



Institute of Certified Management Accountants of Sri Lanka

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May 2023 Examination

Strategic Level

GCE – 404 Corporate Governance, Control Strategy & Ethics

No. of Pages: 08

No. of Questions: 05

Instructions to Candidates:

1. Time Allowed : Reading – **15 minutes**.
Writing - **Three (3) hours**.
2. Total : **100** Marks.
3. This paper consists of two Parts.
Part-I : Question no. 01 (**Compulsory**).
Part- II: Question no. 02 – 05 (**Select any 03 questions**).
4. Answer only four (04) questions including Question No. 01.
5. The answers should be in **English** language.
6. Begin each answer on a separate page in the answer booklet.

PART 1
Compulsory

QUESTION NO. 01

Tesla Manufactures and Exporters PLC (TME) was listed on the Colombo Stock Exchange in 1998. The initial chairman of TME was Mr. Hemaka Amarasena, a Chartered Engineer who graduated from the University of Moratuwa as an Electrical Engineer. He had 51% of the company's shareholding at the time the company was listed on the Colombo Stock Exchange. TEM manufactures wire harness products and exports to the USA and European markets. The company produces two categories of products, one for the international market and the other for the local market, with separate identification barcodes.

Adhering to the principle of "quality first and service first", the company provides its customers with high-quality products and after-sales services. The company also respects talent and pays attention to technology and innovation. The company has obtained ISO9001:2015 management system certification for the entire process and the certification of Sri Lanka Standard Institute for its products.

The factory and the Head Office of TME are situated outside the industrial zone of Horana, where the extent of the factory and office is approximately 6 acres.

The Board comprises currently of Mr. Kesara Amarsena, elder son of Mr. Hemaka Amarasena , holding 15% of his father's shares, his sister Mrs. Githma Fonseka has 15% of shares, Mr. Hemaka Amarasena, with a balance of 21% shares, Mr. Gunasena De Silva one of Mr. Kesara's university friend and another three executive directors along with three independent directors who are having the expert knowledge in finance, wire harness industry, international marketing with higher degrees in respective areas and with a significant number of years of experience in the relevant fields.

The current chairman of the company is Mr. Kesara Amarasena, while Mrs. Githma Fonseka was appointed recently as the Chief Executive Officer of the company by the board. Three independent directors chaired the key committees as follows.

1. Remuneration Committee: Mr. Gavesh Feranado
2. Audit Committee : Mrs. Pubudu de Silva
3. Nomination Committee : Mr. Jagath Herath

Mrs. Pubudu de Silva is a practicing Chartered Accountant and Senior Fellow Member (FCA) of the Institute of Chartered Accountants of Sri Lanka and also a partner of AMBC Associate, a Chartered Accountancy Firm.

The board of directors recently discussed the current economic downturn and future economic risk on the company's operation activities due to the heavy fluctuation of the Dollar against LKR and the IMF involvement. The board agreed to assign AMBC Associate as the company consultant to review the economic situation, identify the possible risks, and recommend the remedial strategies available to mitigate them. The board mentioned that AMBC Associate is the best to carry out this assignment since Mrs. Pubudu De Silva is familiar with the company's operational activities, and can provide the information they require without an issue. Also, they agreed on a fee which is a significant percentage (12%) of the total turnover of AMBC Associate, and said after going through the scope and the depth of the assignment, AMBC Associate will send the acceptance letter and start the preliminary works.

The Risk Management Committee Chair Mr. Panduka De Mel, an executive director of the company and also heading the quality controlling section, submitted a report to the board mentioning the urgent requirement of repairing the wastewater plant. He estimates the cost to be at least USD 100,000 to bring and replace the existing plant since the maintenance has not taken place in the last two decades, and there is a possibility of a severe break - down and non-treated toxified water is going to the water stream and causing substantial environmental pollution.

The board has agreed to consider this requirement as an urgent matter. However, due to the shortage of dollars in commercial banks and the poor liquidity, the company is facing high manufacturing costs as well as high local transportation costs, and high international transportation costs, which resulted in low export orders and low dollar income compared to the previous years. The board agreed to hold the replacement until the company receives adequate foreign currency. They discussed as an alternative, if a break - down of the plant occurs, for a short period let untreated water be released to the stream, as there are no other factories or residents in the surrounding area to protest against untreated wastewater being released to the stream. Mr. Jagath Herath, an expert in manufacturing rubber products, opposed the unethical behaviors of his colleagues on the board.

YOU ARE REQUIRED TO:

1.1. Explain the importance of a corporate governance framework and its features to achieve the corporate goal of TME.

(08 Marks)

1.2. Discuss the important role played by an Independent Director of a public quoted company while referring to the status of the independency of Mrs. Pubudu de Silva as an independent director after accepting the assignment by AMBC Associate.

(08 Marks)

1.3. Discuss the objections placed by an independent director Mr. Jagath Herath regarding the wastewater strategy proposed by the board giving reference to the stakeholder theory and legitimacy theory.

(10 Marks)

1.4. Discuss the meaning of ethics referring to the highlighted incidents mentioned at the discussion of the board of TME.

(07 Marks)

1.5. Examine the professional behavior of Mrs. Pubudu De Silva in accepting the assignment offered by TME.

(07 Marks)

[Total 40 Marks]

QUESTION NO. 02

ABX Power PLC supplies power for the national grid using Coal to generate power. Coal is expected to remain a significant power supply source worldwide, and shifting to Carbon-neutral fuels will be challenging because of growing electricity demand and booming industrialization. At the same time, Coal consumption results in severe air pollution and health concerns. Improvement in emission control technologies is key to improving air quality in coal power plants, and many scientists reported removing air pollutants individually via conventional control methods.

