

# Final Admitting Examination



## PAPER 2 FAE CORE SIMULATIONS

SUMMER 2016 (Wednesday 17<sup>th</sup> August 2016: 10.00 am – 2.30 pm)

### INSTRUCTIONS TO CANDIDATES

1. Answer **ALL** Simulations.
2. Two answer books are provided (marked Case Study 1 and Case Study 2). Please answer each Simulation / Case Study in the correct answer book.
3. The first 30 minutes of this examination is dedicated to reading time.  
  
During this time, candidates may make notes on their examination paper or on their own paper and refer to their materials.  
  
Candidates are **NOT** permitted to open their answer books until instructed to do so.
4. Candidates should indicate clearly whether they are answering the paper in accordance with the law and practice of Northern Ireland or the Republic of Ireland.
5. Taxation:  
Candidates answering the paper in accordance with the law and practice of the Republic of Ireland should answer in accordance with the appropriate provisions up to and including the Finance Act 2014.  
  
Candidates answering the paper in accordance with the law and practice of Northern Ireland should answer in accordance with the appropriate provisions up to and including the Finance Act 2015.
6. Candidates should deem each monetary amount shown with the €/£ symbol to be stated in their relevant currency.
7. All workings should be shown.
8. **Simulation 1** begins overleaf.  
**All appendices are provided in a separate insert.**

**SIM1: NISSI LTD***(Suggested time: 120 minutes)*

You are Sarah Abraham, a recently qualified chartered accountant working in a small firm of accountants called Ebenezer Associates (“EA”). The partners in your firm have agreed for you to go on secondment to a client for nine months, to cover for their financial accountant, Jude Patmos, who is on maternity leave.

Timothy Jason, a partner in EA, informs you that the client you will be working for is a small Irish, privately owned, fashion retailer called NISSI to whom EA have provided advisory services in the past. Timothy explains “NISSI Ltd nearly went under a few years ago but our Business Recovery Team helped them through a difficult time and the business has been turned around. They are now profit making and in fact have plans to expand. I think this is a great development opportunity for you personally and it will be a great help to NISSI over the next few months.” You are excited by this opportunity to get some experience working in industry and tomorrow will be your first day on secondment.

You arrive early, eager to impress, and wait in reception for the Finance Director, Mary Jacobs. “Good morning, you must be Sarah,” Mary says as she walks through the main doors of the premises. “I’m so glad to see you and it’s wonderful that you were able to start today. We’ll obviously let you get settled at your desk and then I can catch up with you later this morning and run through the priorities for the next few days.”

**Accounts**

Later that morning you go to Mary’s office to discuss the immediate priorities over a cup of coffee. Mary begins by saying: “To get right down to business we have some deadlines fast approaching. Our last year-end was 31 December 2015 and I need to file those year-end accounts and complete the tax return as soon as possible. Jude has most of the work completed with regards to the tax return and the accounts, but I just need you to look at a few things to help me finish them off.”

Handing you a sheet of paper Mary says: “Here are the draft numbers for 2015 (see **Appendix I**). These are our management accounts which I will use to draft the statutory accounts, so you don’t need to be concerned about the presentation of the accounts – I will take care of that. As you can see it was a good year for us compared to 2014 and it’s great to see the business picking up after a few very bad years. I’m particularly pleased with how we were able to control our costs in 2015. The big saving was on rent. When our rental agreement came to an end on 30 June 2015 I successfully negotiated a new lease agreement which included a rent-free period for the first twelve months starting from 1 July 2015. That’s why our rental costs in the 2015 accounts are half of the 2014 balance. Of course to get that rent-free period I had to tie us into an agreement until 30 June 2020 with no break clause, but it was worth it to get the first year free. The annual rent for the remaining four years is at 80% of the 2014 figure, so all in all, a great deal for NISSI.”

“The reason I mention it is because Jude spoke to me before going off on maternity leave to say she thought there might need to be an adjustment made to the rental cost as a result of this new lease. I’m not sure what she was referring to but perhaps you could look into this and let me know if we need to make any adjustment? Just bear in mind that I will be producing the statutory accounts under International Accounting Standards.”

