ADVANCED LEVEL EXAMINATION

TUESDAY 20 JULY 2021

(3½ HOURS)

STRATEGIC BUSINESS MANAGEMENT

This exam consists of **two** questions (100 marks).

Marks breakdown

Question 1	60 marks
Question 2	40 marks

1. Please read the instructions on this page carefully before you begin your exam. If you have any questions, raise your hand and speak with the invigilator before you begin.

2. Please alert the invigilator immediately if you encounter any issues during the delivery of the exam. The invigilator cannot advise you on how to use the software. If you believe that your performance has been affected by any issues which occurred, you must request and complete a candidate incident report form at the end of the exam; this form must be submitted as part of any subsequent special consideration application.

3. Click on the **Start Exam** button to begin the exam. The exam timer will begin to count down. A warning is given five minutes before the exam ends. When the exam timer reaches zero, the exam will end. To end the exam early, press the **Finish** button.

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

5. The examiner will take account of the way in which answers are structured. Respond directly to the exam question requirements. Do not include any content or opinion of a personal nature. A student survey is provided post-exam for feedback purposes.

6. Ensure that all of your responses are visible on screen and are not hidden within cells. Your answers will be presented to the examiner exactly as they appear on screen.

The questions in this paper have been prepared on the assumption that candidates do not have a detailed knowledge of the types of organisations to which they relate. No additional credit will be given to candidates displaying such knowledge.

Question 1

Linx Plant Hire plc (LPH) hires out industrial equipment to business customers. The company is listed on the London Stock Exchange and has international operations.

LPH has a 30 June accounting year end.

You are an ICAEW Chartered Accountant who has recently joined the LPH strategic and operations management team. The head of that team, Abeni Abebe, called you into her office and opened the discussion:

“The LPH board is concerned about the company’s performance and financial position and is asking questions about the management of assets and operations. The board has asked me to report on a number of issues.

“I would like your help, as the finance director suddenly became ill last week and is likely to be off work for some time. I realise that you are new to LPH, so I have provided background notes and information on the LPH business model (**Exhibit 1**).

“The board would like an evaluation of LPH’s performance and financial position. The finance director has prepared financial and operating data (**Exhibit 2a**). The operations director has provided comments (**Exhibit 2b**).

“The finance director is concerned about the metrics which should be used in future to inform board-level decisions. He has provided notes, expressing some views (**Exhibit 3**), but he did not provide any supporting explanation or justification for his views before he became ill. The board would like an evaluation of the key metrics used.

“In July 2020, LPH made a significant investment in specialist assets for hire (Exhibit 1).

“In order to improve performance, the board decided to make a major investment in construction equipment for hire on 1 July 2022. The board wants to select the most appropriate method of financing this new construction equipment. I have provided details (**Exhibit 4**).

“In January 2020, LPH appointed a new head of digital technology, Sandra Simms, to support the improvement of asset management and revenue generation. In May 2020, Sandra introduced a new digital information system. The new system is functioning, but the board is concerned that the system is not being used effectively. The board would like advice on how the information made available by the new system can improve operational decisions by depot managers and others (**Exhibit 5**).

“I have set out instructions in a briefing note, explaining in detail what I would like you to do regarding the above matters (**Exhibit 6**).”

Requirement

Respond to Abeni’s instructions (Exhibit 6).

Total: 60 marks

Exhibit 1: Background notes and LPH business model – provided by Abeni Abebe

Company background

LPH hires out a wide range of industrial equipment (eg, plant, machinery, vehicles and machine tools) to business customers in a number of industries, including construction, manufacturing and civil engineering.

Industry and markets

Markets are highly competitive. Price is a key element of competition, but the speed and reliability of delivery are also important in responding to customers' urgent needs.

The UK equipment hire industry is diversified, with a wide range of company sizes. The top five companies make up 30% of the UK market, but many medium and smaller companies also operate in the industry. LPH has a 7% UK market share.

Customer demand varies according to factors such as: economic cycles, seasonality and variations in customers' short-term operating requirements.

LPH's customers vary in size from large multinationals to small construction companies. Most customers use a few equipment hire firms at the same time to satisfy their requirements for different types of equipment in different locations.

About 60% of LPH's revenue is generated in the UK. The remainder is generated in the rest of Europe, concentrated in specific geographical areas.

Business model

To date, LPH has purchased all equipment hired out to business customers. About 90% of hire contracts are short-term, being between one week and three months.

