Please make sure you a copy of the pre-seen information and present value tables and formulae, which are provided to you on exam day.

Papy – Unseen material provided

ANSWER THE FOLLOWING QUESTION

You are the Management Accountant of Papy.

Arif Karp, the Corporate Affairs Director of Papy has asked you to provide advice and recommendations on the issues facing Papy.

Question 1 part (a)

Prepare a report that prioritises, analyses and evaluates the issues facing Papy and makes appropriate recommendations.

(Total marks for Question 1 part (a) = 90 Marks)

Question 1 part (b)

As an Appendix to your report (in either your Word or Excel files if PC based) prepare a summary for use in a presentation to Arif Karp, in bullet point format, for your findings and financial implications of introducing the Papy "Fair Trade" 100% sustainable carrier bag as the alternative to free disposable plastic bags. Your presentation slides should also include your recommendations.

This Appendix should contain no more than 10 bullet points.

(Total marks for Question 1 part (b) = 10 Marks)

Note: Marks for calculations, relevant to Question 1 part (b), are awarded within the Assessment Criterion of Application included in Question 1 part (a)

The new Chief Executive of Papy, Lucas Meyer, has announced that he intends for the Papy chain of supermarkets to change the way in which it operates, in order to become a more sustainable business.

Within a recent press report 24 June 2011, appendix 5, page 14 of the pre-seen information, Lucas Meyer stated "We, at Papy, are going to make changes in the way that we operate that will affect our supply chain and our customers. However, we feel that the changes we will make in the coming months, and years, are the right way to operate a business in the long-term. We are confident that our loyal customers will see that what we plan to do will help Papy to trade in a much more sustainable way. We aim to reduce carbon emissions and make changes in order to become a business that can maintain its long-term presence in this industry".

Until recently, Papy's Board has set targets for reductions in carbon emissions in an unstructured way, there has been no overall strategy developed in order to achieve the reductions. Whilst there has been a range of initiatives, which include more efficient logistics for deliveries to stores, reduced packaging and the increased use of rail transportation rather than road, there has not been an integrated approach on a large scale to tackle and reduce Papy's carbon emissions.

Arif Karp, Corporate Affairs Director, has been working closely with the new Chief Executive, Lucas Meyer; Arif Karp considers that Papy needs to set targets for the coming years and to plan how reductions in carbon emissions can be achieved. The new Chief Executive, Lucas Meyer has also met with RCB : private equity fund, which owns 40% of the equity share capital of Papy. There are 100 million shares in issue, a list of shareholders of Papy is provided below.

Shareholders	**% of share capital**
Papy employees	4%
Papy directors	4%
Papy (founding family)	5%
Pension funds (seek long-term security for pensioners)	15%
RCB : private equity fund (seeks short-term profits)	40%
HSOB bank (Papy is a client)	10%
Private investors (many and varied)	22%
Total	100%

RCB: private equity fund has major concerns regarding the impact on operating profit and earnings per share (EPS) for any new CSR initiatives planned. The earnings per share (EPS) for the year ended 31 December 2010 was €4.544 (year to 31 December 2009 EPS was €4.219). This is an increase of 7.7%.

The latest full year operating profit forecast for year ended 31 December 2011 without any new CSR initiatives planned will be €700 million.

Finance income and expenses forecast for the year ended 31 December 2011 would be €150 million, which would include all borrowings necessary to fund the range of initiatives that Arif Karp is planning for Papy. The new CSR initiatives will be funded partly by retained earnings and also by borrowing €300 million from HSOB bank. HSOB bank has already in principle agreed the loan. The effective tax rate is 25%.

The extract from Papy's Statement of Comprehensive Income, Statement of Financial Position and Statement of Changes in Equity for years ended 31 December 2009 and 31 December 2010 can also be found in appendix 3 of the pre-seen information, page 12.

The new Chief Executive of Papy, Lucas Meyer is planning a shareholders presentation to announce the new green strategies of Papy and how it intends to become a more sustainable retailer. Within the next month Arif Karp will be publically presenting to the media and to Papy shareholders at this meeting , the major changes that Papy stores will be implementing and how all new 'green initiatives' planned for will reduce carbon footprint from retail operations. The forecast for year ended 31 December 2011 for Papy's total carbon emissions is currently 1400 million Kg. This forecast is without taking into account any new initiatives planned within this un-seen information. Lucas Meyer wants to see at least a 400 million Kg of carbon emissions reduction from this current forecast of 1400 million Kg of carbon emissions.