**Grant**

“You’ll also notice we increased our revenue and gross margin in 2015. We got a letter from the government on 29 December 2015 to confirm we would be eligible for a grant of up to €/\$ 200,000. This was great news and arrived in time for me to bring the grant income into the 2015 accounts. The €/\$ 200,000 is sitting in revenue; hence why the increased revenue and margin in 2015. The grant will go towards staff employment, training and development over a five year period starting on 1 January 2016. We simply need to do a claim each year against actual costs. The government will then reimburse us up to the €/\$ 200,000, i.e. €/\$ 40,000 per year. We haven’t received any money yet as our first claim will not be due in until January 2017 but the amount is within ‘Other receivables’ on the Statement of Financial Position.”

“A lot of hard work went into the business plan and grant application. I’m so glad it got approved in time for us to include it in the 2015 accounts - it really helped improve our margin! Jude wasn’t sure about recognising it in the accounts; I think she believed it shouldn’t be in revenue but perhaps somewhere else in the Statement of Comprehensive Income. Anyway, have a think about it and let me know if I need to move it.”

“So job one is to look at these financial reporting points and when you are happy with the year-end profit before tax figure, I would like you to then work out our year-end tax liability. Here is all of the relevant information you will need to complete the tax computation” (see **Appendix II**), says Mary as she hands you another piece of paper. “This is a summary of all the relevant tax information Jude said was necessary for the tax computation to be completed once we finalised the profit figure. You won’t need any other information and please ignore deferred taxation. However I would like to know the balance of losses we will have to carry forward along with the tax written down value of our general pool after you do this year’s current tax calculation. You will see we have accrued €/\$ 4,000 at the moment as an estimate for what the year-end position might be.”

“As a final document I would like you to produce a summary of all journals that I will need to post to adjust the accounts. The document should show any journals required with respect to the financial reporting items we have discussed and/or any tax journals required with regards to current tax.”

### **Other matters**

As you stand up and prepare to leave her office Mary calls after you, “One more thing....Jude is due back in nine months but has requested to go part-time upon her return. I want to facilitate this for her and originally thought about recruiting someone else who could job-share with her. However, I have now had another idea which I would like your feedback on. I have heard a lot about companies outsourcing some, or all, of their finance function. I thought this might be a good option for NISSI and reduce a lot of the work Jude currently does over a five-day week and perhaps it would enable her to return to a role which only requires her to work three days a week.

For example, I thought we could start by outsourcing payroll. I just don’t know enough about outsourcing finance responsibilities but I’m sure you have come across it! When you are emailing me the tax computation and any necessary journals, will you also let me know what the pros and cons are to outsourcing generally and specifically outsourcing payroll? Please also let me know whether or not you would recommend outsourcing as an option?”

You leave Mary’s office and head straight to your desk and start working on the tasks she has given you.

**END OF SIM1**

**SIM 2: BRILLIANT BREAKFASTS LTD***(Suggested time: 120 minutes)*

You are Caleb Harper, a qualified accountant at SUPER CEREALS PLC (“SC”). The company is listed on the FTSE 100, and is the largest cereal manufacturer in Europe. You have worked in the Group Internal Audit department for a year and after impressing your boss, you have now been given the opportunity to work as an Accountant in the Finance function of a recently acquired subsidiary, BRILLIANT BREAKFASTS Limited (“BB”). Earlier this year, SC acquired BB, a leading supplier of gluten-free cereals in Ireland, to expand the group’s footprint in this fast growing sector of the market. BB was founded 5 years ago by John Stephens, considered a visionary in this sector. He saw the gap in the market for people with a gluten intolerance to have a high quality breakfast cereal, and he succeeded by focusing on the things that mattered most to him: product quality, customer satisfaction, and staff retention. John felt that he had taken the company as far as he could, and was happy to sell his business to SC, while remaining on the board of BB as Chairman.

