

**APPLICATION FOR MEMBERSHIP TO ICAEW  
EXAMINATION OF PROFESSIONAL EXPERIENCE**

**STEVE SMITH: Candidate number 100000**

**PART 1: DEMONSTRATION OF PROFESSIONAL SKILLS**

**1.1 Using your recent work experience, describe how you identified two different business or professional issues**

**Identification of potentially incorrect tax treatment of a transaction**

**February 2013**

AAA in one year made profits in excess of £1.2m. Following a restructuring of the company's three associated entities, the three companies now formed a group. One of the directors requested a meeting to discuss the future strategy for the newly formed group.

Prior to the meeting, in order to ensure that I was prepared and up to speed on the company's affairs, I requested the books and records of the company.

In the course of this preparatory reading, I studied the file notes on the share ownership of AAA Ltd and noted that it was a close company. Looking at another file note I discovered that the company had recently transferred £1m into an off shore employee trust.

At the meeting with the director, I discussed this matter. I asked the director for the background and reason for this transaction. The director advised me that the financial advisers that the company employed to advise on the restructuring had suggested the transaction.

I asked the director how the transaction had been dealt with from a taxation point of view. From his explanation and the details of the transaction that I had read about in the file notes, I was not convinced that the transaction had been dealt with correctly. I expressed my concerns with the transaction, as I knew from my experience of similar issues, that there were legal restrictions regarding beneficiaries of such trusts, which excluded participators.

The director told me that a firm of accountants would be instructed to deal with this issue. I requested details of this other firm of accountants.

At this stage, I gave no advice, but from my meeting with the director and my understanding of the way in which the transaction had been dealt with from a taxation

point of view, it seemed to me that the director did not have a full understanding of the transaction, or its tax implications.

I suggested to the director that we should obtain expert advice on what was a very specialist issues, so that more detailed analysis on the matter could be performed and a recommendation made as how to proceed.

**1.2 Using your recent work experience, describe how you identified two different business or professional issues**

**Identification of apparently poor cost management and budgeting**

**February 2011**

A medium sized subsidiary of BBB was experiencing difficulties paying its bills as they fell due. One of the directors asked to meet me so that we could discuss the matter.

In order to prepare for the meeting, I did an initial high-level review of the company's affairs.

Prior to that meeting I did the following:.

I reviewed the company's quarterly management accounts. These accounts comprised summary income statements compared to forecast figures. The desk check of the management accounts enabled me to quickly ascertain which of the company's business divisions were under-performing compared to budget.

I performed a few simple calculations from the management accounts. These calculations enabled me to create some simple estimates of key balance sheet figures. These high-level calculations allowed me to highlight potential issues.

My file review also enabled me to review the company's balance sheet reserve structure. Although these showed that it had positive net assets, it seemed from simple cross-referencing to prior year accounts that this was only as a result of revaluation reserves.

My desk research of the company's file also enabled me to consider its cash flow. None of the last 12 months showed a net negative cash flow. However, it was clear from reading the company's file that certain months included large outgoings (primarily salaries) which were funded solely by single seemingly one-off in nature receipts such as prepayments and intra-group payments that were meant to cover more than 12 months' outgoings.

From my desk research it seemed that the company's finances were in a precarious state, and that it seemed likely that it would face an imminent cash flow crisis. Whilst it was clear that more detailed analysis would be required it seemed likely that the problems were due to poor cost management and budgeting.

**2.1 Using your recent work experience, describe how you have used technical expertise and/or business knowledge to analyse a business or professional situation.**

**Using the business risk approach to identify the areas of higher audit risk for BBB and develop the audit plan**

**April 2012**

Assessing audit risk

In addressing audit risk, YYY Firm uses a business risk approach. In employing this, we consider whether the company's systems of internal control and management reporting provide a sufficient level of assurance in order for us to rely, for statutory audit purposes, on the information produced. From a review of the financial statements, we also assess which of the components (either account balances or classes of transactions) might give rise to a material error.

From this process, we identified the following areas of higher audit risk (inherent and/or control):

- turnover
- gross profit
- stock losses
- cash takings at branches.

Audit planning

Developing the audit plan was one of my principal responsibilities and I was required to prepare the first draft for review by the Senior Manager. I organised, and carried out some of, the following work:

- meeting with management and senior client staff, at head office and the subsidiaries, to document and understand the systems of internal control
- carrying out walk through tests of those systems in order to confirm the accuracy of our information
- discussing with management the information that is provided for them and the reasons why they consider it appropriate for managing the business
- documenting and understanding how such information is produced
- making a preliminary assessment of the internal control and management information systems in order to determine whether it would be possible to rely on them for audit purposes.