Free disposable plastic bags discontinued within stores

The availability of free disposable plastic bags at checkouts is being discouraged within Papy stores and customers in some countries have been offered free re-usable shopping bags. Papy has reduced the weight and the type of plastic used in the manufacture of its carrier bags and is actively encouraging customers to re-use bags, including a credit to customers' loyalty cards for re-using carrier bags.

Papy currently has targets for Carbon emissions (GHGs) (shown as kilograms (kg) per average square metre of sales area) and Free disposable plastic bags (shown as million per average square metre of sales area) within its current Sustainability Indicators, the period 2008 to 2010 is contained within appendix 6 of the pre-seen information, page 15. In 2010, Papy stores purchased from suppliers 750 million plastic bags, the operating cost of providing free disposable plastic bags within Papy stores for the year ended 2010 was €10 million. These levels are planned to remain the same for 2011 without this new initiative.

As from next month free disposable plastic bags will be discontinued in all Papy stores. Customers at Papy stores must now either bring their own bags or alternatively will be offered a Papy 100% sustainable carrier bag made of cotton, bearing the branding of Papy stores, and an internationally recognised fair trade symbol. The carbon footprint from fair trade sustainable shopping bags equates to generating only 0.07kg of carbon emissions per bag. Using free disposable plastic bags currently supplied in a Papy store equates to generating 0.37kg of carbon emissions per bag. Further details concerning the number of free disposable plastic bags sold in Papy stores can be found within Appendix 6 of the pre-seen information page 15.

Customers who need shopping bags will now be offered a Papy "Fair Trade" labelled 100% sustainable carrier bag at a price of €3 each. Each Papy 100% sustainable carrier bag can be manufactured and supplied at a cost of €0.25 each, from India.

If customers purchase a Papy 100% sustainable carrier bag they would then be rewarded each time they visit a Papy store in future with a 1% loyalty discount given at the point of sale, the customer would barcode the bag in future when making purchases to obtain a 1% discount at the point of sale. A maximum of 1% sales discount will apply to each customer despite the number of bags or times a customer barcodes it.

Marketing Director – Karen Wagnes, is unsure of the financial effect of this new initiative planned and has asked you to calculate for her the effects of this new scheme, as well as other factors she may also need to consider. Based upon trials undertaken in 4 Papy supermarkets, she has estimated the probability and forecast number of 100% sustainable carrier bags that can be sold annually each year in all Papy stores (see below). Based on barcoding data of sustainable bags used by customers during trials undertaken, it is forecast that 25% of bags purchased will not be reused after purchase by customers. No feedback has been obtained directly from store managers or customers from these trials undertaken. The average spend in a Papy store estimated from a customer based upon these trials undertaken was €800 per year.

Forecast total annual sales for the Papy "Fair Trade" 100% sustainable carrier bag

Probability	**Bags sold (million)**
70%	4
30%	8

New propane technology for fridges and freezers

Fridges and freezers within Papy stores are environmentally unfriendly and in need of modernisation, the Corporate Affairs Director – Arif Karp, stated at a recent board meeting that existing fridges and freezers "spew out bad gases that make up a large proportion of Papy's total carbon emissions and total energy consumption.

Papy currently has targets for Carbon emissions (GHGs) (shown as kilograms (kg) per average square metre of sales area) and energy consumption (shown as kWh per square metre of total sales area) within its current Sustainability Indicators, the period 2008 to 2010 is contained within appendix 6 of the pre-seen information, page 15.

It is Arif Karp's proposal that Papy should be leading the way in its market by using ground breaking HFC (hydro fluorocarbon) free technology. This will help cut carbon emissions from existing fridges and freezers by up to 20 per cent. There will also be a 25% reduction in annual energy consumption (KWh) from new modern fridges and freezers, generating €35 million annual operating cost savings in energy consumption from all shops and reducing annual energy consumption by 100 million kWh, in total from all stores. 1 kWh of energy consumption equates to 0.8kg of carbon emissions.

