



# Examiner's report

## P1 Governance, Risk & Ethics

### December 2017

#### Introduction

Once again the overall performance of candidates in this paper was good and it provided the opportunity for the well prepared candidate to score well.

#### General Comments

The examination consisted of the standard two sections. Section A contained one question for 50 marks and Section B contained three 25 mark questions, from which candidates had to answer two.

In general most candidates scored equally well in Section A and Section B, which was pleasing, with the majority answering Section A first. This is not mandatory and provided a close eye is kept on time candidates could answer Section B questions first if desired. Candidates should also note that writing pages and pages and going into several additional booklets does not necessarily guarantee success. Indeed a key skill that is being tested, and one which is needed in a modern working environment, is the ability to be able to write in a concise and to the point manner. There is no negative marking in the exam but writing pages of factually correct points, but irrelevant to the question set, will score no marks and will eat into the valuable time available.

Future candidates are also advised to make full use of all the resources freely available to them and two such free resources are highlighted here. Firstly, the published accounts for most public limited companies are freely available on the web. Time is well spent reading through the corporate governance sections to get a feel of the type of information presented as well as the tone and style. Try to look through a range of different entities, in different industries and different regulatory jurisdictions. Secondly, candidates should make full use of the technical articles and study support videos that are freely available on the accaglobal website. For this diet, articles such as "Diversifying the Board – a step towards better governance", "COSO's enterprise risk management framework", "Independence as a concept in corporate governance", and "Ethical decision making" were all directly relevant to the questions set. Similarly, candidates that performed well clearly demonstrated the points raised in the study videos "Answering P1 questions on corporate governance", "Ethical theories kept simple", "Focus on risk" and "Professional marks – the difference between a pass and a fail". Please make use of all these freely available resources that can make the difference between a pass and a fail.

#### Question One

The long case study for this diet concerned a world leading organisation in a highly volatile industry, where there is heavy competition for key markets, products and key staff. As a consequence there is high staff turnover within the industry and organisations are always trying to identify new opportunities, either through diversification or acquisition, in order to maintain market share and returns for shareholders. Details were given as to the constitution and the current effectiveness of two committees required by corporate governance regulation, as well as shareholders concerns regarding the pay and performance of key personnel.

Part (a) for 6 marks required a discussion on the accountability of non-executive directors with regards to one particular corporate governance issue. The stronger candidates limited their answer to this one particular issue and scored well. Weaker candidates gave a generic list of the roles and characteristics of non-executive directors, the majority of which was irrelevant to the question set.

Part (b) was very well answered and many candidates scored the maximum 10 marks. Candidates had to explain the key components of the point discussed in part (a) and then explain the benefits of each to the organisation. Well-constructed answers often had a sub heading for component, and a sub heading for benefit. In this way candidates reminded themselves to answer both parts. Weaker candidates tended to discuss the characteristics rather than the components.

Part (c) 6 marks were available for a discussion on how the brief for one of the corporate governance committees discussed in the case could be extended and the benefits that would bring to the organisation. Once again as in part (b) well prepared answers clearly stated the nature of extension and then the benefit that would bring, ensuring they answered both parts of the question to maximise marks – future candidates are advised to adopt this approach.

Part (d) required a statement to be produced to be included in the annual report. There were four professional marks available for clarity, persuasiveness, flow and appropriate structure. It was disappointing that very few statements were actually produced – there were many letters, memos and speeches but unfortunately these were not required. Future candidates are advised to be fully familiar with the contents and structure of a set of published accounts, together with the reports contained therein.

Part (d)i for 8 marks required a discussion of the link between pay and performance, specifically concerning key areas highlighted in the case. The better answers concentrated on the issues raised in the case whereas weaker candidates provided generic text book answers on pay and performance.

Part (d)ii required identification, explanation and critical evaluation of risks the organisation faced on a particular issue given the circumstances raised in the case and this was generally well answered. It was very pleasing to see a significant majority of candidates clearly highlighting the pros and cons to answer the critical evaluation. There were 8 marks for this part.

Part (d)iii The final part for 6 marks required an explanation of a specific risk (that had been discussed in the case), and the appropriateness of a particular business strategy to reduce that risk to the organisation. In general this was not well answered – many struggled to explain the risk correctly and a significant minority did not attempt this part.