LPH owns the equipment for hire on average for six years. At the end of its useful life, each asset is sold on the used equipment market. Replacement equipment for hire is then purchased.

Maintenance of equipment for hire is a significant cost. Damage sometimes means that early replacement is necessary. There are also early disposals of equipment (before the end of their expected useful lives) to respond to the changing demands of customers.

In addition to replacements, there are new equipment purchases each year to expand the pool of available equipment for hire.

Market competitiveness is a key factor in considering the amount and timing of equipment purchase and disposal decisions. To be competitive, LPH needs to maintain an appropriate portfolio of equipment in the right locations, so it can deliver the right equipment, at the right time, at the right price. LPH delivers 90% of orders to customers within 24 hours of an order.

Equipment for hire utilisation rates are a key factor in generating revenue and profit. Predicting the appropriate quantity of each item of equipment to hold is essential if LPH is to meet variations in customer demand without incurring excessive unutilised time for equipment.

It is also important to store equipment for hire in an appropriate location. This saves costs and avoids delays in moving equipment long distances to customer locations.

LPH has 180 depots in the UK and Europe, each of which has a depot manager responsible for its operations. Each depot covers a designated local geographical area.

Each depot holds enough equipment for hire of each type, appropriate for the expected needs of the customers in its local area. However, if a depot cannot supply a customer order, it will request the equipment from another depot. Depot managers are important for business success in knowing and meeting the needs of local customers.

Five new UK depots were purchased and opened in the year ended 30 June 2021 at a total cost of £5 million.

Investment in specialist assets in July 2020

The operations director proposed the purchase of specialist assets for a major expansion of LPH's range of equipment for hire. After some discussion, the board supported this proposal and LPH purchased new specialist assets costing £30 million in July 2020.

The specialist assets were financed with a £30 million, 10-year, 4% bank loan.

The company's strategy is to use the specialist assets to penetrate new markets. The plan is to attract new types of customer who will hire, not only the specialist assets from LPH, but also other equipment.

The specialist assets acquired were in addition to purchases of normal asset replacements during the year ended 30 June 2021.

Management information for the year ended 30 June 2021 shows that the specialist assets had an average utilisation rate of 40% (calculated as the average days hired out as a proportion of days available to hire).

The operations director believes that the investment in specialist assets has increased LPH's revenue and profit for the year ended 30 June 2021 (Exhibit 2b).

Exhibit 2a: Financial and operating data – prepared by the finance director

Management information is provided as follows:

Summary statements of profit or loss for the years ended 30 June

	2021 Draft £m	**2020 Final £m**
Revenue	355	330
Cost of sales	(162)	(151)
Gross profit	193	179
Distribution and administration costs	(164)	(153)
Operating profit	29	26
Finance costs	(4)	(2)
Profit before tax	25	24
Tax	(5)	(5)
Profit for the year	20	19

Summary statements of financial position at 30 June

	2021 Draft £m	**2020 Final £m**
Non-current assets		
Equipment for hire	220	196
Other property, plant and equipment	35	31
Current assets		
Inventories	28	27
Trade and other receivables	75	53
Cash	10	5
Total assets	**368**	**312**
Equity		
£1 ordinary shares	23	23
Retained earnings	206	186
Non-current liabilities		
Bank loans	96	66
Current liabilities	43	37
Total equity and liabilities	**368**	**312**

Other financial data	**2021 £m**	**2020 £m**
EBITDA	70	62
Depreciation	41	36
Additions to equipment for hire:		
• New equipment for expansion (including specialist assets)	34	6
• Replacement equipment	37	39

Additions to other PPE (including new depots)	7	0
Net debt	86	61

Other operating data	**2021**	**2020**
Utilisation rate of equipment for hire	52%	56%
Average age of equipment for hire (months)	33	36
ROCE	8.9%	9.5%
Net debt as a multiple of EBITDA	1.23	0.98
Number of customers	25,200	24,100
Number of depots at 30 June	180	175

Exhibit 2b: Operations director's comments

The operating director commented on the result of his proposal to purchase new specialist assets as follows:

> "This has been a successful year for LPH. Profit has increased and that is the only key metric that really matters. I think this increase in profit is largely because of the new specialist assets, which have generated extra revenue of £5.6 million. Of the new customers we have attracted this year, I believe that about 800 are due to the new specialist assets."

Exhibit 3: Notes on performance monitoring – prepared by finance director

LPH currently reports to the board on monthly performance only for the company as a whole. The focus is on the following three key metrics:

(1) Return on capital employed (ROCE).

