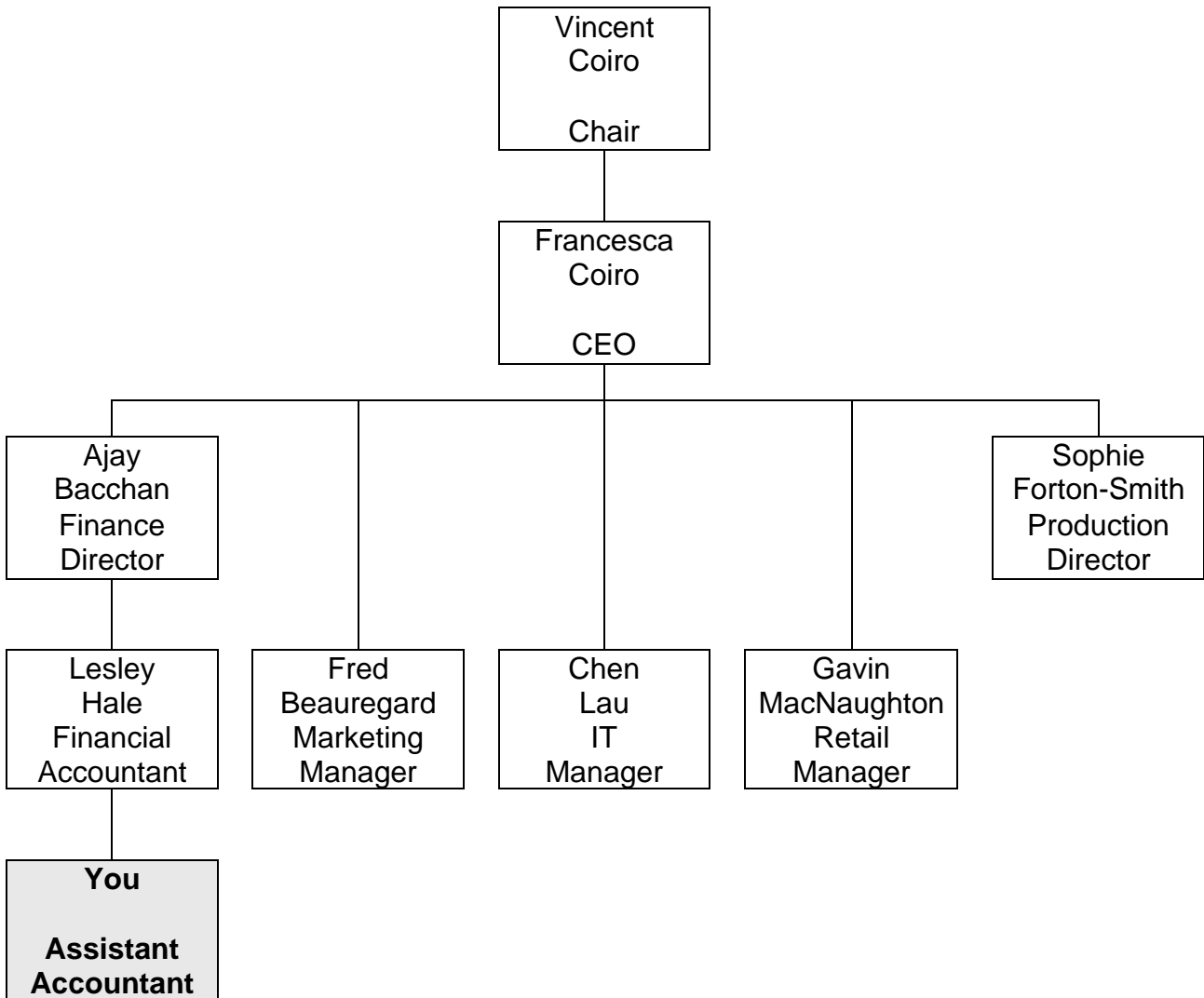
The industry is fragmented with a large number of manufacturers. At the lower end, products are mass-produced and distributed globally. At the higher end, artisans work with traditional materials and produce high quality, long-lasting, hand-made items.

Sales volumes of specific types of product have changed over time. For example, sales of paper diaries and photo albums have declined in recent years, and sales of new accessories such as mobile phone cases and tablet holders have increased.