Having determined the volumes of the major categories of transactions, I recommended a plan of work (interim visit, physical stockcounts, final visit and group consolidation) to support the preparation of the audit opinion on the group, and individual company, statutory accounts.

## **2.2 Using your recent work experience, demonstrate how you used numerical techniques to analyse a business situation**

**Using historical data relating to income, expenditure and staff requirements to develop an annual budget for AAA Group.**

**July 2013**

### Chargeable hours

My starting point for the budget-setting process was the target chargeable hours for the group. Standard hours per person were 1,625 per annum before deducting non-chargeable time (administration, management, recruitment etc), sick leave, study leave, CPE etc. Using historical data, I had estimates of chargeable time for each grade of staff from which to budget overtime. I set a maximum limit of 2,000 hours for any staff grade, although in practice some individual members of staff exceeded this. However, in my judgement, this was not a sustainable level of work.

### Income – recurring and special

I analysed the historical data by constructing a model that used historical recovery rates for audit work and anticipated premiums for special work. By doing so, I was able to translate the chargeable hours into budgeted fee income for recurring audit work and non-audit work (“special work”).

### Staffing requirements

Operationally, the staff budget was of critical importance. Recruitment was carried out nationally and had a long lead-time. Accordingly, I had to ensure that the staff budget reflected accurately the group’s likely requirements; too conservative and there would be excess staff costs and higher levels of “available time” (i.e. time that was not allocated to chargeable or non-chargeable work). During the coming year, my monitoring of the level of available time would be a key performance indicator. Conversely, if I did not organise for the recruitment of enough staff, overtime would become excessive (with the risk of staff burnout and the potential for reductions in work quality) and AAA Group would have to turn down new work.

I prepared the staff budget by using known data for forthcoming leavers and joiners and historical trends in newly qualified, recruitment and leaving rates. I discussed these trends with National Office and adjusted them for any factors affecting the UK recruitment market generally and YYY Firm specifically (e.g. joining salaries).

### **3.1 Using your recent work experience, describe how you have used professional judgement in choosing between options**

#### **Developing a system for costing special projects at XXX.**

**November 2014**

The company had a range of standard products (manufactured for stock) and also carried out specialised project work. This work was the manufacture of systems (comprising standard and non-standard components) and could include the installation of the systems at the clients' premises. At this time, there was very little information regarding the costs of producing these systems and, therefore, whether the company was making a profit or loss on them. I concluded that what was required was a time and materials recording system, the time system being similar to that used at YYY Firm.

I considered three options for the time recording system:

- Daily charge out rates:
- Hourly charge out rates; and
- ½ hourly charge out rates.

At YYY Firm we had recorded our time in half-hour units but I considered this to be too sophisticated for XXX Ltd's purposes. At YYY Firm I had been in charge of ensuring appropriate and sufficient use of the timesheet system to ensure that we were able to create meaningful management data. I would then produce resource reports showing a cost benefit analysis of greater precision in the keeping of records on the one hand versus time spent on record-keeping and staff resistance, on the other. I considered these criteria in relation to XXX. I took account of the different work output and billing structure. This involved having discussions with the Engineering Director, to review the work of the project and production engineers and determine what an appropriate level of detail might be. This needed to balance the requirement for sufficient costing details with the additional administrative work but to take into account the nature of the work and typical time periods spent on projects

After considering each of the three options, and based on the way that way that the firm operated I recommended a system of hourly charge out rates.

### **3.2 Using your recent work experience, demonstrate how you have used professional judgement to prioritise issues**

#### **Designing and implementing improvements to the stock control system for raw materials and finished goods at XXX Ltd.**

**April 2014**

Another area of concern that arose soon after I joined XXX Ltd was the lack of adequate stock records for raw materials and finished standard products. In the past the company had held large quantities of stock but these had been reduced to improve the investment in working capital. However, as a result there were an increasing number of stock-outs that were causing production difficulties.

Although there was a stock requisition system in place, I considered that the processing of the data into the computer systems was too slow and the accuracy of the data held on it was not monitored. The issues were as follows:

- Lack of any staff responsibility for the recording of stock movements.
- Ad hoc processing of stock movements data.
- No sample checks on physical quantities or comparisons with stock records.
- No analysis of the reasons for stock outs.