(2) Utilisation rate of equipment hired to customers (the average days hired out as a proportion of days available to hire).

(3) Net debt as a multiple of EBITDA.

I am not sure that all of these are good metrics to inform board-level decisions. Also, the board needs a more detailed analysis of monthly performance.

Exhibit 4: Proposals for financing construction equipment – provided by Abeni Abebe

The board has decided to acquire construction equipment for hire on 1 July 2022 with a value of £40 million.

The board is willing to consider a bank loan for the purchase of the construction equipment. However, the board is concerned that LPH’s gearing is already high and that banks will charge high rates of interest for increased borrowing.

LPH’s existing lending agreements contain restrictive covenants relating to gearing, so the board is anxious to minimise the recognition of liabilities in its statement of financial position. An additional bank loan of £40 million would take LPH close to breaching the restrictive covenants.

An alternative to a bank loan is for LPH to acquire the construction equipment by leasing from the manufacturer.

After consultation, LPH has identified two potential types of leasing contract to acquire the construction equipment for a six-year cycle:

- A six-year lease.
- Two consecutive three-year leases. New equipment would be provided by the manufacturer at the end of the first three years.

The finance director supplied the following information on the three financing choices for the construction equipment, but he became ill before he could provide any analysis or explanation:

<u>Choice 1 – Purchase with a bank loan</u>

The purchase of the construction equipment would cost £40 million. This amount can be borrowed from LPH’s relationship bank. Interest, payable annually, would be at 5%. The entire principal would be repayable on 30 June 2028. The construction equipment is expected to be sold on that date for its estimated residual value of £4 million.

<u>Choice 2 – lease on a six-year contract</u>

Lease rentals would be £8 million per year, payable by LPH to the equipment manufacturer as lessor. Lease payments would be made annually in advance for six years, commencing 1 July 2022.

All rights of use would revert to the lessor at the end of the lease agreement.

<u>Choice 3 – lease under two consecutive three-year contracts</u>

For the first period of three years, lease rentals would be £8.4 million per year, payable by LPH to the equipment manufacturer as lessor. Lease payments would be made annually in advance for three years, commencing 1 July 2022. The construction equipment would be identical to the equipment in the six-year lease.

The lease for the second period of three years is independent of the first three-year lease. New construction equipment would be provided by the manufacturer on 1 July 2025 and the previous equipment would be returned by LPH to the lessor.

Lease rentals on this second consecutive lease are expected to be £9 million per annum, payable by LPH to the equipment manufacturer as lessor. Payments would be made annually in advance for three years, commencing 1 July 2025.

All rights of use will revert to the lessor at the end of each lease agreement.

Working assumptions

- The construction equipment would initially all be acquired on 1 July 2022 and be available for use on that date.
- LPH will make a profit on hiring out the equipment, but the amount of profit is uncertain.
- LPH's annual weighted average cost of capital is 10%.
- As the rate implicit in the lease cannot be reliably determined, LPH uses the annual borrowing rate of 5% to discount lease payments.
- The corporate tax rate is 20%.
- Tax relief is given at the end of the period in which the expenditure is incurred.
- Lease rentals paid each year are allowable for tax. There is no tax depreciation (ie, no capital allowances) available on leased assets.
- Depreciation in the financial statements will be charged on a straight-line basis.
- Purchased equipment will attract a 15% reducing balance capital allowance in the year of expenditure and in every subsequent year of ownership by LPH, except the final year. In the final year, the difference between the equipment's tax written down value and its disposal proceeds will be treated either:
  - as a balancing allowance, if the disposal proceeds are less than the tax written down value; or
  - as a balancing charge, if the disposal proceeds are more than the tax written down value.

Exhibit 5: New digital information system – provided by Abeni Abebe

A new head of digital technology, Sandra Simms, was appointed in January 2020. On appointment, Sandra was set the objective of creating digital information systems to support the improvement of:

- Asset management
- Revenue generation

Sandra decided that LPH management needed a real-time software solution to locate and trace all equipment for hire and to maintain a record of all hiring transactions for each significant piece of equipment. She approached a business software provider, T-Soft, to deliver a solution.

T-Soft recommended a cloud-based system, hosted by T-Soft and accessed by LPH and its customers via the internet. Sandra agreed to this proposal and the new system was implemented in May 2020.