Organisational structure and ownership

Carmenta was founded in 1905 by Giovanni Coiro. Its head office is in a converted country house in southern England and there is a purpose-built manufacturing facility next door.

Extract from organisational chart



Key personnel

Vincent Coiro, Giovanni's great-grandson, started work in the business in 1990 and took over from his father as Chair in 2012. Francesca Coiro is Vincent's daughter. She took on the role of CEO from Vincent in 2012, when Vincent became Chair.

The board of directors comprises Ajay Bacchan, the Finance Director, and Sophie Forton-Smith, the Production Director, as well as Vincent and Francesca. There is a formal board meeting every three months. The most recent meeting was held on 14 December 2020 and the next meeting will be held on 22 March 2021.

You are employed by Carmenta as an assistant accountant. You have been working there for just over one year and you are training to be an ICAEW Chartered Accountant. You report to Lesley Hale, the Financial Accountant. Both Ajay and Lesley are ICAEW

Chartered Accountants. The Staff Code of Conduct applies to all employees and directors of the company (see **Appendix C**).

Gisele Taylor is studying accounting at college. She is a placement student and works at Carmenta on one day per week in order to gain experience. You have been explaining some of your work to Gisele to help her in her studies.

Ownership

All the shares are held by members of the Coiro family. Vincent owns 60% of the issued shares and Francesca owns 20%. The remaining 20% is held by six other family members who take no part in the running of the business. These shareholders attend each AGM and, like Francesca, always vote the same way as Vincent.

Financial information

See **Appendix A** for extracts from Carmenta's financial statements for the year ended 31 December 2019 and **Appendix B** for details of accounting policies.

Production

Carmenta purchases raw materials such as leather, silver and paper from high quality, long-established suppliers with whom it has good relations. Many have been working with Carmenta for years and their managers are known personally to the directors. The suppliers are based in England, Scotland, Italy, Croatia and France.

The company has only one manufacturing facility, located in England, where it employs designers and manufacturing staff. Most of these employees are highly skilled and use traditional techniques that require a significant amount of expertise.

All Carmenta's products are of very high quality and made from traditional, natural materials. They are visually striking and often incorporate distinctive elements such as two contrasting colours of leather, irregular stitching or asymmetrical patterns. All items feature the company logo of a bird in flight. Each item is hand-made or hand-finished, differing slightly from others in details such as stitching and colours. See **Appendix D** for a list of the types of product made by Carmenta.

Over time, Carmenta has developed several different sub-brands, to appeal to new customers, with additional logos for use on these products. Carmenta has also purchased a small number of brands from other companies, which it has used with varying degrees of success. The intellectual property in all brands and logos is protected by registered trademarks.

Sales

Many customers have been purchasing Carmenta's products for a long time and it is common for customers to introduce their family members to the brand.

Carmenta has four sales channels:

Independent retailers

Approximately 60% of sales, by volume, are to independent retailers which sell products from many different manufacturers. These retailers are located all over the world. Carmenta has well-established relationships with many of the retailers. In many cases the retailer's directors or procurement managers are known personally to Vincent.

Carmenta shop

Carmenta operates one shop, in central London, which sells its full range of products to the general public. Customers who visit the shop in person can request for their items to be customised, for example by adding a monogram, selecting a preferred combination of different coloured leathers or even including design elements in precious metals and jewels from a menu of options. A member of the shop's staff works with the customer to help them specify the design of the finished item.

The shop is managed by Gavin MacNaughton, Retail Manager, who reports directly to Francesca. Sales from the shop form approximately 10% of sales by volume.

Online

Carmenta sells the full range of products online via its website. Customers can order monogramming online but cannot specify any other customisation. Orders placed by customers on the website are fulfilled by the staff at the Carmenta shop. Online sales form around 10% of sales by volume.

Corporate contracts

The remaining 20% of sales volume comprises items produced for corporate clients which they distribute to their own customers and/or staff. For example, Carmenta has contracts with several clients that regularly order notebooks and diaries carrying their own branding as well as Carmenta's logo.

Marketing

Carmenta places adverts in fashion magazines and on lifestyle-oriented websites. Carmenta's directors spend significant amounts of time and money building relationships with retailers, corporate clients and influential people such as magazine publishers and celebrities. Carmenta's directors are issued with corporate debit cards and credit cards to facilitate corporate entertaining. See **Appendix G** for details of these arrangements.

