



**TPE 2023 – Mock 1**

**Theme Park – Case Study Part 2**

©ICAS 2023



**This mock exam is taking place remotely.**

**ICAS would remind you to continue to be ethical and observe the exam conditions applicable to the TPE exam.**

## CASE STUDY

It is now Tuesday afternoon and you are feeling content, having sent the briefing paper to Lee and taken your dog – Marshmallow – for a walk during lunch. You finish up your break and begin to catch up on the mountain of emails that seem to have accumulated since first thing this morning. You find one from the group financial controller, Ian (Appendix 1). You start to read it and are halfway through and becoming rather concerned when the bottom right hand corner of your laptop screen begins to flash. It's an instant message from Katherine asking you to pop into her office. You make a mental note to revisit the email later this afternoon and head to Katherine's office.

"Hello, Eric. I've received some exciting news. A significant opportunity has arisen to bid for the North Yorkshire Train Operating Company Limited ('NYTOC'), which will be awarded a seven-year franchise by the Department for Transport to operate the Whitby to York railway line, a 47-mile stretch of track. I am a railway enthusiast as you might know!

"Lee and I are considering a cash bid for the entire share capital of NYTOC. We will likely need some external funding and potential investors have requested an earnings valuation for comparability purposes. I, therefore, need you to provide an earnings-based valuation for the company, explaining any assumptions you make. I would also like you to advise on the key commercial issues I need to be aware of when running this venture. I expect there are a number of points to consider. I will send you my estimate of the likely earnings for you to consider and update as necessary (Appendix 2). I will also provide the franchise specification I received from the Department for Transport which includes key information about NYTOC (Appendix 2)".

"How interesting," you say. "It's quite a change in direction." Katherine replies, "It is, however, nothing stays the same forever. Please prepare a report for my brother and me which covers the following areas in relation to NYTOC:

- an earnings-based valuation of NYTOC; and
- advice on the key commercial points which arise if we were to run the rail franchise."

"I will get to work on this right away. Have you considered financing?" you say.

"Please discuss this with Lee as he is dealing with this aspect," responds Katherine.

You head back to your desk and no sooner have you sat down than the desk phone rings and, as you suspected, it's Lee.

"Eric?" he says. "It's Lee, again. Thanks for the briefing paper. Katherine has told me she has asked you to prepare a report about the opportunity to bid for NYTOC. We need to raise finance to make a bid and have received an approach from Scarborough Entertainments Limited ('Scarborough').

They have put forward a proposal to either:

- acquire the entire trade and assets of Goody's theme park; or
- acquire 49% of the shares of Goody Attractions Limited (Appendix 3).

"Goody Attractions Limited, as you know, is wholly owned by my father. He has agreed to gift the cash proceeds that arise from any sale to Scarborough – after tax of course – equally to Katherine and I, to help us fund the purchase of NYTOC. Therefore, I need your advice as to which offer is preferable from a tax point of view. I also need you to consider how we could deal with any funding shortfall which might arise based on the preferred route. Please can you also briefly set out the practical implications on the remaining group if we decide to go through with one of the offers from Scarborough?"

"I have a lot to do," you say. "I will focus on the key points only."

Lee replies, "That's excellent, I need something which is straightforward to understand. Please include your tax and funding advice as a section in the report Katherine has requested and provide us with an overall conclusion on whether or not we should bid for NYTOC. I need the report available by close of business this afternoon."

You go back to reading the email from Ian and recall, from your induction course, details of the whistleblowing hotline available to all employees and make a note to yourself to consider this further during this afternoon.

"I'd better get started," you say to yourself before opening up your laptop to begin.

### Required:

- prepare the report as requested by Katherine and Lee; and
- prepare an email to the whistleblowing hotline setting out ethical matters arising.

## APPENDIX 1

### Email from Ian

From: lan@goodyattractions.co.uk  
 To: Eric@goodyattractions.co.uk  
 Subject: Hello  
 Date: Today 12:44 PM

Eric,

I hope you are well. I am sorry I haven't met you in person yet but, as you know, I am currently on sick leave. I wanted to give you a heads up on a few things which have happened at Goody's in recent times that you should be aware of – so that you don't fall into the same trap I did.

I put my stress down to Lee, for the most part. He would often bring sizeable sums of cash into the park and distribute them around the various pay stations at some of the larger rides, usually later in the day or near to closing time.

The amounts were included in the ride takings for that day and the cash banked in the name of Goody's. I recorded the additional cash as sales in the accounts of Goody's. It started a couple of years ago and I would admit I turned a blind eye. However, the sums were initially quite small – maybe £1,000 a week in total.