All items of equipment worth more than £3,000 are tagged and tracked using a radio frequency identification device (RFID). The new system is linked to the RFID. The system shows the location of each asset in real time and records a history of utilisation for LPH management. Financial transactions, including invoices, relating to each item are recorded and processed in the system.

The system generates management information at company-wide and depot levels. It includes a dashboard displaying key information for managers.

For each item of tagged equipment, the system tracks and records the location and movement of the equipment for hire from LPH's storage, transport, delivery to the customer, usage by the customer, subsequent return and back to storage by LPH.

The new system and dashboard can be accessed from a variety of devices, including mobile phones and tablets.

The board wants to understand how the information made available by the new system can be used by depot managers and others. In particular, it wants to improve asset management and revenue generation through better operational decision making.

However, depot managers are reluctant to use the new system. They are continuing to rely on their own experience and knowledge of individual customer needs in the local area covered by their depot.

Sandra has a computer science background, but not a business background and therefore needs some help in responding to the board.

Exhibit 6: Instructions – from Abeni Abebe

Prepare a report for the board. You should:

(1) Analyse and evaluate the performance and financial position of LPH for the year ended 30 June 2021, compared with the year ended 30 June 2020 (Exhibit 2a). Suggest reasons for changes in performance and financial position. Include an evaluation of the comments made by the operations director (Exhibit 2b).

(2) Explain:

  (a) the three key metrics currently reported to the board and evaluate the appropriateness of these metrics to inform board-level decisions (Exhibit 3). Further calculations are not required.

  (b) the benefits of reporting a more detailed analysis of monthly performance to the board. Identify and justify additional, appropriate performance measures.

(3) In respect of the financing of the construction equipment (Exhibit 4):

- Set out and explain the financial reporting treatment for each of the three financing choices over the six-year asset life cycle. Ignore taxation.

- Determine and justify the most appropriate method of financing from the three choices identified. Show supporting calculations for all three financing methods, including tax effects. Explain relevant financial and non-financial factors.

Use the working assumptions in Exhibit 4 and other available information.

(4) Explain how the new digital information system (Exhibit 5) can support operational decision making to improve:

- Asset management
- Revenue generation.

Question 2

Tallam plc is a global manufacturing company with three subsidiaries. It produces semiconductor devices (semiconductors) and integrated microelectronic circuits (IMCs).

Semiconductors and IMCs are used globally in the manufacture of electronic items in many industries.

The majority of Tallam's semiconductors are sold to external customers. However, some semiconductors are transferred internally to be used as components in Tallam's manufacture of IMCs.

You are Ashley, an ICAEW Chartered Accountant. You joined Tallam last week as an assistant to the finance director, Mike Reed.

Mike has just sent you the following email:

Dear Ashley

The board is concerned about Tallam's cash management and treasury activities, particularly in respect of multiple currency operations. The board is also concerned about foreign currency risks arising from our operating activities.

I need to report to the board about these concerns and I would like your help.

I have provided you with background information (**Exhibit 1**). I have also provided information on cash management and foreign currency risk (**Exhibit 2**).

In addition, the internal audit department raised some concerns to which I need to respond. I have provided you with details (**Exhibit 3**).

One final matter – yesterday, I received an anonymous letter from a treasury staff member making a complaint about the group treasurer, Linda Jones. As you will be aware, Tallam is a company which aims to uphold the highest ethical standards. I think it might be a good idea to discover who sent the letter and then discuss the matter with them in more detail. I have provided a copy of the anonymous letter that I received (**Exhibit 4**).

I have set out instructions explaining in detail what I would like you to do in respect of the above matters (**Exhibit 5**).

Thanks.

Mike

Requirement

Respond to the instructions from Mike Reed, the finance director, (Exhibit 5).

Total: 40 marks

Exhibit 1: Background information

Industry background

A semiconductor is a microscopic electronic component made from materials such as silicon. Semiconductors form an essential part of IMCs, which are used in many industries and end-user products including: smartphones, tablets, digital communications, medical equipment, wearable devices and computers. IMCs are typically less than one square centimetre and can contain many thousands of semiconductors.

The global semiconductor industry has shown a high average growth rate over many years. However, the trend has been volatile with periodic cycles of high and low growth rates.

Company background

Tallam has a 30 June accounting year end.

Tallam generated revenue of £6,000 million in the year ended 30 June 2021. It expects to achieve similar revenue in the year ending 30 June 2022.

At 30 June 2021, Tallam held a cash and cash equivalents balance of £87 million and has budgeted for this balance to rise to £107 million by 30 June 2022.

