

PILOT PAPER – 2023-2027 SYLLABUS

SL4.4 Corporate Governance & Ethics

Strategic Level

ANSWER KEY

Part I – Compulsory Question

QUESTION NO: 01

1.1. Explain the concept of corporate governance and outline its significance in the implementation for a company like PGM&E. (06 Marks)

Candidates are required to explain corporate governance

- Definition of corporate governance.
- Rules, practices, and processes that guide company management and control.
- with reference to decision-making, accountability, transparency, and ethical behavior.

Candidates are required to explain any of the four points of significance for PGM&E.

- Transparency and accountability
- Shareholder protection
- Risk management
- Compliance with regulations
- Ethical behavior
- Long-term sustainability

Mark allocation

- Explanation of corporate governance (maximum 2 marks)
- Four points of significance = 0.5 marks for the identification and 0.5 for the explanation each (maximum 4 marks)

1.2. Examine the Agency theory and the Stewardship theory and their relevance to PGM&E. (05 Marks)

Candidates are required to:

Explain Agency Theory

- Description of the theory that focuses on the potential conflicts of interest between principals (owners) and agents (managers) due to differing goals.

Explain the relevance to PGM&E

- Discussion of how Agency Theory is relevant to PGM&E due to the separation of ownership and management in the company.
- Mention of potential conflicts between shareholders and executives' interests, especially with the expansion and partnership.

Explain the pros and cons

- Identification and explanation of the advantages and disadvantages of Agency Theory. Examples of how this theory might help align interests could also lead to managerial opportunism.

Explanation of Stewardship Theory

- Description of the theory that emphasizes the alignment of interests between managers and shareholders, assuming managers act as responsible stewards of shareholders' resources.

Relevance to PGM&E

- Discussion of how Stewardship Theory aligns with PGM&E's goal to foster responsible corporate behavior, especially during expansion and partnership.
- Mention of the theory's focus on loyalty, responsibility, and commitment.

Pros and cons

- Identification and explanation of the advantages and disadvantages of Stewardship Theory. Examples of how this theory might promote ethical behavior could also overlook conflicts of interest.

Mark allocation

- Explanation of Agency Theory (maximum 0.5 marks)
- Relevance to PGM&E (maximum 1 mark)
- Pros and cons (maximum 1 mark)
- Explanation of Stewardship Theory (maximum 0.5 marks)
- Relevance to PGM&E (maximum 1 mark)
- Pros and cons (maximum 1 mark)

1.3. Discuss the rule-based approach to corporate governance with its advantages and disadvantages. (07 Marks)

Candidates are required to explain the rule-based approach

- The rule-based approach to corporate governance entails adhering to specific rules and regulations set by external regulatory bodies or governing authorities.

Candidates are required to explain the advantages of the rule-based approach

- Clear guidelines
- Legal and regulatory compliance
- Compliance and Accountability

Candidates are required to explain the disadvantages of the rule-based approach

- Rigidity.
- Potential for rule manipulation
- Complexity

Mark allocation

- Rule-Based Approach Explanation: maximum 2 marks
- Advantages of Rule-Based Approach: maximum 2.5 marks
- Disadvantages of Rule-Based Approach: maximum 2.5 marks

1.4. Comment on the major role that should be played by the Board of Directors of the company in the implementation of the appropriate corporate governance framework with reference to the intended joint venture partnership with Bayan Holding Pty Limited (BJH). (05 Marks)

Candidates are required to explain the major roles and responsibilities of the board in relation to corporate governance

1. Setting and enforcing corporate governance policies
2. Oversight of management
3. Appointment of independent directors
4. Risk management
5. Monitoring and reporting

Candidates are required to explain the major roles and responsibilities of the board in relation to corporate governance in the context of the intended Joint Venture partnership with Bayan Holding Pty Limited.

Mark allocation

- Explanation of Board of Directors major roles (3 marks)
- Importance of role in Joint Venture with Bayan Holding Pty Limited (2 marks)

1.5. Examine the status of the independent directorship of Mr. Robert Dahanayake currently, referring to the "Code of Best Practice on Corporate Governance – 2017 of Sri Lanka". (05 Marks)

Candidates are required to explain the independent directorship

- The position held by individuals who are not affiliated with the company, its management, or its major shareholders.
- Independent directors are expected to provide an objective perspective and exercise independent judgment in board decisions, free from conflicts of interest.