In recent months the amounts became much larger – £10,000 or £15,000 a week. When I challenged Lee as to why he wanted additional sales recorded in Goody's accounts he got very defensive and said that I should mind my own business and do the job he was paying me for or he would sack me. His manner was quite intimidating and so I just did what he asked.

Then there is Katherine. One of her bright ideas was to do an online survey for customers who stayed at the Clifftop. The survey asked for quite a lot of sensitive information: name; age; address; household income of the customer; and comments on their stay. Customers completing the survey were entered into a monthly competition to win a weekend stay at the Clifftop.

Katherine asked me to download all details for the completed surveys and she emailed them to her former employer at the bank – copying me on the email!

I know that I should have reported all of this in detail to the whistleblowing hotline as it is administered by an independent firm of lawyers but I didn't. The email address for the hotline is [whistleblowing@goodyattractions.co.uk](mailto:whistleblowing@goodyattractions.co.uk).

I'm glad I have finally got this off my chest – the worry of keeping it all to myself has been too much at times. You know what they say: "a trouble shared is a trouble halved"!

With thanks

Ian

## APPENDIX 2

### Projected earnings before interest and tax, prepared by Katherine

	Note	Yr52 £'000	Yr53 £'000	Yr54 £'000	Yr55 £'000	Yr56 £'000	Yr57 £'000	Yr58 £'000
<b>Turnover</b>								
Passenger ticket income	1, 2	49,000	50,470	51,984	53,544	55,150	56,804	58,509
Train catering	3	490	505	520	535	552	568	585
Train wi-fi		15	15	15	15	15	15	15
		<u>49,505</u>	<u>50,990</u>	<u>52,519</u>	<u>54,094</u>	<u>55,717</u>	<u>57,387</u>	<u>59,109</u>
<b>Other operating income</b>								
Government subsidy	4	7,100	7,100	7,100	7,100	7,100	7,100	7,100
Property sub-letting	5	90	90	90	90	90	90	90
		<u>7,190</u>	<u>7,190</u>	<u>7,190</u>	<u>7,190</u>	<u>7,190</u>	<u>7,190</u>	<u>7,190</u>
<b>Expenses</b>								
Staff costs	1	12,500	12,875	13,261	13,659	14,069	14,491	14,926
Depreciation of rail infrastructure	6	18,200	18,200	18,200	18,200	18,200	18,200	18,200
Depreciation of rolling stock	6	11,550	11,550	11,550	11,550	11,550	11,550	11,550
Finance costs on leases		3,605	3,119	2,624	2,120	1,605	1,081	546
Fuel	1	6,000	6,180	6,365	6,556	6,753	6,956	7,164
Raw materials and consumables	1	250	258	265	273	281	290	299
		<u>52,105</u>	<u>52,182</u>	<u>52,265</u>	<u>52,358</u>	<u>52,458</u>	<u>52,568</u>	<u>52,685</u>
<b>Earnings before tax</b>		<u>4,590</u>	<u>5,998</u>	<u>7,444</u>	<u>8,926</u>	<u>10,449</u>	<u>12,009</u>	<u>13,614</u>

#### Notes:

1. Passenger ticket income, staff costs, fuel and raw materials and consumables have been increased in line with inflation (3%).
2. Yr 52 figures are based on pre-pandemic passenger numbers.
3. Train catering has been calculated as 1% of passenger ticket income.
4. Inflation is not permitted on the government subsidy.
5. It is assumed that all available units will be sub-let.
6. The fair value of the right-of-use rail infrastructure is £127.40m and the sterling equivalent fair value of the right-of-use rolling stock is £80.85m. The lease term on all assets is seven years although the useful lives of the assets are significantly greater.

## Extract from Franchise Specification

### *Background*

NYTOC is a newly-incorporated entity and will hold the right to operate the Whitby to York railway line for a period of seven years commencing on 1 January Yr52 ('the franchise period'). The line follows a scenic route and is steeply graded in both directions in order to navigate through the North Yorkshire moors.

The entire issued ordinary share capital of £1.00 of NYTOC is available to purchase by prospective bidders as part of the franchise payment and the bid deemed to be most attractive by the Department for Transport ('DfT') will secure ownership of NYTOC for the successful bidder ('the franchisee'). During the franchise period, NYTOC cannot be sold to another party. At the end of the franchise period, the franchise will be transferred to a new entity and NYTOC will be liquidated. The franchise will hold a negligible amount of owned assets throughout the franchise period – rail infrastructure and rolling stock will, instead, be leased.

