



Institute of Certified Management Accountants of Sri Lanka
Incorporated by Parliament Act No.23 of 2009

November 2021 Examination

Strategic Level **GCE – 404 Corporate Governance, Control Strategy & Ethics**

No. of Pages: 07
No. of Questions: 05

Instructions to Candidates:

1. Time Allowed : Writing - **Three (3) hours**.
Reading & software handling – **30 minutes**.
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.

This examination was conducted online on Pearson VUE platform

PART-I **Compulsory**

QUESTION NO. 01

Agro Import & Export Enterprise PLC (AIEE) was established in 2010 to import agro related products such as fertilizer, pesticides, and any other related products from China, India, USA, Germany, and Lithuania and to export fruits, vegetables, processed foods, spices, and cinnamon products to USA, Europe, and Australia. The current Sri Lankan government policy on the import of chemical fertilizer and pesticides adversely affected AIEE's operations and the company performance drastically dropped incurring significant losses during the financial year 2020/21. The company has opened an L/C (Letter of Credit) with their bank to import organic fertilizer from a supplier in India supporting the government's current policy. The majority of the board members supported this decision while Mr. Kalpana Fernando opposed it due to the lack of support from farmers and other pressure groups on the ban of chemical fertilizer. However, the majority felt that AIEE should be the pioneer in importing organic fertilizer and capture the market. Mr. Kalpana had a different view and he emphasized that still the import regulations have not been amended and that there are different Parliamentary Acts prohibiting import of organic materials which are harmful to our soil and other plants. However, the board decided to place an order without seeking an expert opinion on this matter. The company opened the L/C with their banker to import organic fertilizer from a reputed fertilizer exporter in India.

However, after arrival of the shipment, the opposition to it arose daily from various groups including experts, scientists, farmers, and other interested groups requesting not to allow the harmful organic fertilizer into the country. AIEE had to respond immediately and requested the bank to hold the payment on the L/C until they get a sample from the shipment tested to see whether there are any harmful elements in the fertilizer. Two lab reports mentioned the presence of harmful pathogens in the sample tested by them. The bank advised that they have to follow the UCP600 and if they do not find any discrepancies in the documents that they have to make the payment within five working days. However, the Chairman of AIEE Mr. Henry Silva advised the bank that, though the company has missed to mention such test report in the L/C according to the prevailing law, it is not allowed to bring any organic materials with harmful pathogens, and accordingly they have not complied with the law of the country. The bank rejected the request by the company and advised since there are no discrepancies, the bank will honour the L/C as per UCP600 requirements. The board was not happy about decision of the bank and wanted to change

their bank to another immediately and find a solution to the problem of unloading the fertilizer shipment. One of the senior directors, Mr. Nishan De Costa suggested to offer a valuable gift to officers in the testing organization to obtain a report confirming that there are no harmful pathogens in the sample obtained from the subject shipment and get the cargo immediately to avoid huge loss of money to the company which the company could not afford.

However, Mr. Kalpana Fernando, once again opposed this attempt and wanted to have a negotiation with the exporter in India to come to a reasonable settlement to sort out the issue between two companies amicably. He also pointed out that the company should have principle-based approach to corporate governance and the board of directors should always act ethically in solving issues.

You are required to:

1.1. Explain the principle-based approach to corporate governance and the importance of this approach in implementing a sound governance principle in an organization.

(06 Marks)

1.2. Discuss whether directors of AIEE acted in complying with the legal duty of skill to exercise reasonable care and diligence in importing organic fertilizer.

(08 Marks)

1.3. Explain the importance of having a sound corporate governance framework to prevent occurrence of a strategic risk that has happened at the time of importing organic fertilizer.

(06 Marks)

1.4. Explain the importance of having corporate ethics in an organization.

(05 Marks)

1.5. Discuss the unethical behaviour of the board of directors of AIEE, referring to the ethical theories.

(08 Marks)

1.6. Explain "Do you agree with Mr. Kalpana's suggestions to solve this issue".

(07 Marks)

[Total 40 Marks]

PART II

QUESTION NO. 02

Express Selling (Pvt) Limited (ESL) is a reputed supermarket chain having more than 150 Supermarkets Island wide. They have introduced ESL.Com online ordering system to serve their customers during the lockdown period and even thereafter. The Managing Director, Mr. Sarath Gamage advised their key strategic managers to implement an effective control system to make sure that their customers have willingly adapted to the system and also to ensure that existing customers will not switch to the competitors due to failures of services. However, he advised the General Manager to form a committee to study the existing control system and submit a report to him with lapses and suggestions to improve the system to achieve his target.

