

Part One – Chartered Governance Qualifying Programme

Corporate Governance

Time allowed: 3 hours (plus 15 minutes reading time)

You must not take this paper out of the examination workspace.

The examination paper contains **9** questions of which you must attempt **8**. You must attempt **all questions** in Section A and **3 questions** in Section B.

Section A contains 25 marks and Section B contains 75 marks. There are **100 marks** available in total for the paper.

Note: Unless otherwise specified, you should assume that an Act or an organisation referred to in the questions is a Malaysian Act, Code or organisation.

Section A

Answer **all** the questions in this section.

1. Explain the advantages of the 'apply and explain' approach to corporate governance compared to the 'comply or explain' approach.

(5 marks)

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2. Describe the issues to be considered when designing an effective induction programme for a new non-executive director of a company.

(5 marks)

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3. Explain why a company's external auditor may need to issue a modified audit report.

(5 marks)

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4. Describe how a company can ensure that its Company Secretary is able to give independent advice to the Board.

(5 marks)

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5. Explain whether a company can provide an indemnity or insurance cover for its directors to protect them from liability in relation to their role as directors.

(5 marks)

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TOTAL FOR SECTION A = 25 MARKS

Section B

Answer **three** questions only.

Question 6

Sinarjaya Properties Berhad (Sinarjaya) is a company whose shares are listed on the Main Market of the Bursa Malaysia. Its business is buying, letting, and selling commercial properties.

Sinarjaya complies in full with the Malaysian Code on Corporate Governance (MCCG).

Sinarjaya's business has been loss making over the last year and its major shareholders have been critical of the company's strategy. As a result, the company's CEO handed in his resignation two months ago and the Sales Director has been acting as interim CEO. The Nomination Committee has been leading the search for a new permanent CEO. After conducting interviews of the shortlisted candidates, the Committee has recommended that the Board appoints Lim Xiu Zhi who they think is the outstanding candidate. Lim is the highly regarded CEO of another property company, Bumiprima Real Estate Berhad (Bumiprima).

The Board has approved the appointment of Lim, subject to the Remuneration Committee agreeing a remuneration package with him. Lim has told the Nomination Committee that he will only accept the CEO role if he gets a guarantee that the share awards, he will receive under Sinarjaya's long-term incentive plan (LTIP) will be similar to those he has been receiving at Bumiprima and if the total vesting and holding period for the Sinarjaya shares is reduced to three years to compensate him for losing his future share awards at Bumiprima.

The Sinarjaya Board has asked the management team to develop a new strategy for Sinarjaya to try to make the business profitable again. The outline of the proposed new strategy has been sent to the Board for approval at the next Board meeting. The proposal includes major changes to the company's property portfolio, which would mean the sale of a large number of its existing properties and the purchase of new properties. New bank loans would be required to finance the property purchases unless the company is successful in selling the existing properties quickly and at a good price. The Chair of the Audit Committee is concerned about the sale and purchase plans. In particular, he is concerned about whether the company will be able to negotiate a new loan agreement with its bank and impact of any new bank loan on the company's finances, particularly if interest rates increase over the next year. The Chair of the Audit Committee has therefore asked the Finance Director of Sinarjaya to provide the Board

with a report setting out a risk assessment of the proposed new strategy so that it can be considered at the Board meeting.

REQUIRED:

- (a) Analyse the statutory, Bursa Malaysia Listing Requirements and MCCG practices that the Remuneration Committee will need to consider when agreeing the LTIP share awards for Lim as the proposed new CEO of Sinarjaya.

(13 marks)

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- (b) Discuss how the risk assessment for the proposed new strategy should be carried out by the Finance Director and how the Board should take the assessment into account when considering whether to approve the proposed new strategy.

(12 marks)

[Total for Question 6 = 25 marks]

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Question 7

Brightstar Solar Sendirian Berhad (Brightstar) is a private company which installs solar panels on farmland in Malaysia. The company has been successful and is planning to significantly expand its workforce over the next year. It has just diversified its business by entering into a contract with a building company to install solar panels on the roofs of new houses.

Brightstar has a Board of 5 directors: a non-executive Chair, Liyana Kamil, and 4 executive directors. Following a review of governance, the Board of Brightstar has recently agreed that it should adopt the Malaysia Code on Corporate Governance (MCCG). The Board has also agreed that it should search for, and appoint, two new non-executive directors to the Board. There is currently no ethnic diversity on the Board and all of the executive directors are male. Liyana has asked the Company Secretary of Brightstar, Amira Azhar, to provide a note for the Board about the factors the Board should consider when selecting the new non-executive directors. Liyana says that she does not think that they need to use a recruitment firm as part of the recruitment process because Brightstar can advertise the new roles on social media and can use the networks of the existing Board members to publicise the new roles.

The Company Secretary of Brightstar, Amira Azhar, has been asked by the Finance Director, Tariq Asnan, who has recently joined the Board, to carry out a review of the latest draft of the company's next annual report and accounts (annual report) which is due to be published in a few months' time. In particular, Tariq wants Amira to check if the non-financial information in the draft annual report is sufficient to comply with the mandatory content requirements. He also wants Amira to consider whether Brightstar should expand the information in the annual report on corporate social responsibility issues to include voluntary disclosures that go beyond the mandatory requirements. Tariq thinks that the annual report needs to include more positive news and that it should showcase the company's successes.