Candidates are required to explain the provision related to the independence in Code of Best Practice on Corporate Governance – 2017 of Sri Lanka

- the independent status of a director will be lost if he or she has a close family member who is a director or chief executive officer or Key Management Personnel (and/or an equivalent position)

Candidates are required to evaluate Mr. Robert Dahanayake's status as an independent director according to the Code of Best Practice on Corporate Governance - 2017 of Sri Lanka

- Taking into account any changes in his circumstances or relationships that may have occurred since his appointment.
- Mr. Dahanayake's familial ties, specifically through his son's marriage to the daughter of Ms. Ananda Daassanayke, who holds a position as a family-owned director at PG&ME.

Mark allocation

- Explanation of Independent Directorship (maximum 2 marks)
- Reference to the "Code of Best Practice on Corporate Governance – 2017 of Sri Lanka" (maximum 1 mark)
- Examination of Mr. Robert Dahanayake's Status as an Independent Director (maximum 2 marks)

1.6. Explain the deontological and teleological approaches to ethics. (05 Marks)

Candidates are required to explain the deontological approach to ethics

- In moral philosophy, the deontological approach to ethics emphasizes the importance of duties and obligations.

Candidates are required to explain the teleological approach to ethics

- The teleological approach to ethics, also known as consequentialism, considers the consequences or outcomes of actions as the basis for moral judgment.

Mark allocation

- Explanation of the deontological approach to ethics (maximum 2.5 marks)
- Explanation of the teleological approach to ethics (maximum 2.5 marks)

1.7. Discuss the proposed transaction by Mr. Robert regarding the excess dollars, emphasizing the ethical theories discussed above (1.6). (07 Marks)

Candidates are required to explain the proposed transaction from a deontological perspective

- Selling the excess dollars at a markup raises questions about fairness and transparency. It may be seen as taking advantage of the shortage of dollars to profit at the expense of importers who need to pay a higher price for their imports.
- If the markup is considered unfair and contrary to the principle of fairness, it may be deemed ethically inappropriate.

Candidates are required to explain the proposed transaction from a teleological perspective

- If the transaction leads to overall negative consequences, such as damaging the company's reputation or harming relationships with importers, it may be considered ethically problematic.
- On the other hand, it also may be interpreted as this transaction may benefit the organization in multiple ways.
 - it allows the company to generate additional income by collecting markups from importers, contributing to financial stability and profitability.
 - it may facilitate smoother import processes by providing the necessary currency at a reasonable rate, enabling import-oriented enterprises to operate efficiently and ensuring customers have access to products (including essentials) without deficits.

Candidates are required to provide their recommendations related to the proposed transaction.

Mark allocation

- Explanation of the proposed transaction from a deontological approach to ethics (maximum 3 marks)
- Explanation of the proposed transaction from the teleological approach to ethics (maximum 3 marks)
- Recommendation related to the proposed transaction according to the candidates' perspective (maximum 1 mark)

(Total 40 Marks)

Part II – Answer any 03 questions

QUESTION NO: 02

2.1. Discuss the existing internal control system for the online ordering, delivery, and payment system of MER referring to the Committee of Sponsoring Organizations (COSO) Internal Control-Integrated Framework: (05 Marks)

Candidates are required to explain the relevant application of the COSO Framework to MER's System

- Control environment
- Risk assessment
- Control activities
- Information and communication
- Monitoring

Mark allocation

- Explanation of relevant application of the COSO Framework to MER's System (maximum 5 marks)

2.2. Evaluate the adequacy of the existing internal control system related to the online ordering, delivery, and payment system of MER: (05 Marks)

Candidates are required to be evaluated for their adequacy related to the online ordering, delivery, and payment system of MER.