Tallam has three subsidiaries. Each subsidiary is a division operating from a single factory. The divisions are located in the UK, Germany and Malaysia.

Each division produces both IMCs and semiconductors.

IMCs

Each division produces IMCs which are specific to one industry:

- UK division – Aerospace industry
- German division – Digital communications industry
- Malaysian division – Computing industry

Each division sells its IMCs to global external customers operating in the related industry. For example, the UK division produces IMCs in the UK and sells them to aerospace customers worldwide.

Semiconductors

Each division produces a specific type of semiconductor to generate economies of scale. Semiconductors produced by each of the three divisions can be used in a number of different industries.

Each division sells about 75% of its semiconductors to external customers globally. The remaining semiconductors are transferred internally to other divisions, to be used as components in IMC production.

External sales and internal transfers

Each division makes global sales, which are normally invoiced in the currency of the country where the division is located. However, US sales are an exception and are invoiced in US$. The US is a major market for semiconductors and IMCs for all divisions.

While each division has some operating autonomy, transfer prices for interdivisional trading are set centrally by the Tallam board.

Internal transfers are invoiced in the currency of the country where the selling division is located. Balances outstanding between divisions are settled in cash on a monthly basis.

Exhibit 2: Cash management and foreign currency risk

<u>The treasury department</u>

On 1 July 2020, Tallam centralised its treasury department to co-ordinate the treasury activities of all three divisions. Previously, each division had operated its own treasury activities.

Also, on 1 July 2020, a new group treasurer, Linda Jones, was appointed.

The central treasury department manages foreign currency risks for the group as a whole.

<u>Cash management</u>

Tallam generates and uses cash in a variety of currencies. Given the multi-currency sales and costs and the multi-division transfers, cash flow forecasts for each currency are uncertain and are volatile.

The company's data analytics team carried out an analysis of net operating cash flows for Tallam's four major currencies. The team produced the following table showing the average amounts (mean) and variability (standard deviation) of monthly net operating cash inflows during the year ended 30 June 2021:

	Net operating cash inflows (per month)	
Currency	**Average (mean)**	**Standard deviation**
British pounds (£'000)	40,000	19,596
Euro (€'000)	27,500	22,000
Malaysian ringgit (RM'000)	75,000	30,000
US dollars (US$'000)	26,000	16,444

Exchange rates at 30 June 2021 were as follows:

£1 = €1.1 = RM5.0 = US$1.3

<u>Foreign currency risk</u>

The Tallam board is concerned that the group is not adequately managing its foreign currency risks.

In previous financial years, Tallam has not hedged its exposure to fluctuations in foreign currency exchange rates on operating cash flows. However, in the year ended 30 June 2021, following the centralisation of the treasury department, the company has started to use foreign currency derivatives to hedge currency risks on its operating cash flows.

<u>Interdivisional transactions and balances</u>

Tallam uses the £ as the base currency for hedging purposes and it is also the functional currency and presentation currency of Tallam for financial reporting purposes.

The trading of semiconductors between divisions creates significant interdivisional receivables and payables balances in multiple currencies between the three divisions.

Up to now, these interdivisional balances have been settled on a bilateral basis between the two divisions concerned.

The treasury department has made a proposal to introduce multilateral netting-off of interdivisional balances. The group treasurer has argued that the centralisation of the treasury department has made this possible.

Under this proposal, all divisions will inform the treasury department of their transactions with each other. The treasury department will then inform each division of the outstanding amounts payable or receivable to settle the balances arising from interdivisional transactions.

The board would like to understand how the proposed multilateral netting-off procedures would work and whether they would be beneficial for Tallam. As illustrative data, the interdivisional balances at 30 June 2021 were:

	Payables division		
	UK	**Germany**	**Malaysia**
Receivables division			
UK (£'000)	-	£24,000	£18,000
Germany (€'000)	€5,500	-	€11,000
Malaysia (RM'000)	RM35,000	RM50,000	-

The treasury department has stated that net settlements will be made in £ sterling. For illustration purposes, exchange rates at 30 June 2021 are to be used.

Exhibit 3: Internal audit department's concerns

The internal audit department has identified two concerns.

Concern 1 – Credit risk on foreign sales

A receivable of £12 million relating to the sale of semiconductors made by the UK division to a customer in Thailand remains outstanding. The semiconductors were delivered to the customer, LaserTeck, in January 2021 on credit terms of 90 days. A long period of credit was provided in order to win the contract.