A recent study carried out by the social activist mentioned that ABX poses irreversible grave impacts to the health, safety, and livelihoods of surrounding communities and causes irreparable damage to the environment, both land and sea, a few of which are highlighted in its report. The impact is, however, not limited to its immediate vicinity as the toxic emissions travel to other parts. It mentioned that ABX had not adopted a proper management control system indoors to protect the environment. Also, ABX does not conduct regular management audits to maintain a

proper environmental protection control system. Hence, severe damage has happened, as mentioned above, within the surrounding environment.

The chairman of ABX PLC, Mr. Kamal Kulathunga, appointed you, holding fellow member of the Institute of Certified Management Accountants, Sri Lanka (CMA) and the Management Accountant of ABX PLC, as the head of the team to study the report recently published against the environmental pollution happening due to poor pollution control system.

YOU ARE REQUIRED TO :

2.1. Discuss the important role played by the Management Control System to maintain the Proper pollution preventive system of ABX PLC.

(08 Marks)

2.2. Explain what a Management Audit is and the differences between the Management Control System and Management Audit.

(08 Marks)

2.3. Recommend possible steps to be implemented to rectify the poor Management Control System in the company.

(04 Marks)

[Total 20 Marks]

QUESTION NO 03

CBS Console PLC is a large manufacturing entity where the raw material requirements of all manufacturing plants are to be sourced centrally by the Central Procurement Department (CPD) of the head office at Colombo Central. There is a purchasing office based in each plant to request the necessary raw materials, raising the purchase requisition through the system. CBS has established a procurement policy manual and detailed guidelines for Standard Operating System (SOP) for purchasing, vendor registration, vendor selection, evaluation, etc. A newly appointed General Manager pointed out to review the existing SOP and the company's corporate governance framework to integrate them to maintain a strong internal control system that complies with the corporate governance requirements within the framework.

YOU ARE REQUIRED TO:

3.1. Discuss the salient characteristics of an effective Standard Operating Procedure (SOP) for a sound internal control system of the CBS.

(12 Marks)

3.2. Discuss the suggestion made by the newly appointed General Manager about integrating the corporate governance process with the SOP.

(08 Marks)

[Total 20 Marks]

QUESTION NO. 04

PART-A

ABC Holding PLC is a conglomerate listed on the Colombo Stock Exchange, and ABC has several subsidiaries whose sole ownership is with ABC Holding PLC. The key Shareholder/Chairman of ABC, Mr. Kalum Dissanayaka brought Ms. Shyama De Silva, who is a good friend of Mr. Kalum Dissanayaka as an Independent director. However, Ms. Shyama supports all the actions and decisions of Mr. Dissanayake, and at times those actions and decisions are unethical, yet they improve the company's financial performance. At the recent board meeting, some directors were critical of Ms. Shyama's behaviour, and they highlighted the possible negative impacts on the board's performance due to her conduct.

You are required to:

4.1. Explain the Managerial and Class Hegemony Theory

(04 Marks)

4.2. Evaluate the behaviour of Ms. Shyama De Silva and its impact on Board's performance emphasizing the Hegemony Theory.

(04 Marks)

PART-B

Lever Brothers (Pvt) Limited is a large manufacturing company that produces many consumer products and has an urgent requirement of capital to expand its production. The company's Chairman requested the finance director to evaluate going public and listing the company on the Colombo Stock Exchange. The Finance Director formed a special committee for this purpose and assigned tasks among members to gather information necessary for evaluation purposes. You are one of the team members assigned to evaluate the Audit Committee, one of the main committees mentioned as mandatory committees to be formed by a listed company in the Colombo Stock Market.

YOU ARE REQUIRED TO:

4.3. Discuss the functions, benefits, and setbacks of an audit committee formed by a listed company.

(12 Marks)

[Total 20 Marks]

QUESTION NO. 05

PART-A

The Board of Directors of Excel Holding (Pvt) Limited, which was established in the year 2008 and manufactures coir products for the international market looking to list the company on the Colombo Stock Exchange to raise the required capital for the modernization of the factory and expand the capacity due to the higher demand. Also, Japanese buyer is keen to invest the required capital. The board is keen to know the theoretical aspects of corporate governance and if they decide to list the company as a public company in the Colombo Stock Exchange The company board of directors has assigned you to explain the following for their knowledge to evaluate two alternative sources of funds.

YOU ARE REQUIRED TO:

5.1. Explain briefly key Corporate Governance Theories.

(08 Marks)

5.2. Explain the role and function of the Company Secretary.

(04 Marks)

PART-B

South East Bank PLC is a commercial bank that was established in the year 1985. As an ethical bank, South East Bank always tries to develop a more favorable environment in society. South East Bank considered providing more flexible re-payment schemes for their customers just after the outbreak of Covid -19 in Sri Lanka and also considered waiving a certain percentage of interest for their good customers. The chairman of the bank, Mr. Balapatiya mentioned in a recent interview that the bank is involved with ethical business and always takes decisions from the point of view of its customers. You are the Company Secretary, and your assistant Miss Padmini approached you after the chairman's speech and requested you to briefly explain the following.

YOU ARE REQUIRED TO:

5.3. Explain ethical business and ethical banking.

(04 Marks)

5.4. Discuss the Pros and Cons of ethical banking.

(04 Marks)

[Total 20 Marks]

-End of the Question Paper-