When Vincent was younger he became well-known for entertaining, sometimes flying to a different country just to take an important customer out for an expensive dinner. Magazine publishers are now regularly invited to social events hosted by Carmenta and are offered free products in exchange for additional editorial content or favourable advertising rates.

Over time, Vincent and Francesca have developed both formal and informal agreements with high-profile celebrities who act as brand ambassadors. They are regularly seen with the company's accessories on social media.

Receipts and payments

Carmenta pays all its suppliers and employees by bank transfer.

Independent retailers and corporate clients buy from Carmenta on credit and pay by bank transfer or cheque. Customers visiting the shop in person can pay by card or cash. Customers buying online pay by card.

Carmenta's policy is to minimise cash payments in order to reduce the risk associated with holding and managing cash and to minimise the risk of inadvertently becoming involved in money laundering (see **Appendix E**).

Recent and ongoing developments

Shop refurbishment

During 2020, Carmenta invested £1.12 million in refitting and refurbishing the Carmenta shop in central London. This was financed partly from cash and partly by increasing an existing long-term loan from £3.25 million to £3.75 million. Carmenta's bank readily agreed to an increase in the loan on the same terms as the existing loan.

For the month of December 2020, sales from the shop increased 10% year on year.

Product portfolio

The directors are concerned that Carmenta has no strategic overview of its product portfolio (see **Appendix D**). At the December 2020 board meeting, Francesca suggested assessing Carmenta's product portfolio and developing appropriate product strategies using the Boston Consulting Group (BCG) matrix. Following this review, the company intends to reduce the number of types of accessory that it produces and sells, so that resources are concentrated on accessories which generate positive net cash flows or which have the most potential to do so.

At the December 2020 board meeting, Francesca informed the board that she had recently agreed to sell 'Lion Diary', one of Carmenta's purchased brands, with its registered trademark, as it was not being actively used by Carmenta.

Project Greensleeves

Fred Beauregard, the Marketing Manager, has undertaken some preliminary market research and believes that there is a significant demand for luxury accessories made from products that are not of animal origin. Francesca and Fred have had two meetings with a large retailer which wishes to sell such accessories in the USA and India, marketing them as animal-free products and vegan-friendly. Carmenta is considering the purchase of 3D printing equipment to produce this type of accessory, using artificial materials rather than leather. Details of forecast additional revenue and expenses for this development, known as 'Project Greensleeves', are in **Appendix F**.

Francesca has asked Ajay to present a paper at the next board meeting that considers the net present value (NPV) and accounting rate of return (ARR) for Project Greensleeves to enable the directors to decide whether or not to invest in the project.

Technology

Carmenta is considering introducing digital technology in the design and manufacture of new products and in marketing and sales activities. For example, Carmenta could use design software to generate high quality detailed preview images of new products before producing them. More customers are asking to order customised items via the website and Carmenta could use software to allow customers to preview images of their items before deciding on the final customised design elements such as colour combinations.

At the board meeting in December, the directors agreed to investigate how Carmenta could offer online video consultations via the website, so that a customer shopping online could replicate the experience of speaking to a member of sales staff in the shop. The directors established a task force comprising Gavin MacNaughton, Sophie Forton-Smith and Chen Lau, the IT Manager. They agreed to investigate how intelligent systems, and automation, including artificial intelligence (AI), could be used by Carmenta in designing, manufacturing and selling.

External audit

Carmenta's current auditors are Harris LLP, appointed in 2015. The audit manager is Lucy Carpenter and the audit will be led by Sara Lien.

Lucy contacted Ajay to discuss plans for the audit of the financial statements for the year ended 31 December 2020. The final audit is expected to take place in mid-March 2021.

Lucy told Ajay that Harris LLP will not seek reappointment as auditors after they have completed the final audit because the firm wishes to move away from statutory audit work.

Ajay has asked Indigo LLP to tender for the audit of the 2021 financial statements. He told Lesley Hale to be prepared to provide Indigo LLP with any information they might need to undertake a risk assessment on Carmenta and to decide whether to accept the audit engagement. The risk assessment will involve assessing the factors which indicate risk is higher or lower than normal. Ajay is aware that Indigo will also communicate with Harris LLP.

More information about external audit issues is in **Appendix G**.