1. Online ordering and delivery system customer satisfaction.
2. Online payment gateway
3. Daily reports for the Chairman

Mark allocation

- Identification and explanation of the criteria related to the adequacy of the online ordering, delivery, and payment system of MER. (maximum 5 marks)

2.3. Assess possible IT-related (Cyber) frauds that can take place under the current controlling system of MER: (04 Marks)

Candidates are required to explain the possible IT-related (Cyber) frauds that can take place under the current controlling system of MER

1. Unauthorized access and data breaches
2. Phishing and social engineering attacks
3. Malware and ransomware attacks
4. Insider threats

Mark allocation

- Identification and explanation of possible IT-related (Cyber) frauds that can take place under the current controlling system of MER (4 marks)

2.4. Recommend appropriate strategies to enhance the existing internal controls system of MER: (06 Marks)

Candidates are required to Recommend appropriate strategies to enhance the existing internal controls system of MER.

1. Implement Access Controls
2. Regular Security Awareness Training
3. Implement Data Encryption
4. Regular IT Security Audits
5. Implement Fraud Detection and Monitoring Systems
6. Implement Segregation of Duties

Mark allocation

- Identification and explanation of 3 appropriate strategies to enhance the existing internal controls system of MER. (maximum 6 marks).

(Total 20 Marks)

QUESTION NO: 03

3.1. Discuss shareholders' rights and shareholder activism referring to the current situation of ABC PLC: (06 Marks)

Candidates are required to discuss shareholders' rights and shareholder activism.

- Shareholder rights are determined by the company's articles of association and company law, predominantly the Companies Act.
- With the ownership of shares come rights: to receive notice, attend and vote at shareholder's meetings, to inspect the shareholder register and the register of directors and officers, and to regular information.
- However, shareholders do not have the right to be involved in the day-to-day management of the business or to inspect company records or management accounts (Tricker 2011).
 - Shareholder activism is the course of action shareholders take to influence corporate governance by utilizing their ownership privileges.
- The key strategies employed for it are proxy conflicts, negotiations, public campaigns, shareholder resolutions, and litigation.

Candidates are required to discuss the relevance to ABC PLC

- It is essential for ABC PLC to engage in constructive dialogue with the shareholders and address their concerns

Mark Allocation

- Discussion of shareholders' rights and shareholder activism. (2 marks)
- Discussion of shareholder activism (2 marks)
- Relevance to ABC PLC (2 marks)

3.2. Examine possible disadvantages of shareholder activism to ABC PLC and advise possible strategies to explain and convince the current status of the company to the shareholders: (07 Marks)

Candidates are required to explain the possible disadvantages of shareholder activism to ABC PLC.

- Divergence of interests
- Disruption and expenses
- Reputational damage and lower share price

Candidates are required to explain the possible strategies to convince the current status of the company to the shareholders.

- Extraordinary General Meeting (EGM)
- Shareholder Communications
- Shareholder Advisory Panels
- Public Announcements and Press Releases
- Shareholder Engagement Platforms
- Roadmaps and Timelines

Mark Allocation

- Explanation of the possible disadvantages of shareholder activism to ABC PLC. (3 marks)
- Explanation of the possible strategies to convince the current status of the company to the shareholders. (maximum 4 marks)

3.3. Discuss the areas that the Board should pay attention to in order to strengthen the existing corporate governance framework, considering the impact of the pandemic and the economic downturn in Sri Lanka:(07 Marks)

Candidates are required to provide an introduction to the impact of the pandemic and economic downturn on corporate governance.

Candidates are required to discuss the areas that the Board should pay attention to in order to strengthen the existing corporate governance framework, considering the impact of the pandemic and the economic downturn in Sri Lanka

- Legal environment:
- Health requirements
- Future strategic direction
- Financial requirements
- Technological changes
- Stakeholder demands
- Supply chain trends

Mark Allocation

- Explanation of the impact of pandemic and economic downturn on corporate governance: (1 mark)
- Identification and explanation of three areas for the board's attention to strengthen corporate governance. (6 marks)

(Total 20 Marks)

QUESTION NO: 04

4.1. Critically evaluate the importance of having professional behavior by the external auditor of a company in relation to the implementation of good corporate governance of that company:(08 Marks)

Candidates are required to explain the Role of the External Auditor

- Management prepares financial statements.
- Lack of credibility in financial statements due to agency conflicts.
- Independent auditors verify and report findings to shareholders.
- External auditors foster public trust by confirming the accuracy of financial statements.
- Address concerns about the credibility and reliability of financial information.

