

# ICMAP Pathway Exam

Tuesday 15 June 2021

**Time allowed**

4 hours including reading, planning and reflective time.

This question paper is an integrated case study with two questions containing a total of 100 marks and ALL questions must be completed.

All questions contain Professional Skills marks which are included in the marks shown.

**Do NOT open this question paper until instructed by the supervisor.**

**You must NOT write in your answer booklet until instructed by the supervisor.**

**This question paper must not be removed from the examination hall**

# Paper IPE

**ACCA**

Think Ahead

The Association of  
Chartered Certified  
Accountants

## **1 Company background**

Fun Holidays (FH) was established forty years ago by its founder Fritz Janssen, an experienced travel industry professional. He developed a new holiday concept idea, where he would guarantee that any customers going on holiday with FH would have “fun” and if they did not, he would refund them the cost of the holiday.

At the time this was a very innovative promotional idea for businesses in the travel industry, but Fritz was confident that he knew the requirements for a “fun holiday”. He believed that as a new start-up travel business, he would need an aggressive, albeit risky, marketing strategy to encourage customers to try out a “fun holiday” with FH.

Through a combination of the right service, staff, accommodation, location and activities, FH delivered what it promised to 99% of its customers in those early years, and FH used this as a platform to establish itself as a major travel holiday company. Since its inception FH has continued to grow and has become well established in Gerland, its home country. Although it is still known for its fun holidays, it no longer offers its customers a refund if they do not have fun.

Gerland is a developed country with a population of 80 million and high levels of employment due to its educated and skilled workforce, and Gerland is currently experiencing growth in most sectors of the economy. Gerlanders (the name given to people from Gerland) like to spend their high levels of disposable income going on several holidays each year to various warm and sunny countries overseas. FH became a listed company in Gerland in 2010, following Fritz’s retirement from the board. Fritz’s son, Karl Janssen, is now the Chief Executive Officer (CEO), and is head of the management board reporting into a supervisory board. This two-tier board structure is common for listed companies in Gerland.

### **The current environment**

Karl has established a reputation as a capable and very efficient business leader and has been the key driver behind FH’s growth to becoming the number one holiday travel company in Gerland. FH now takes more Gerlanders on holiday than any other travel company, and FH’s success has been very much aligned with Gerland’s own progression as one of the worlds’ wealthiest countries. To this point FH has only provided holidays to “short haul” destinations, which the travel industry classifies as any destinations within 6 hours flying time. Those destinations beyond 6 hours flying time are classed as “long haul”.

FH has contracts with several different airlines in Gerland, who will fly FH customers to various destinations throughout the year. This arrangement has worked well in the past when FH was confident of customer numbers and, therefore, willing to enter into annual contracts with airlines with agreed passenger capacity levels, as FH was able to fill these planes with holidaymakers on a consistent basis.

However, given increasing competition, which has resulted in lower passenger numbers and rising airline costs, particularly fuel, and the fixed nature of the airline contracts, FH’s margins are now coming under severe pressure.

### **Shareholder forums**

Shareholders have duly been happy with Karl and FH's performance to date but are now concerned about possible future returns given Gerland's maturing holiday market, and the increasing competitive rivalry from both home and overseas travel companies. FH hosts quarterly forums with its major shareholders, which is an opportunity for the management and supervisory board members to engage with shareholders in a more informal environment, to discuss performance and future plans.

At the last shareholder forum it was agreed that the management board would consider options that would secure continued future returns and to report back to shareholders at the next forum meeting. During this meeting shareholders expressed a preference for FH to remain focused on the holiday product, but to consider ways that they could improve margins and still maintain their leading position in Gerland. Shareholders did also suggest that they may be willing to inject further funds and encouraged the board to consider opportunities outside of Gerland.

### **New opportunity**

The management board has been exploring options to maintain FH's level of returns and have identified the possible acquisition of a majority shareholding in iFly.

iFly is an established airline in Veeland, which is located 1,000 kilometres from Gerland. The climate and economic conditions in Veeland and Gerland are very similar, with customers having very similar preferences and budgets for overseas holidays.

In its early years of operating, iFly flew customers from Veeland to overseas destinations, generally within two to three hours flying time. However, iFly has expanded significantly in recent years by flying to much further destinations – up to 10 hours flying time – to take advantage of the growing market for long haul travel.

iFly is listed on the Veeland stock exchange and operates a unitary board, which currently comprises eight directors - five independent non-executive directors, including the chair, and three executive directors, including the Chief Executive Officer (CEO) and the Chief Operating Officer (COO), who are the two original founders of iFly. All directors have been on the iFly board for at least 5 years. The Veeland Corporate Governance Code was recently established and it allows listed companies flexibility to follow a unitary or two-tier approach to their governance, although to this point, a unitary approach is favoured by the majority of Veeland listed companies and their institutional investors.

Karl would like iFly to continue as a Veeland-based company following any acquisition, as it would help position FH as a global travel company. The supervisory board at FH, however, is unfamiliar with iFly's current unitary board structure and would, therefore, need to be convinced that such a structure can work effectively in practice after acquisition.