Appendix A – Carmenta Ltd financial statements for the year ended 31 December 2019 (extracts)

Statement of profit or loss for the year ended 31 December 2019

	£'000
Revenue	31,289
Cost of sales	(10,941)
Gross profit	<u>20,348</u>
Administrative expenses	(7,863)
Distribution costs	(9,121)
Profit from operations	<u>3,364</u>
Finance costs	(210)
Profit before tax	<u>3,154</u>
Income tax	(631)
Profit for the period	<u>2,523</u>

Statement of financial position as at 31 December 2019

	£'000	£'000
ASSETS		
Non-current assets		
Property, plant and equipment		6,119
Intangible assets		800
		<u>6,919</u>
Current assets		
Inventories	3,670	
Trade and other receivables	4,614	
Cash and cash equivalents	1,496	
	<u>9,780</u>	
Total assets		<u>16,699</u>
EQUITY AND LIABILITIES		
Equity		
Ordinary share capital (£1 shares)		1,000
Share premium		2,280
Retained earnings		7,795
Total equity		<u>11,075</u>
Non-current liabilities		
Borrowings		3,250
Current liabilities		
Trade and other payables	1,778	
Borrowings	255	
Income tax payable	341	
	<u>2,374</u>	
Total equity and liabilities		<u>16,699</u>

Statement of cash flows for the year ended 31 December 2019

	£'000
Cash flows from operating activities	
Profit before tax	3,154
Finance costs	210
Depreciation	854
Increase in inventories	(482)
Increase in trade and other receivables	(986)
Increase in trade and other payables	49
Cash generated from operations	<u>2,799</u>
Interest paid	(210)
Income tax paid	(595)
Net cash from operating activities	<u>1,994</u>
Cash flows from investing activities	
Purchase of property, plant and equipment	(130)
Net cash used in investing activities	<u>(130)</u>
Cash flows from financing activities	
Dividends paid	(1,250)
Net cash used in financing activities	<u>(1,250)</u>
Net increase in cash and cash equivalents	614
Cash and cash equivalents at 1 January 2019	<u>882</u>
Cash and cash equivalents at 31 December 2019	<u>1,496</u>

Appendix B – Accounting policies (extracts)

Introduction

Assets, liabilities, expenses, income and equity items are recognised and measured in the financial statements in accordance with International Financial Reporting Standards (IFRS) and the Conceptual Framework for Financial Reporting. The financial statements are prepared using the accrual basis of accounting in accordance with IFRS.

Intangible assets

Intangible assets include registered trademarks and acquired brands. Registration of trademarks is renewable indefinitely at minimal cost. Trademarks and brands have indefinite lives and are not amortised. They are subject to annual impairment tests.

Property, plant and equipment

Property, plant and equipment is accounted for using the cost model and is measured at cost less accumulated depreciation and impairment losses. Freehold land has an indefinite life and is not depreciated. Buildings are usually depreciated monthly over an estimated total useful life of 40 years, plant and equipment are usually depreciated monthly over an estimated total useful life of 10 years, both taking into account residual values. Depreciation is recognised in administrative expenses. Property, plant and equipment are reviewed at the end of each reporting period for any indications of impairment.

Appendix C – Staff Code of Conduct (extracts)

Introduction

This Code applies to all employees and directors of the company and forms part of your contract of employment with Carmenta Ltd.

Professional behaviour

All directors and employees are expected to act in a manner which is professional, courteous and ethical when dealing with colleagues, suppliers and customers.

Directors and employees who are members of a professional body (either qualified or in training) must act in accordance with both this Code and the ethical and professional requirements of their professional body.

Corporate entertaining

Directors and authorised managers are encouraged to entertain business contacts for the purpose of better promoting the company and its products, provided the costs incurred are appropriate, proportionate and reasonable.

Concerns

Staff wishing to raise a concern or grievance should, in the first instance, do so with their immediate line manager. If this is not possible or appropriate, or if this does not resolve the issue, they should approach a more senior manager.

Appendix D – Product portfolio

The directors have been concerned that some of Carmenta’s products are suffering from declining sales.

Fred Beauregard has prepared an initial analysis of Carmenta’s product groups, excluding products sold only to corporate customers. The market growth rate for each product group is based on the mean annual market growth rate in the three years 2018, 2019 and 2020.

Product group	Market growth rate
Stationery – diaries, notebooks, notebook holders and folios	low
Cases – cases for mobile phones, laptops and tablets	high
Bags – handbags, purses, wallets and cardholders	high
Keyrings – keyrings and key fobs	low

Appendix E – Email from finance director to finance team

Ajay Bacchan has sent the following email to the finance team .

