



PAMIBIA UNIVERSITY
OF SCIENCE AND TECHNOLOGY

FACULTY OF COMMERCE, HUMAN SCIENCES AND EDUCATION
DEPARTMENT OF ECONOMICS, ACCOUNTING & FINANCE

QUALIFICATION : BACHELOR OF ACCOUNTING (HONOURS)	
QUALIFICATION CODE: 08BOAH	LEVEL: 8
COURSE CODE: GRE 811S	COURSE NAME: CORPORATE GOVERNANCE, RISK MANAGEMENT AND ETHICS
DATE: JUNE 2025	PAPER: THEORY AND APPLICATION
DURATION: 3 HOURS	MARKS: 100

SECOND OPPORTUNITY EXAMINATION	
EXAMINER:	Dumisani R. Muzira
MODERATOR:	Marko Tandota

INSTRUCTIONS
<ul style="list-style-type: none">• This question paper is made up of FOUR (4) questions.• Start each question on a new page.• Answer All the questions and in blue or black ink.• You are advised to pay due attention to expression and presentation. Failure to do so will cost you marks.• Start each question on a new page in your answer booklet

PERMISSIBLE MATERIALS

Non-programmable calculator/financial calculator

THIS QUESTION PAPER CONSISTS OF 6 PAGES (Including this front page)

Question 1

Z00 LTD

Background information

Z00 Ltd is a large family-owned private company operating in the UK in the contract services sector. The principle business that Z00 undertakes is project management on large, long-term building projects in the UK. Z00 Ltd has no overseas customers. The company provides a complete project management service, enabling the customers to deal just with Z00 Ltd. Z00 deal with all subcontractors. The business has been very successful in recent years and as a result has become a potential acquisition target for a major international company, Nama Inc, based in the US. Nama Inc is listed on the New York Stock Exchange and is interested in furthering its businesses in Europe.

Some of the members of the family that own Z00 Ltd (the Williams) are keen to dispose of their shares and it is therefore expected they will sell to Nama if a suitable price can be agreed. The managing director of Z00, Peter Smith (not in the William family), is currently negotiating with the directors of Nama over a price for the shares.

Following the negotiation Peter will make a proposal to the William family. Peter and other selected staff have already been offered positions in Nama if the acquisition proceeds.

Financing the acquisition

Nama Inc have a corporate policy of financing their acquisitions through loans. In previous foreign acquisitions, they have used either US or foreign loans depending on their views on economic and political factors in the US and in the foreign markets. They have no strong views on where to raise finance. They expect to need to borrow in 4 months' time to finance the acquisition.

One factor that the directors of Nama Inc do feel needs to be considered however is that they are considering selling an existing UK division within a year and the proceeds are expected to be in the region of the acquisition price for Z00 Ltd. The disposal will definitely occur after the acquisition of Z00 Ltd, probably six months later.

Corporate governance

In anticipation of Z00 Ltd becoming part of the Nama Group the group CFO, Bert Bailey, has forwarded to Peter Smith a memo he sent last year to all divisional CEOs on corporate governance. He told Peter that the same process would operate for Z00 Ltd, but with the dates about a year on.

MEMO

To: Divisional CFOs and CEOs

From: Bert Bailey

Subject: SOX compliance

Date: 15 January 2025

As you are all no doubt aware, we are implementing Sarbanes-Oxley (SOX) this year. This memo summarises the timetable; more detail on the processes and procedures required will follow later.

Feb – May Document key financial reporting systems and controls. Decide key controls and report any material design weaknesses in systems

Jun – July Divisional management to test key controls to confirm compliance and the effectiveness of the systems

Aug – Sept Group internal audit to review documentation and testing, and report on each division to the audit committee

Oct – Nov External audit to conduct the majority of their attestation work

Dec Management certification and assertions as required by sections 302 and 404.

The control framework the US companies will be using is the COSO framework. Overseas companies can use a local framework, if desired, provided it is approved in advance by the group SOX project team. Documentation must be standard across the group.

Required:

Explain the risks that could exist for Nama in making the investment in ZOO Ltd and discuss how Nama could assess their likely impact on the company. (25 marks)

Question 2

Tatenda Tan, a fund manager at institutional investor Sentosa House, was reviewing the annual report of one of the major companies in her portfolio. The company, Eastern Products, had recently undergone a number of board changes as a result of a lack of confidence in its management from its major institutional investors of which Sentosa House was one. The problems started two years ago when a new chairman at Eastern Products (Thomas Moo) started to pursue what the institutional investors regarded as very risky strategies whilst at the same time failing to comply with a stock market requirement on the number of non-executive directors on the board.

Tatenda rang Eastern's investor relations department to ask why it still was not in compliance with the requirements relating to non-executive directors. She was told that because Eastern was listed in a principles-based jurisdiction, the requirement was not compulsory. It was simply that Eastern chose not to comply with that particular requirement. When Tatenda asked how its board committees could be made up with an insufficient number of non-executive directors, the investor relations manager said he didn't know and that Tatenda should contact the chairman directly. She was also told that there was no longer a risk committee because the chairman saw no need for one.