Because of a staffing resource constraint, it was not practical to address all of these issues at the same time. In order to prioritise the issues, I considered their impact on creating stock-outs. From my work it became clear that it was vital that the company had a good understanding of the reasons for the stock-outs. This issue was therefore dealt with first so that lessons could be learnt from each stock-out.

As a second priority I concluded that sample checks were necessary so that proactive stock management was facilitated.

The final two issues were then dealt with after the two high priority issues had been concluded.

**4.1 Using your recent work experience, describe two situations where you have used your technical knowledge and/or practical experience to develop advice**

**Improving financial performance at XXX Ltd.**

**January 2015**

Costing of special projects

From my work with the Engineering Director and Managers, I considered what would be an appropriate unit for time recording for the two different types of engineers that the company employed. I compared their work with that done by the partners and managers at YYY Firm. The principal difference was that the engineers tended to work on only one or two projects at a time, unlike the partners and managers who were responsible for a substantial portfolio of clients. Accordingly, I implemented a system using a minimum unit of half a day for project engineers and one day for production engineers.

As a result of much better costing information, XXX Ltd was able to negotiate higher prices for its special projects, which were not particularly price sensitive, and improve the overall gross profit margin by nearly 10%.

Reducing the credit given to customers

As part of my review of XXX Ltd's working capital management, I identified that we needed to reduce the credit given to customers. Using my understanding of the working capital cycle and how credit had been negotiated with clients of YYY Firm, I recommended the existing policy should be changed so that:

- new customers were required to pay on delivery of goods
- known customers were allowed up to 30 days credit, if they negotiated for it
- only high volume, long established customers were given up to 60 days, and negotiations were started to reduce this if possible.

I also recommended that the relationships with customers should be carefully monitored to ensure that there was no loss of business. We also found that most customers were prepared to accept the new credit terms. The key was the high quality of the products and meeting agreed delivery dates.

The reduction in credit given contributed to a significant improvement in the use of working capital, with a consequential reduction in the average level of overdraft financing by some 30%.

**4.2 Using your recent work experience, describe two situations where you have used your technical knowledge and/or practical experience to develop advice**

**Producing a budget for AAA Group that was demanding but achievable.**

**January 2013**

I reviewed the chargeable hours and fee income budgets for AAA Group for reasonableness in the light of existing audit work that the group had, known special work in the pipeline, and outstanding proposals for audit and non-audit work. From this I identified the “work gap” that would need to be filled by finding new work. I applied judgment, based on past experience, as to whether this was likely to be achieved. I initiated the use of key performance indicators by monitoring the Group’s progress against target chargeable hours (volume of work carried out) and income (level of recoveries).

The translation of the income budget into staffing requirements needed considerable skill and experience. I worked closely with the staff administrators and the staff partner to achieve this and I used a computer model to flex our assumptions for numbers, and timing, of recruitment, promotions, leavers and sick leave.

Finally, the chargeable hours and staffing budgets were reviewed against historical performance and the practical constraints facing the AAA Group and the YYY Firm:

- the demand for qualified accountants in the UK market place, which would impact on leaving rates
- the level of flotations on the Stock Exchange in London, and takeovers in the corporate sector generally, which would impact on the level of due diligence work
- the number, and seniority, of staff available to advise clients on the transition towards the adoption of IAS
- the impact of work on clients requiring reports on controls over financial reporting (eg Sarbanes-Oxley Act) and their consequential lack of availability for other projects.

On completion of the above work, I was able to recommend a budget based on the model that I had developed. The model incorporated all of the factors described above.

Based on my model, a budget was recommended that was demanding but achievable. The model that I developed was used not just for one year but from that point on by the group.

**5. Using your recent work experience, demonstrate how you dealt with an ethical issue**

**Dealing with issue of potential bribes paid to secure contracts**

**June 2015**

In 2015, when I was working as the Commercial Director at XXX Ltd, I overheard a conversation at a work summer party between the Commercial Manager and a member of the team discussing making facilitation payments to an overseas company to secure work. I had only been with XXX Ltd for a few months when this situation arose. The Commercial Manager was responsible for responding to Invitations to Tender (ITTs) and reported directly to me.

I knew that the matter would be particularly difficult to investigate as I had a difficult relationship with the Commercial Manager. During a meeting in which I was setting her work objectives, she had refused to agree to some objectives because she considered them to be too difficult to achieve.

I discussed the matter of facilitation payments being made to secure contracts, with our in house lawyer, who confirmed that such payments would be inappropriate and probably be illegal, irrespective of the country in which the work was being performed by XXX Ltd. In addition, I ascertained that XXX Ltd had a strict rule that any such payments were against the firm's code of conduct and operational policies.