Date: 11 January 2021
To: Finance team
From: Ajay Bacchan

Subject: Cash payments and money laundering

Dear colleagues

As part of my responsibility for risk management I have reviewed our policies and practices on cash payments and their associated risks, including money laundering.

In line with Carmenta's strategy of minimising the risk of inadvertently committing or facilitating money laundering, the company's policy is to minimise cash transactions. In accordance with this policy, all our corporate clients pay by bank transfer or cheque and we pay all our suppliers by bank transfer.

Earlier this year, one of our suppliers enquired about the possibility of being paid in cash and we were very clear that we would not agree to this.

A few weeks ago, Vincent handed me some cash and told me that it was from Tony Travers, the chief executive officer of Serendipity Ltd. He had paid an invoice by cash during a lunch meeting with Vincent. Vincent didn't even think to ask him what it related to and it took me a while to match it to an invoice.

I asked Vincent to remind Tony that our policy is to require payment by bank transfer and in general I am trying to encourage the directors to keep better records and to follow our systems.

Regards

Ajay

Appendix F – Project Greensleeves

Fred Beauregard has prepared the following information about the potential purchase and use of 3D printing equipment for Project Greensleeves. Fred has assumed that the investment would take place and operations would start in early 2022.

Revenue

Fred has forecast the total additional revenue from Greensleeves products as follows:

	Year ending 31 December				
2022	2023	2024	2025	2026	
£'000	£'000	£'000	£'000	£'000	
700	1,050	1,200	1,350	1,500	

Investment in new equipment

The new 3D printing equipment will be purchased and installed on 1 January 2022. The cost of purchasing the equipment is estimated at £1,600,000. Installation costs are estimated at £120,000. The equipment is forecast to have an operating life of five years.

Marketing support

An initial marketing campaign will run for one year from January 2022, at a cost to be determined.

Other operating costs

Fred has made the following estimates of other operating costs:

- variable costs would be 20% of sales revenue;
- depreciation would be £344,000 per year, based on the five year operating life of the 3D printing equipment and assuming no residual value.

Appendix G – External audit issues

Lesley Hale has told you that you will be helping to prepare information for the auditors during the final audit. She has given you some briefing notes about audit issues.

Window dressing

On 31 December 2019 a bank transfer of £372,000 was received from a retailer in respect of an order placed and despatched on 19 December 2019. The auditors were initially suspicious because the order was unusually large, representing approximately four months of normal sales to the retailer, and the retailer usually took 30 days credit. However there were no subsequent returns from this customer in 2020 and the auditors concluded that this was not window dressing.

We can expect that the auditors will be particularly alert to the possibility of window dressing in the 2020 accounts and they will be testing for that.

Receivables collection

The receivables collection period has been steadily increasing this year. This is a concern for Ajay and we need to better manage the collection of receivables.

For example, in November 2020, Alpha Ltd, a customer owing £172,000, was declared insolvent. At that time we were awaiting payment of two invoices, both of which were over 60 days old, even though our contract with Alpha specified a payment period of 30 days.

Ajay is due to discuss these issues at the next board meeting in March. He has asked me to calculate the receivables collection period and propose ways to reduce it. In the meantime, you should be aware that the auditors will probably focus on receivables during the final audit.

Directors' expenses, cash balances and cash management

All directors are issued with corporate debit cards and credit cards. The directors should use these cards to pay for expenses. The directors can also use the cards to make cash withdrawals (for example if they are travelling overseas and need local currency). Directors should provide receipts for all transactions, including cash transactions, and confirm how much cash they are holding, each month. However, sometimes they are late in doing so and they do not always have receipts. This creates problems when preparing bank reconciliations since it is not always possible to confirm how much cash has been spent and how much cash the directors are holding.

Sara Lien, who is leading the external audit by Harris LLP, has already contacted Carmenta's bank to confirm bank balances as at 31 December 2020 and has discovered a number of discrepancies. I explained to Sara that I had not yet accounted for cash balances held by directors and cash expenses incurred by them. I also explained that Carmenta recently opened a new account, at our current bank, denominated in US dollars. This account has a zero balance at the moment; because it is used only to receive payments from a retailer based in the USA who insisted on paying us in US dollars.