Recently an anonymous email, from a concerned iFly director, has been received by Karl Janssen regarding an issue at iFly.

A member of Karl's management team has managed to meet, informally, with the director

that sent the anonymous email (Exhibit 1) and during this meeting the iFly director provided evidence to support their claims, and FH is now confident that the claims made are an accurate reflection of recent events between iFly and its airline partner, Flyline. Before FH continues further with a potential acquisition of iFly, Karl would like advice to consider the ethical issues identified in the email.

You are an external consultant hired by Karl Janssen to assist him in addressing a number of issues surrounding the potential iFly acquisition.

**Required:**

**(a) Prepare a briefing note to the FH supervisory board that evaluates the following options if FH were to acquire iFly:**

- 1. iFly to maintain its unitary board structure; or**
- 2. FH to impose a two-tier board structure on iFly.**

**Recommend which option FH should select and clearly state your reasons.**

**(16 marks)**

**Professional skills marks are available for demonstrating *evaluation* skills in assessing the two potential board structure approaches that FH could select following the acquisition of iFly.**

**(4 marks)**

**(b) Prepare an email to Karl Janssen which assesses iFly's decision to continue flying the Express aircraft using Tucker's five question approach and advise Karl as to what action he should now take.**

**(14 marks)**

**Professional skills marks are available for demonstrating *scepticism* in challenging iFly's decision to continue flying the Express aircraft.**

**(3 marks)**

The next step in the assessment of iFly as a potential acquisition target will be to identify financial information that can assist FH in its evaluation of iFly. To help prepare for the next FH senior management meeting, Karl has asked you what characteristics financial information should exhibit for it to be useful for the FH board.

**(c) Prepare two presentation slides, and supporting notes, for Karl to share with his management team, which:**

**i. explain the qualitative characteristics required for financial information to be useful; and**

**(4 marks)**

**ii. specify sources of financial information that may be relevant in relation to iFly explaining why each source will be useful to FH.**

**(6 marks)**

**Professional skills marks are available for demonstrating *communication* skills in presenting concisely and effectively the qualitative characteristics of financial information and the sources relevant to FH.**

**(3 marks)**

**(50 marks)**

**Exhibit 1: A copy of an email received by Karl Janssen regarding an issue at iFly.**

**CONFIDENTIAL**

To: karljanssen@funholidays.com  
From: anonymous@ifly.com  
Subject: iFly is risking the lives of passengers and crew!

Good morning Mr Janssen,

I am writing to you as I am aware that FH may be interested in acquiring iFly, and I feel that I have a duty to inform you about some recent practices within iFly that cause me concern, and I am sure that they would also cause a problem for you and FH if you were to pursue an interest in this company. I have expressed my concerns internally to my fellow directors of iFly, but they do not appear willing to listen.

iFly has recently purchased 10 new "Express" model aircraft from the manufacturer, Flyline. This new aircraft has been developed by Flyline, who, as you know, is a global aircraft manufacturer, to satisfy three key objectives in aircraft design: increased safety, improved passenger comfort and greater efficiency in fuel costs.

Flyline agreed a heavily discounted deal with iFly for it to be the first airline to acquire and fly the new aircraft, and allow it to promote the aircraft as the "iFly Express", in order to provide a competitive advantage for iFly in the airline and holiday marketplace.

iFly has identified a possible safety fault within the design of the Express aircraft, which has recently caused iFly to make two emergency landings. iFly has not publicly stated this, and the recent incidents have simply been explained as operational precautions.

It is believed that Flyline has requested iFly to continue flying while it addresses the possible fault. Flyline does not believe the faults to be major, but cannot confirm this until further investigations have taken place. Flyline, however, has requested that iFly do not disclose this issue publicly, to ensure that there are no reputational issues for both Flyline and iFly. Flyline has also indicated that the favourable pricing on iFly's initial order could only be continued if iFly was to comply with Flyline's requests during this period of time until the fault is investigated and solved.

I trust that this information will be useful to you if you do enter negotiations to acquire iFly.

Regards

A very concerned iFly director.

## **2 Organisation background**

Experteez (EZ) is a fast growing management consultancy and professional services business. The business has a core of in-house employed consultants, which is complemented by a much wider network of associate consultants who are contracted to work on specific EZ client engagements.

EZ is privately owned by the original founders, who are three accountants that met during their time at university, and continued to discuss and develop the idea for this business while qualifying with large accountancy firms.

Through their early careers the founders developed wide networks of business contacts in many different sectors, and particularly at a senior level, which has been the basis of their success to date. Although a relatively new organisation, EZ has established effective working relationships with many large global, listed organisations, and has become the partner of choice for expert services for many of these companies.

EZ is seen as providing a very professional and reliable service that not only provides highly experienced experts, but, also delivers efficient support systems to make it easy for clients to do business with EZ. The founders pride themselves on this efficiency, which they recognised early as a source of competitive advantage.

For the year ending March 2021 the company achieved revenue of \$10 million for the first time in its history, and was able to secure a net margin of 15%. The revenue significantly exceeded the budgeted revenue of \$8 million for 20/21, and highlights the increasing demand for EZ's services on a global basis.