REQUIRED:

- (a) Prepare a note from the Company Secretary, Amira Azhar, to the Chair, Liyana Kamil, about the selection process for the two new non-executive directors, explaining how Board diversity and skills should be taken into account.

(12 marks)

- (b) Analyse the role of Amira, as Company Secretary, in relation to the draft annual report and why it would be advantageous for Brightstar to include additional voluntary CSR reporting in its next annual report.

(13 marks)

[Total for Question 7 = 25 marks]

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Question 8

Aspen Animations (Aspen) is a private company which supplies special effects to the film industry.

Aspen was set up 25 years ago by two brothers, Izzuddin Shamsul and Faiz Shamsul. The Board of Aspen consists of 3 directors: Izzuddin is the Chair and CEO, Faiz is the Finance Director and Faiz's daughter, Bella, is the Commercial and Human Resources Director. Izzuddin and Faiz each hold 30% of the shares in Aspen and the other shareholders who hold the remaining 40% are their two sisters and their parents.

The Shamsul brothers have recently asked the Company Secretary of Aspen, Lutfi Amin, to help them to plan for the future ownership and governance of the company. They say that they want to retire in a few years' time and that when they retire they want the ownership and control of the company to be transferred to Bella and to Izzuddin's two children who do not currently work in the business. Izzuddin says that he would like to step down as CEO later this year and become the non-executive Chair of the Company. He would like Bella to become the CEO of Aspen in his place. Faiz is concerned about how the Board should go about splitting the Chair and the CEO roles. Faiz is also concerned about the handover of control to their children. He thinks that the children may have disagreements if they are on the Board together and that they may not want to take the same approach to the business as he and Izzuddin have done.

Aspen has an office in Malaysia and has 40 staff. The Board has been considering whether the company should invest in a new facility outside Malaysia, which would improve its technology capabilities, but which would be expensive to set up. The company has been having problems retaining and recruiting staff. A recent staff survey suggested that staff are unhappy about their working hours and their salaries, with a substantial number of employees saying that they thought that they could get better working hours and higher salaries at other special effects companies. The HR manager has prepared a paper for the Board setting out the results of the survey and suggesting that all staff should be given a large salary increase this year.

Bella has asked Lutfi to provide her with refresher training on her duty as a director to promote the success of the company. Bella wants to understand how the duty applies to Aspen as a family-owned company and whether it means that the directors should try to make the company as profitable as possible each year. Bella also wants to know how she should take the interests of employees into account when performing her duty as a director to promote the success of the company.

REQUIRED:

- (a) Discuss the issues that Izzuddin and Faiz should consider when planning for the future ownership and control of the company by their children and how the role of Chair and CEO should be split.

(14 marks)

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- (b) Explain Bella's duty to promote the success of the company including how she should take the interests of Aspen's employees into account when performing that duty.

(11 marks)

[Total for Question 8 = 25 marks]

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Question 9

Hunter Logistics Berhad (Hunter) is a company which is in the road haulage business and has its shares listed on the Main Market of the Bursa Malaysia. Hunter complies in full with Malaysian Code on Corporate Governance (MCCG).

Last year Hunter sold its business in Ireland and announced that its new strategy was to expand its business in Malaysia rather than internationally. The company has just announced its half year results which showed that the profits of its Malaysia business have fallen. The Hunter share price dropped significantly after the results announcement. As a result, three of Hunter's institutional shareholders, including one with a 2.5% holding, have privately expressed concerns to the Board about the Board's strategy. The shareholders have suggested that the Board should not be just focusing on expansion of the business in Malaysia, but the Board has rejected their criticisms. The three institutional shareholders are all signatories to the Malaysian Code for Institutional Investors (MCII). A new shareholder has recently acquired a 1.5% shareholding in Hunter. Hunter's registrar thinks that the new beneficial owner of the shares is an activist hedge fund but the name in which the shares are registered in the company's register of members is a nominee company. The Hunter Board is concerned that the new shareholder could join with the other activist shareholders to try to challenge and change Hunter's strategy.

Hunter has recently been the subject of a critical report by a climate change group which said that Hunter had not yet provided any strategy for changing to electric vehicles and that its longer-term sustainability is therefore uncertain. The Board has asked the Audit Committee whether, given the likely impact of the phasing out of petrol and diesel vehicles in future, the company's climate change related risks need to be reassessed and whether the risk disclosures in the annual report and accounts need to be amended to reflect that new assessment.

REQUIRED:

- (a) Explain how the Hunter Board could get information about the new beneficial owner of the 1.5% shareholding in the company and what shareholder rights the hedge fund and other activist shareholders might use to try to challenge and change Hunter's strategy.

(11 marks)

- (b) Analyse the [statutory, Listing Requirements and MCGG] responsibilities of the Board and the Audit Committee for the assessment of Hunter's climate change risks and the disclosures about those risks in its annual report and accounts.

(14 marks)

[Total for Question 9 = 25 marks]

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TOTAL FOR SECTION B = 75 MARKS

TOTAL FOR PAPER = 100 MARKS

The scenarios included here are entirely fictional. Any resemblance of the information in the scenarios to real persons or organisations, actual or perceived, is purely coincidental.

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