## **Question Two**

The first optional question in Section B, and the most popular of all the optional questions, concerned a well-established public limited company currently undergoing its statutory annual audit. The scenario provided details of the company and the audit firm, highlighting long established links at senior level between the two organisations, and potential areas for concern discovered during the audit process.

Part (a) 7 marks were available to effectively evaluate the actions described in the scenario of a key member of personnel of the public limited company. Candidates had to describe what the primary roles were, to criticise the actual actions and then to recommend more appropriate behaviour. It was very pleasing to find that this question was generally very well answered with many candidates scoring full marks. Many candidates, although scoring heavily, wrote in great detail and often came up with valid points that could earn no more marks as the maximum had

already been achieved. Future candidates should take note of the requirements and how many marks there are and then write their answer accordingly. In this case there were three elements – to describe the role, to criticise and to recommend all for 7 marks. Each of these elements could be worth no more than 3 marks so candidates must try to think about how great a detail they should provide in an answer considering the marks that are available.

Part (b) required an explanation of the potential areas of concern highlighted in the scenario with regards to the threat of independence. As with part (a) this was once again generally very well done. However once again, with only 6 marks available for this part, many candidates would have exceeded their time allocation on this part judging by the amount that was written.

Part (c) for 12 marks required recommendations for both the public limited company and the audit firm to prevent such threats arising in the future. Despite this part being almost twice as many marks as part (a) and part (b) the majority of answers were very short, and as a result could not score very highly. This was probably due to candidates running out of time on the question, as a result of spending too much time on parts (a) and (b). Once again future candidates are reminded to allocate time between questions and also between parts of a question depending upon the marks available. Where candidates had attempted a fuller answer, many points related to corrective measures rather than the required preventative measures.

### **Question Three**

This was the least popular of the three optional questions and concerned a very successful global pharmaceutical company looking to develop a new drug. The company achieves high levels of return from its existing products and as a result enjoys an excellent relationship with its investors. A key aspect of the success of the company is down to its extensive and highly effective internal controls.

Part (a) for 12 marks required candidates to evaluate the main components of the internal control system. Weaker candidates tended to either produce a generic list of the features of a successful internal control system with no reference at all to the case, or tried to find only fault in the controls. Stronger candidates scored very highly on this part, clearly understanding the verb evaluate and producing an answer that made a judgement on the controls highlighted in the case. The fact that this was a successful company meant that there were very few weak areas and future candidates should note that questions will not all be based on weak or failing organisations.

Part (b) required an explanation of the need for a certain report to be issued to the shareholders of the company and to describe what the main contents of that report would be. Many candidates made a reasonable attempt at the needs for the report but answers on the content of the report were weak, with many clearly guessing. This part was worth 8 marks.

Part (c) The final part of this question for 5 marks required an explanation for the need for adequate information and this was generally not well answered. Many candidates saw the word “information” in the question and proceeded to write about the characteristics of useful information. This completely missed the point of the question and future candidates are advised to stop and think for a minute before they dive in to ensure they are answering the question set and not the question they would like to be set.

#### **Question Four**

The final optional question of this diet concerned a multi-national retail company that had become insolvent as a result of recent poor strategic decisions. The collapse of the share price and the loss of thousands of jobs instigated an independent enquiry which produced a damning report that highlighted the main reasons for the failure. Key amongst these was the non-compliance by the company to a particular key element of the corporate governance code of the country where the company was registered.

Part (a) 8 marks were available for an explanation of the board level responsibilities in regards to this particular key element of the corporate governance code. Strong candidates produced relevant and specific points whereas the weaker candidates provided a list of all board level responsibilities – some of which were not relevant to the question.

Part (b) for 9 marks required candidates to discuss how the company could have mitigated against the key reasons for the failure as identified in the case scenario. Once again the stronger candidates scored well on this, clearly identifying the reasons for the failure and coming up with suitable mitigations. Weaker candidates provided generic answers on general risk mitigation which could not score many marks, and provided little or no application to the information in the case.

Part (c) for 8 marks required a description of a particular ethical stance followed by description of the behaviour of the board was a clear breach of that particular ethical approach. Candidates who could effectively describe the ethical stance could often clearly relate it to the case and would go on to score well. Future candidates are reminded that a wide breadth of knowledge is required for this Professional level paper as a surprisingly large minority either missed this part out or could not provide a correct description.