The Whitby to York railway line will operate four British Rail Class 158 'Express Sprinter' trains, each with three carriages and total seats of 142 per train. The trains were built in Yr26 and were refurbished in Yr39. The Whitby to York line has five stations, which will be leased to the franchisee by Network Rail. The track itself is also leased to the franchisee by Network Rail – together with the stations, this represents the 'rail infrastructure'.

A new dual carriageway is currently under construction close to the line and, once opened, in December Yr55, it is expected that there will be a 10% drop in year-on-year passenger ticket income as a result.

Bids are required to be submitted by 1 December Yr51 to the DfT.

### *Key financial information*

A 3% annual rise in train ticket prices, in line with forecast wage and general inflation, will be automatically applied by DfT. Based on current information, passengers spend the equivalent of 1% of ticket spend on catering whilst on board.

A government subsidy of £7.10m per annum (no allowance for inflation permitted) will be paid annually to the successful franchisee.

Within the leased stations, there are nine small retail units of similar size which are sub-let for £10,000 per annum. The franchisee has sole discretion over the use of the units during the franchise period.

The PE ratio for a comparable quoted company is 10.

## Operational matters

Existing train crew, comprising train drivers, train guards and on-board catering staff, will transfer to the franchisee from the previous franchisee on 1 January Yr52. Executive management of the previous franchisee will not transfer to the successful franchisee.

The rolling stock (i.e., trains) will be leased to the franchisee from The Rolling Stock Company (Netherlands) Limited for €15.00m per annum (fixed price) over the franchise period. The franchisee will be required to procure third-party maintenance services for the trains over the franchise period and, as a rule of thumb, annual maintenance costs are £1.00m per year rising annually by inflation.

## Key performance indicator

Punctual train arrival is critical to the success of the line. Punctuality is assessed as the percentage of trains that arrive at their destination within five minutes of their scheduled arrival time for rural routes, having called at all scheduled stations. Set out below are the results for actual performance level Yr50, the expected performance levels for Yr51 and the required performance levels for Yr52 onwards:

	<b>Yr50</b>	<b>Yr51</b>	<b>Yr52</b>	<b>Yr53</b>	<b>Yr54</b>	<b>Yr55+</b>
	<b>Actual</b>	<b>Expected</b>	<b>Required</b>	<b>Required</b>	<b>Required</b>	<b>Required</b>
	<b>%</b>	<b>%</b>	<b>%</b>	<b>%</b>	<b>%</b>	<b>%</b>
Punctuality	79.3	80.1	83.5	84.2	87.2	90.6

Failure to deliver against the required punctuality by the franchisee will result in a claw-back of 25% of the annual government subsidy.



## APPENDIX 3

### *Extract of offer from Scarborough Entertainments Limited*

This sale and purchase agreement, dated 1 November Yr51 is between Scarborough Entertainments Limited ('purchaser') and Fred Goody ('seller'). The seller intends to sell and the purchaser to purchase either the entire trade and assets or 49% of the issued ordinary shares of Goody Attractions Limited ('the company') for the purchase price. The purchase price for the trade and assets will be £35,000,000 and the purchase price for the shares will be £20,000,000.

The trade and assets will comprise the title to all existing park rides and associated infrastructure. All existing supplier contracts will be transferred to the purchaser. For the avoidance of doubt, the title to the area of land on which the park is situated will not transfer to the purchaser and will remain the property of Fred Goody. An annual rental charge will be levied by Fred Goody for use of the land.

Should the offer be accepted by the seller for 49% of the issued ordinary shares, the company will then operate in the future with 49% of the shares held by Scarborough and 51% by Fred Goody. Each party will have three board members and Scarborough will appoint the chairman of the board, who will have the casting vote on any day to day operational decisions.

### *Notes by Lee Goody*

My accountant tells me that £23,500,000 will be taxable as a result of the sale of the trade and assets. I expect that after taking into account the relevant corporation tax the post-tax amount received by the company can be paid out by our father to Katherine and me for the rail franchise bid.

The selling costs of a share sale will be 3% and the original cost of the shares being sold was £2,500. The offer for the shares is interesting as I believe we will still control the business as we have the majority of shares, and my father is reluctant to relinquish his involvement entirely in the park. Under either scenario, we will receive annual rental income on the land which is a bonus. I expect Scarborough to be a silent partner and that I will still run the business.

**END OF PAPER**