Arif Karp is committed to rolling out a modernisation programme, using this latest technology to all Papy stores within the next 12 months. This modernisation will completely remove HFC (hydro fluorocarbon) gases from all fridges and freezers, which can have a high global warming potential if leaked. Existing refrigeration units are now 12 years old and fully depreciated.

Details of new fridges and freezer investment

- 10 year contract
- Total investment outlay €400 million in total for all stores, to be depreciated over 10 years.
- 50% reduction in annual servicing and maintenance costs, saving €20 million in operating cost from all stores in total.
- Each store would have to close for 5 days for installation to be completed.
- Will reduce annual energy consumption by 100 million kWh, in total from all stores.
- 1 kWh of energy consumption equates to 0.8kg of carbon emissions.

Environmental improvements to stores

Arif Karp, Corporate Affairs Director, has prepared proposals to invest in a range of technologies to improve Papy's environmental profile for the construction of its new stores. The business plan for the year ended 31 December 2011 is to open 30 new stores. It is Arif Karp's intention that all new store openings should now include a range of mandatory environmental initiatives, including improved management of waste on-site, IT solutions to reduce electricity usage and improved employee training on environmental issues. Because of these new initiatives the capital expenditure to build new stores will rise by €1.0 million per store.

Arif Karp's proposals also include the installation of solar panels at 40 Papy stores, located in hotter European climates, at a total cost of €20 million. It is forecast that this could save 30% in electricity costs, which would result in an annual operating cost savings of €1.0 million from these 30 stores, in total. The investment in solar panels within these stores identified has been an issue repeatedly delayed in the past due to a lack of funding allocated for it. The proposal has a long payback period and therefore made less commercial sense in the past when evaluated with other proposals.

All initiatives explained above will have the result of reducing carbon emissions in 2011 by 35 million Kgs. Papy depreciates new stores and all capital expenditure over a 10 year period.

TORN Abattoirs

In a survey of Papy's supply chain, over 90% of suppliers considered they are treated with respect by Papy and that a fair price was negotiated. Some of Papy's suppliers have entered into longer-term contracts than in the past, in order to reflect Papy's commitment, loyalty and support to agricultural producers worldwide. Papy also inspects the working conditions at supplier sites to ensure compliance with its policy for suppliers' working conditions.

Across most European countries, Papy operates annual contracts with local meat farmers. The Operations and Logistics Director - Rafael Lucci did not renew in July 2011, an existing contract with SNS Abattoir choosing instead to renew with a new supplier TORN Abattoirs.

Some environmental protesters have recently publicised to the media, secret footage shot inside a TORN Abattoir, which has ignited a public row over abattoir cruelty, following a series of undercover films that have shed new light on the way animals are killed behind closed doors. Film footage showed a slaughter man slitting the throat of sheep and then cutting off their heads while they are still alive.

The Operations and Logistics Director - Rafael Lucci has been involved in an internal investigation following adverse publicity. TORN Abattoirs supplies over 60% of its fresh meat sold to Papy stores within that country. Rafael Lucci is planning to recommend to the Papy Board that Papy cancels immediately its contract with TORN Abattoirs. He is also recommending to the Board that Papy should refuse to accept any responsibility for this adverse publicity caused by these films being leaked by the media.

New IT package for transportation

Papy for the year ended 31 December 2011, is forecast to spend in operating cost €150 million on fuel alone for its delivery Lorries and vans. This roughly equates to 57 million gallons of fuel. Carbon emissions of 12.2kg are recorded within Papy's current performance measures for each gallon of fuel its organisation consumes.

According to the IT Director – Ziad Abbill, better fleet load optimisation can be achieved by investment in a new IT package which will cost €10 million and will be compatible with Papy's existing fleet management system. The new system will use live real time monitoring of vehicles and will optimise loading and unloading to ensure full loads is always the proper action to take. Papy depreciates new software over a 2 year period.

The new software package will enable some fleet vehicles to be removed from the road altogether due to greater efficiency of logistics. Fuel consumption will reduce by 10%. Also a further saving in operating cost of €2 million annually, due to fewer vehicles and 24 staff redundancies.

End of information