**Recent discovery**

The new BB Finance Director, Trudy Peters, greets you on your first day at BB and invites you into her office for a chat, where she doesn’t waste any time. “Caleb, you’re very welcome to the team” she begins, “as you will be aware from your time in the Group Internal Audit department, a fraud was recently discovered at BB. Management had manipulated the last set of quarter-end results this year through the posting of fictitious journals to boost revenue and thus profits. Needless to say, the people responsible have left the company and I have been hired to get the Finance Department back on track. I need some assistance from you.”

Trudy continues “I understand that you have strong knowledge of what good governance entails. John Stephens was the Managing Director for 3 years, and he was in charge of everything, before the company became too big. That’s when he stepped up to become Chairman, and he hired the Managing Director and Finance Director who were with the company for the last 2 years. They were the other two board members along with John, but they were the ones who together committed the fraud. John is an honest guy and felt that the Managing Director and Finance Director would just do the right thing and he trusted them. He later found out that staff had suspicions and concerns but had no avenue to highlight their concerns. The offenders have been replaced by the new Nomination Committee, with me as Finance Director and a new Managing Director who you’ll meet next week.

**Best practice**

SC would like to strengthen the board composition of BB from a governance point of view to reflect best practice and to this end; I would like you to write a report, outlining how we can improve the composition of our board. SC also wants to ensure that there is a mechanism for whistle-blowers to report any concerns that they have. I should add that the Group’s Audit Committee is responsible for the entire Group and is satisfied that no audit committee is required locally.”

“Governance is just the first step though. What we also need is for you to advise on internal controls, over the revenue and receivables cycle, that should be put in place to prevent this fraud occurring again. We have to be able to prevent manual fictitious revenue postings being made and fictitious accounts receivable balances being created. We need strong controls around the specific risks of existence of accounts receivable balances and the occurrence of revenue, to stop this happening again.” You interject to find out what controls are already in place. “There’s not much Caleb,” Trudy laments, “we’re starting from a low base – the auditors told me that we don’t have any revenue and receivable controls that they can rely on in their testing, so their audit is fully substantive. They have been recommending the implementation of controls for a couple of years. One thought I had is that you could ask our external auditors to provide a second person for a while to help with this. Can you please include in your report your initial thoughts and highlight some good controls that you have seen utilised elsewhere in the group from your time in the Internal Audit department that will address these specific risks.”

As Trudy pauses, you ask a very pertinent question, “Why did management commit the fraud Trudy? How were they to gain from this?” “Good question Caleb,” she responds, “Their bonuses were based on two things – revenue and profits. Manual fictitious revenue journals increased both.” You question whether this bonus structure is still in place and Trudy confirms it is, also noting “We’d like you to consider this in your report too. Can you outline the pros and cons of our current bonus structure? Then can you also make a recommendation as to whether we should change the management remuneration package by increasing base salary and reducing, or perhaps even removing, the bonus element related to revenue and profit so to reduce the incentive for management to commit fraud?. I also think that sound financial governance should be an incentive for management too.”

### **Future developments**

Before Trudy concludes the meeting, she has a further request. “Finally Caleb, we’re implementing a new product line. It’s a new range of ‘on-the-go,’ single portion per packet, gluten-free breakfast cereal bars. This will cater for the demands of customers who don’t have time to sit at the breakfast table for 15 minutes every morning. Aside from financial considerations, we think it’s feasible. I’m concerned however that we haven’t done an appropriate investment appraisal from a financial point of view so I’d like to you to perform a net present value calculation and conclude on the financial viability of the project. There’s a memo on your desk from our Operations Manager, Nicola O’Hara, which has all the information you need (see **Appendix I**) other than the Weighted Average Cost of Capital, which is 8% and for the purposes of this please do not worry about including tax considerations.”

“We want you to focus on this report immediately and it will go straight to the board at the end of the week. I’ll be travelling until Friday, so I’ve made sure that you have enough information to conclude the report in my absence. Welcome to Brilliant Breakfasts Caleb, and best of luck!”

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