LaserTeck is an existing customer which has paid on time in the past, although no previous sale to LaserTeck was more than £1 million. It is now known that LaserTeck is having financial difficulties.

The internal audit department's report on this matter stated:

> "We have concerns that credit risk on foreign sales is not being appropriately managed. The case of LaserTeck illustrates that enthusiasm to win a contract has, on occasion, meant that insufficient consideration has been given to the ability and willingness of a customer to settle amounts outstanding.
>
> "Significant losses caused by irrecoverable receivables have been incurred this year on a number of foreign sales contracts. The doubtful recoverability of the LaserTeck receivable is illustrative of our general concerns over receivables management on foreign sales.
>
> "We recommend that new procedures should be developed to manage credit risk on foreign sales contracts."

Concern 2 – Transfer pricing

Following up on an issue raised by the external auditors last year, the internal audit department reviewed the financial reporting and business implications of transfer pricing arrangements.

Semiconductors are sold internally to other divisions at an average mark-up of 10% on full cost. However, they are sold to external customers at an average mark-up of 30% on full cost.

The internal audit department's report recommended that we review the financial reporting and business issues arising from the differences between internal and external pricing arrangements.

Exhibit 4: Letter from anonymous member of treasury staff

I am writing to make senior management aware of concerns I have about the appropriateness of the behaviour of the group treasurer, Linda Jones. Other staff in the treasury department have the same concerns, but they are too afraid to share them with senior management.

Linda became ill suddenly last week. A number of treasury staff agreed that the tasks Linda normally carries out should be shared between us and we needed to access the necessary documents. Linda's desk was locked and there was no key available. It was decided by the treasury staff to force the desk open to find the documents.

Amongst the documents in the desk was correspondence that made it clear that many foreign currency hedging transactions undertaken by Linda were with Mooton Bank. The head of Mooton Bank's foreign currency department is Linda's brother, James.

I believe that Linda has been undertaking unapproved hedging transactions through Mooton Bank because her brother not only works there, but is directly operationally responsible for these transactions.

I also believe that the terms of these transactions were not as favourable for Tallam as similar transactions being offered by other banks at the same date. I have provided an example below of a forward contract entered into by Tallam as evidence.

This example shows Linda's notes which were found in her desk. It also shows my notes detailing an alternative transaction with another institution, Kimmel Bank, which Linda could have entered into on the same day.

<u>Linda's notes made on 31 March 2021 − Forward contract with Mooton Bank</u>

Current date: 31 March 2021.

On 30 June 2021, Tallam needs to pay US$4.8 million to a supplier of silicon.

On 31 March 2021, the £/US$ market spot rate was:

£1 = US$ 1.3110 – 1.3144

Mooton Bank has offered, on 31 March 2021, the following over-the-counter, forward contract to which I have agreed:

£/US$ Three-months forward 0.78 – 0.72 cents premium

<u>My notes − Alternative available transaction with Kimmel Bank</u>

I have identified the following alternative over-the-counter, forward contract with Kimmel Bank which Linda could have used on 31 March 2021:

£/US$ Three-months forward 0.80 – 0.73 cents premium

Exhibit 5: Instructions from Mike Reed – finance director

Please:

(1) Evaluate and interpret the data provided by the data analytics team (Exhibit 2). Explain the relative risks arising from the net operating cash flows for each division and the resulting risks for the company as a whole.

(2) Calculate the settlements in £ of interdivisional currency balances at 30 June 2021 by applying multilateral netting-off procedures to the illustrative data provided (Exhibit 2).

Explain:

- how multilateral netting-off procedures may be of benefit to Tallam
- the extent to which multilateral netting-off procedures may have been facilitated by introducing a centralised treasury department.

(3) In respect of the concerns raised by the internal audit department (Exhibit 3), prepare a report for the audit committee which sets out and explains:

- appropriate procedures for Tallam to manage credit risk on foreign sales contracts (Concern 1); and
- the financial reporting and business issues arising from the differences between internal and external pricing arrangements (Concern 2).

(4) Identify and explain the ethical issues for the Tallam board and members of the treasury department arising from the matters described in the anonymous letter (Exhibit 4).

Evaluate, with supporting calculations, the claims made in the anonymous letter regarding the forward contract. Set out any ethical and business implications.

Explain the actions that should be taken by the Tallam board in response to the receipt of the anonymous letter and the ethical issues identified.