Tatenda telephoned Thomas Moo, the chairman of Eastern Products. She began by reminding him that Sentosa House was one of Eastern's main shareholders and currently owned 13% of the company. She went on to explain that she had concerns over the governance of Eastern Products and that she would like Thomas to explain his non-

compliance with some of the stock market's requirements and also why he was pursuing strategies viewed by many investors as very risky. Thomas reminded Tatenda that Eastern had outperformed its sector in terms of earnings per share in both years since he had become chairman and that rather than question him, she should trust him to run the company as he saw fit. He thanked Sentosa House for its support and hung up the phone.

Required

- (a) Explain what an 'agency cost' is and discuss the problems that might increase agency costs for Sentosa House in the case of Eastern Products. (7 marks)
- (b) Describe, with reference to the case, the conditions under which it might be appropriate for an institutional investor to intervene in a company whose shares it holds. (10 marks)
- (c) Evaluate the contribution that a risk committee made up of non-executive directors could make to Tatenda's confidence in the management of Eastern Products. (4 marks)
- (d) Assess the opinion given to Tatenda that because Eastern Products was listed in a principles-based jurisdiction, compliance with the stock market's rules was 'not compulsory'. (4 marks)

Question 3

There has been a debate in the country of Beeland for some years about the most appropriate way to regulate corporate governance. Several years ago, there were a number of major corporate failures and 'scandals' caused in part by a number of single powerful individuals dominating their boards. Business leaders and policymakers were sceptical about a rules-based approach, and this led the Beeland stock exchange to issue guidance in the 'Beeland Code' as follows. 'Good corporate governance is not just a matter of prescribing particular corporate structures and complying with a number of rules. There is a need for broad principles. All stakeholders should then apply these flexibly to the varying circumstances of individual companies.'

Given the causes of the Beeland corporate governance failures, there was a debate about whether the separation of the roles of chairman and chief executive should be made a legal requirement. This resulted in the stock exchange issuing guidance that whilst a rules-based or 'box ticking' approach would specify that 'the roles of chairman and chief executive officer should never be combined ... We do not think that there are universally valid answers on such points.'

One company to take advantage of the flexibility in Beeland's principles-based approach was Anson Company. In July 2010, Anson Company announced that it had combined its roles of chairman and chief executive in a single role carried out by one individual. In accordance with the Beeland listing rules, it made the following 'comply or explain' statement in its 2011 annual report.

'Throughout the year the company complied with all Beeland Code provisions with the exception that from 1 July 2010 the roles of chairman and chief executive have been exercised by the same individual, William Klunker. We recognise that this has been out of

line with best practice. We understand the concerns of shareholders but believe that we have maintained robust governance while at the same time benefiting from having Mr Klunker in control. On 31 July 2012 Mr Klunker will step down as executive chairman, remaining as chairman until we conclude our search for a non-executive chairman to succeed him, no later than March 2013.'

Required

(a) Briefly distinguish between rules and principles-based approaches to corporate governance. Critically evaluate the Beeland stock exchange's guidance that 'all stakeholders should then apply these flexibly to the varying circumstances of individual companies.'

(12 marks)

(b) Explain why a separation of the roles of chairman and chief executive is considered best practice in most jurisdictions.

(8 marks)

(c) Assess the 'comply or explain' statement made by Anson Company in its 2011 annual report.

(5 marks)

Question 4

Num and Moo is an established audit practice in Deetown and has a large share of the audit services market among local businesses. Because Deetown is a relatively isolated area, many clients rely on Num and Moo for accounting and technical advice over and above the annual audit. This has meant that, over time, Num and Moo has also developed expertise in compliance advice, tax, strategy consulting and other professional services.

Because non-audit work is important to Num and Moo, staff have 'business growth' criteria strongly linked with bonuses and promotion. This means that many of the professional accountants in the firm actively seek to increase sales of non-audit services to businesses in the Deetown area, including from audit clients. The culture of the firm is such that everybody is expected to help out with any project which needs to be done, and this sometimes means that staff help out on a range of both audit and non-audit tasks. The lines between audit and non-audit services are sometimes blurred and staff may work on either, as workload needs demand. Managing partner Cherry Moo told staff that the non-audit revenue is now so important to the firm that staff should not do anything to threaten that source of income.

Cherry Moo said that she was thinking of beginning to offer a number of other services including advice on environmental reporting and the provision of environmental auditing services. She said she had spoken to local companies which were looking to demonstrate their environmental sustainability and she believed that environmental reporting and auditing might be ways to help with this. She said she was confused by the nature of environmental reporting and so was not sure about what should be audited.

Required

(a) Explain 'ethical threat' and 'ethical safeguard' in the context of external auditing, and discuss the benefits of effective ethical safeguards for Num and Moo. (8 marks)

(b) Explain 'environmental audit' and assess how environmental reporting and auditing might enable companies to 'demonstrate their environmental sustainability' as Cherry Moo suggested. (8 marks)

(c) Some corporate governance codes prohibit audit firms such as Num and Moo from providing some non-audit services to audit clients without the prior approval of the client's audit committee. This is because it is sometimes believed to be against the public interest.

Required

Explain 'public interest' in the context of accounting services and why a client's audit committee is a suitable body to advise on the purchase of non-audit services from Num and Moo. (9 marks)