The General Manager requested you to provide the following information regarding an effective control system in order to prepare the final report.

You are required to:

2.1. Explain the types of management controls and necessity of having an effective control system in an organization.

(06 Marks)

2.2. Discuss the characteristics of an effective control system of an organization.

(06 Marks)

2.3. Identify the key areas to be controlled in ESL to satisfy its stakeholders.

(08 Marks)

[Total 20 Marks]

Question No 03

Hanson Distributors (Pvt) Limited (HDL) was established in 2005 as an exclusive agent and distributor for a world-famous international brand of mobile phones within Sri Lanka. However, with the growth of the demand for mobile phones, HDL expanded its agency relationship with other brands too. The company has opened more than 200 outlets in all main cities and also appointed authorized dealers in addition to its own outlets. Mr. Jackson Perera, the Managing Director of HDL, discussing at regular management meetings pointed out that, the company does not have any person to monitor whether the existing internal control systems are functioning smoothly. Since there are different brands, and the values of the stocks are high, there are possibilities of stealing and various malpractices by the staff and the people involved in the distribution and selling of those products. Hence, he suggested to have an internal audit department in order to monitor the control system running smoothly and effectively and to prevent any malpractices such as fraud etc. Mr. Perera assigned you to gather information required to evaluate the proposal immediately.

You are required to:

3.1. Explain the need and scope of an Internal Auditor in managing an effective control system in an organization.

(06 Marks)

3.2. Explain different types available to an internal auditor to audit in the areas of the governance process, risk management, and internal control of HDL.

(08 Marks)

3.3. Advise the possible frauds and internal control weaknesses that can occur in a high-value product distributor like HDL.

(06 Marks)

[Total 20 Marks]

QUESTION NO. 04

Assume that you have been appointed as company secretary of ABC PLC which has been recently listed on the Colombo Stock Exchange as a public company. The chairman of ABC, Mr. Greshan Mudalige addressing the first board meeting delivered a very comprehensive welcome speech mentioning the importance of a sound corporate governance framework since ABC is now a public company stating that, it is no more a family concern. The board has legal and voluntary duties, and they must act in good faith to create value for the shareholders while satisfying all other stakeholders of ABC hereafter. He just briefed the development of the corporate governance framework and the Code of Best Practices on Corporate Governance - 2017, which has been used as a code in Sri Lanka. Also, he advised the board that it is the duty of the directors to ensure the sound governance principles are implemented and to maintain a sound Risk Management and Internal Control system as an integral part of a sound corporate governance framework. You have been advised by the chairman to educate all the directors by circulating a memo covering the following areas briefly.

You are required to:

4.1. Discuss in brief the corporate governance framework referring to appropriate definitions and directors' responsibility of implementing a sound corporate governance framework in a public company.

(08 Marks)

4.2. Explain according to the provisions of the Sri Lankan code on corporate governance (2017), how ABC PLC could implement a sound Risk Management and Internal Control System in the company.

(12 Marks)

[Total 20 Marks]

QUESTION NO. 05

The following has been extracted from the article under the topic “Covid-19 is Rewriting the Rules of Corporate Governance”, published in the Harvard Business Review in October 2020.

“Boards are facing a complex new reality as a result of Covid-19. The new environment is characterized by pressures and demands from various stakeholder groups, heightened expectations for societal engagement and corporate citizenship, and radical uncertainty about the future. These factors are complicating board decision-making and challenging the shareholder-centric model of governance that has guided boards and business leaders for the past several decades. A board’s ability to deliberate in a thorough and thoughtful, but efficient manner and come to a considered conclusion around key issues will be a critical aspect of its effectiveness in the post-Covid era.”

You are required to:

5.1. Explain what is meant by “the shareholder-centric model of governance” mentioned in the above extract.

(04 Marks)

5.2. Discuss the common challenges/complexities faced by boards of directors in a new environment as a result of Covid-19.

(08 Marks)

5.3. Suggest in brief remedial strategies to overcome the challenges and complexities faced by the board.

(08 Marks)

(Total 20 Marks)

-End of the Question Paper-