Having clarified the position with regards to payments to secure contracts, I had no option but to formally discuss the matter with the Commercial Manager. This was an incredibly awkward conversation as I had only become aware of the matter when I overheard a conversation at the company's summer party.

Initially, the Commercial Manager denied that she had discussed the matter and was quite hostile. I acknowledged that it was an awkward situation and that I understood her being upset that I was referring to a conversation that I was not a party to but had overheard. I explained that in my role as Commercial Director, I was ultimately responsible for the conduct of all the people that worked for me, and in particular contracts that had been awarded to us as a result of competitive tenders. I also explained that I had received legal advice that any such practices might be illegal. I explained that I would prefer the Commercial Manager to co-operate in the matter, but that if she did not I would continue my investigations regardless. The Commercial Manager denied that she had been involved in making facilitation payments.

I was not happy with the Commercial Manager's response on the matter and decided to review all of the contracts that she had won on behalf of the company in the last 12 months. My investigations revealed that three of the six contracts included clauses that seemed to imply that 0.5% of the contract value would be payable to a third party organisation upon the contract being signed. Further investigations suggested that the 0.5% fee had been made to the person who had awarded the contracts to our company.

When I discussed the contracts with the Commercial Manager, she confessed that facilitation payments had indeed been made. She tendered her resignation and I handed over the matter to our company's lawyer who then handled the matter to its conclusion.

**Skills demonstrated**

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|--------------------------------|---|
| <u>Integrity:</u>              | Being honest about the situation and concerns relating to facilitation payments and not being associated with misleading business practices |
| <u>Professional behaviour:</u> | Dealing with the potential bribes in a professional and appropriate manner, taking into account company policies and laws and regulations   |
| <u>Objectivity:</u>            | Not being influenced by the interests of the Commercial Manager   |

## PART 2: SUMMARY OF EMPLOYMENT

Steve Smith – candidate number 1000000

Date  (12 month sections)	Description of role	What you did during this period  (projects / tasks / assignments)	Question that refers to this experience
<b>01 Jan 2011 to 31 Dec 2011</b>	<b>Assistant Manager, Audit of BBB</b>	<ul style="list-style-type: none"> <li>• Making an initial assessment on whether the company's systems of internal control and management reporting systems provided a sufficient level of assurance in order for us to rely, for statutory audit purposes, on the information produced</li> <li>• Developing the audit plan</li> <li>• Preparing a staffing and financial budget</li> </ul>	1.2
<b>01 Jan 2012 to 31 Dec 2012</b>	<b>Assistant Manager, Audit of BBB</b>	<ul style="list-style-type: none"> <li>• Supervising the audit work carried out by three teams</li> <li>• Preparing a draft of the Memorandum on Examination that set out the principal matters arising from the audit as a whole and how they were resolved</li> <li>• Carrying out a detailed review of the client's draft statutory accounts to ensure that they complied with the Companies Acts and Statements of Standard Accounting Practice.</li> </ul>	2.1
<b>01 Jan 2013 to 31 Dec 2013</b>	<b>Staff Manager, AAA Group, YYY Firm, London</b>	<ul style="list-style-type: none"> <li>• Setting target chargeable hours, including budgeted overtime, for each grade of staff in the group</li> <li>• Developing a fee income budget for recurring audit work and non-audit work ("special work")</li> <li>• Including the allocated expenditure items set centrally for London office and YYY FIRM nationally</li> <li>• Developing a staffing requirements budget from the income budget</li> <li>• Analysing actual monthly management information</li> <li>• Disseminating monthly management information to the appropriate staff who had specific managerial responsibilities</li> <li>• Contributing to monthly management meetings where we would consider the reasons for variances from budget.</li> </ul>	1.1  2.2  4.2

<b>01 Jan 2014 to 31 Dec 2014</b>	<b>Commercial Director, XXX Limited, London</b>	<ul style="list-style-type: none"> <li>• Overall management of the company's financial processing and reporting systems</li> <li>• Preparation of the monthly management report and accounts</li> <li>• Supervision of the company's data processing systems</li> </ul>	<p>3.1</p> <p>3.2</p>
<b>01 Jan 2015 to 31 Dec 2015</b>	<b>Commercial Director, XXX Limited, London</b>	<ul style="list-style-type: none"> <li>• Preparation of the annual budget</li> <li>• Managing the company's day to day working capital</li> <li>• One-off projects regarding financing, investment, costing and profit measurement.</li> </ul>	<p>4.1</p> <p>5</p>