The founders have further ambitions for EZ, and would consider listing the business or selling the business to one of the large global consultancy firms in the short to medium term. They recognise that future investment will be required to grow, and are comfortable with diluting their current shareholdings for the right type of equity investor.

### **The finance function**

Up to this point all three founder directors have very much concentrated on growth, with the acquisition of new clients and the development of existing client relationships being the key internal drivers within EZ. One of the founders, Naomi Paton, fulfils the Finance Director (FD) role within EZ, and she has recognised that the drive for client growth has had a detrimental effect on the internal development of EZ, in terms of its staff, systems and processes.

There have been a number of recent problems within the EZ finance function, including over-expenditure compared to budget, delays to the month-end process and declining staff motivation levels. There is a feeling among the finance team that the founders have forgotten about them and now just expect them to continue to work longer and harder to satisfy the increased level of business.

The finance team are also aware that the consultants, both employed and associate, are paid significantly more than them, and are also eligible for bonus and commission payments based on the number of client engagements undertaken and client satisfaction ratings.

In order to address the motivational issues within the finance team, Naomi would like to introduce some form of incentive or reward scheme.

The finance function is by far the largest internal department within EZ and Naomi would now like to invest in this resource, as she sees it as key for supporting EZ's future growth aspirations. Naomi believes that an efficient finance function can be scalable to meet future business requirements and will add value to EZ in its plans for listing or future sale.

### **Budgeting**

EZ has always followed a fixed budgeting process, whereby budgets are prepared annually towards the end of the current financial year in preparation for the following year. The normal budget planning cycle would start in November and budgets would be finalised in January, ready for the new financial year from April to March. Monthly reports are then produced during the year, which provide a comparison of actual versus budgeted performance on a monthly and year-to-date basis.

Naomi feels that a growing professional services firm such as EZ should be using a more dynamic budgeting approach, to reflect the changing nature of the industry. In previous years, EZ has often reported large variances from its original budget early in the year, as new opportunities have arisen, which have required further, unbudgeted expenditure and/or investment, to achieve future returns.

### **Time recording system**

The typical month end process for EZ is 14 working days – the time taken from the closure of the ledgers at the end of the month to the distribution of internal management accounts.

This is primarily due to the manual time recording system that both its internal staff and associate consultants need to complete when booking time to client jobs. This system involves the following steps:

- EZ consultants work for clients
- Consultants complete a manual timesheet at the end of each month
- Timesheets are emailed to one of the founder directors
- The directors print out all timesheets and either approve or reject them
- Rejections are returned to consultants for explanation and/or amendment
- Once approved timesheets are passed to finance staff for input into a central database
- A report is produced from the database showing time booked per client
- Finance staff prepare client invoices using this information and input all invoices to the accounts system



Naomi would like to consider how technology could improve this time recording process to enable a much quicker month end, which results in reports being distributed at the end of working day 3 each month, rather than working day 14.

### **Asia revenue**

Given EZ's recent growth record, and their future plans, the directors are keen to ensure that any future performance continues to be aligned with forecasts, especially at the end of each quarter. Naomi has recently asked the Finance Manager to recognise revenue for a number of client engagements in Asia for the first quarter, and upon investigation the Finance Manager could not find any evidence that work has actually started and no time has currently been booked by EZ consultants. When Naomi was challenged on this issue, she abruptly said to "just do it" otherwise the month end process would be delayed further.

You are the new EZ Finance Manager, Jeff Chang, a qualified accountant, recruited by Naomi to help support her in developing the finance function to make it appropriate for the next stage of EZ's growth plans.

**Required:**

- (a) Prepare a note to Naomi and comment on the limitations of the current budgeting approach for EZ, and propose an alternative budgeting method, with reasons, for the directors to consider for future use in EZ.

(12 marks)

Professional skills marks are available for demonstrating *evaluation* skills in assessing the limitations of the current budgeting approach and presenting the most appropriate alternative approach which meets EZ's requirements.

(3 marks)

- (b) Prepare a briefing note for Naomi briefly explaining the concept of business process automation (BPA) and discuss how BPA could be used to improve the time recording process at EZ.

(10 marks)

Professional skills marks are available for demonstrating *analysis* skills in considering how the application of business process automation may improve EZ's time recording process.

(2 marks)

- (c) Prepare an email to Naomi that identifies the key principles of a good reward scheme and propose a scheme that may be introduced to the EZ finance team linked to an improvement in the month end process.

(8 marks)

Professional skills marks are available for demonstrating *commercial acumen* skills in using appropriate judgement to propose a suitable reward scheme for the EZ finance team.

(2 marks)

- (d) Draft an email to Naomi to discuss your concerns regarding the recognition of the first quarter revenue in Asia and briefly recommend any action that you feel is required.

(10 marks)

Professional skills marks are available for demonstrating *scepticism* in challenging Naomi regarding her request to recognise revenue.

(3 marks)

**(50 marks)**

**End of Question Paper**