Candidates are required to explain the external Auditor's Role in Corporate Governance

- Corporate governance ensures effective management and control.
- External auditors contribute to transparency, accountability, and integrity.
- External auditors are independent and separate from the company.
- Their objectivity ensures unbiased assessment of financial statements.
- External auditors regulated by laws and standards.
- Compliance ensures quality work and minimizes abuse.

Candidates are required to apply to ABCH Case

- Importance of professional behavior in ABCH's external audit.
- Adherence to auditing standards, regulations, and IFRS requirements.
- Compromise undermines the credibility of financial statements.
- Affects the trust of shareholders, stakeholders, and market perception.

Mark Allocation

- Role of External Auditor (maximum 3 marks):
- External Auditor's Role in Corporate Governance (maximum 3 marks):
- Application to ABCH Case (maximum 2 marks)

4.2. Discuss ethical and professional issues faced by X&Y Associates in relation to the audit of ABCH: (06 Marks)

Candidates are required to explain the ethical and professional issues in relation to the audit of ABCH.

1. Independence and objectivity
2. Scope limitation and reduced audit fee
3. Failure to value inventory and financial assets at fair value
4. Potential influence from management

Mark Allocation

- Identification and explanation of four ethical and professional issues in relation to the audit of ABCH. (maximum 6 marks)

4.3. Discuss the available remedies and actions for X&Y Associates to overcome those issues effectively: (06 Marks)

Candidates are required to explain the remedies and actions to overcome the ethical and professional issues faced by X&Y Associates in relation to the audit of ABCH.

1. Uphold Independence and Objectivity
2. Expand the Scope of the Audit
3. Address Fair Value Measurement
4. Preserve Auditor Independence

Mark Allocation

- Identification and explanation of remedies and actions to overcome the ethical and professional issues faced by X&Y Associates in relation to the audit of ABCH. (6 marks)

(Total 20 Marks)

QUESTION NO: 05

5.1. Discuss the concept of Digital Corporate Governance and its importance in the context of modern business operations:(05 Marks)

Candidates are required to explain the Digital Corporate Governance concept.

- Digital Corporate Governance refers to the framework and processes implemented by organizations to ensure effective management, control, and oversight of their digital assets and operations

Candidates are required to explain the importance of Digital Corporate Governance

- It helps organizations manage the risks associated with digital technologies and data
- It enhances transparency and accountability
- It supports effective decision-making
- It facilitates the alignment of digital strategies with the organization's overall objectives, enabling agility and innovation in a rapidly evolving digital landscape.

Mark Allocation

- Explanation of the Digital Corporate Governance concept. (2 marks)
- Explanation of the importance of Digital Corporate Governance (3 marks)

5.2. Discuss the importance of sustainability practices for companies such as Company X in the technology sector. Provide examples of sustainable initiatives that can benefit both the company and the environment:(05 Marks)

Candidates are required to discuss the importance of Sustainability practices for companies such as Company X, in the technology sector.

- Reputation and stakeholder engagement
- Risk management
- Cost savings and efficiency
- Innovation and competitive advantage
- Improve goodwill and brand image

Candidates are required to the identification of examples of sustainable initiatives that benefit both the company and the environment

- Adopting renewable energy sources to power operations and reducing carbon emissions.

- Implementing recycling and waste reduction programs to minimize environmental impact.
- Promoting employee well-being and diversity to create a sustainable and inclusive work environment.
- Engaging in community development projects and supporting local initiatives.

Mark Allocation

- Discuss the importance of Sustainability practices (maximum 3 marks)
- Identification of examples (maximum 2 marks)

5.3. Identify three major cyber threats and discuss how they can impact a company, such as Company X, in terms of its operations and reputation: (05 Marks)

Candidates are required to identify three major cyber threats;

- Phishing attacks
- Ransomware attacks
- Data breaches

Mark Allocation

- Identification and explanation of three cyber threats (maximum 05 Marks)

5.4. Present three strategies or practices that can enhance cybersecurity and protect the digital assets of a specific company, such as company X:(05 Marks)

Candidates are required to identify preventive measures to mitigate the cyber risks of companies such as Company X

- Employee training and awareness
- Robust access controls and authentication mechanism
- Regular security assessments and penetration testing
- Incident response and business continuity planning

Mark Allocation

- Identification and explanation of preventive measures to mitigate the cyber risks (maximum 5 marks)

(Total 20 Marks)
