



CS ADVANCED LEVEL

PILOT PAPER

GOVERNANCE AND COMPLIANCE AUDIT

December 2021.

Time Allowed: 3 hours.

Answer ALL questions. Marks allocated to each question are shown at the end of the question.

QUESTION ONE

MEDICO DIAGNOSTICS LIMITED (MDL)

Medico Diagnostics Limited (MDL) is an ultra-specialist medical laboratory. Started in year 2004 by two retired medical doctors in the Westland's suburb of Nairobi, the health services provider has steadily expanded to have laboratories in the main cities in Eastern Africa. Over this period MDL has experienced very minimal changes in the top management with Dr. Tom, one of the founders being the Executive Chairman since Dr. Tito the other founder member started ailing in 2009. Most of the Board Members have served continuously for over 10 years. Tommy, as he is affectionately called by employees, the Executive Chairman has hinted at retirement due to advanced age and having served in the combined role for 12 years of a full 17-year career at MDL. Although the Board of MDL has never formally considered the issue of succession planning, anxiety has started setting in at the MDL headquarter. This concern has arisen due to a number of factors. First is the advanced age of Dr. Tom, the poor health of Dr. Tito and the changing market dynamics facing MDL. MDL has operated as a niche medical provider since inception. However, this changed with the onset of the COVID- 19 in early 2020 that saw the demand for laboratory services increase astronomically. This saw MDL opening many satellite laboratories to meet the increasing demand for testing services. Established hospitals entered into testing service contracts with MDL. One of the young shining stars at MDL has been Dr. Shem, the Chief Operating Officer (COO). During one of the end of year parties for the Staff and Board, the Executive Chairman was overheard telling one of the invited guests that, "heading to my sunset years, I wouldn't mind leaving MDL in the hands of Dr. Shem... That lad will go places".

Dr. Shem has spearheaded the growth of MDL and especially in pinpointing strategic locations for the MDL satellite laboratories. The Board of Directors (BOD) is quite pleased with their COO's performance. The Board has 15 members with 12 being company executives heading specialised units and the other three being prominent medical personalities sourced from Tanzania, Uganda and Rwanda were MDL has operations. The three Non-executives were drafted in by the Executive Chairman due to their key expertise in MDL's regional markets. None have regular contact with shareholders and fellow board members. The board meets irregularly and mainly to review current financial performance. Dr. Shem as the COO has complete freedom to act with consultation with the Executive Chairman and this is widely seen as the reason for the company's positive trading position in a highly specialised and competitive medical field.

The Shareholders of MDL are also pleased with the performance of MDL and especially the performance during the COVID-19 pandemic which saw revenues more than triple. However, apprehension and reservations are being felt and expressed by some shareholders due to the advanced age of the Executive Chairman and Dr. Tito the ailing major shareholder and cofounder. Two Pharmacies who are institutional investors have aired their concerns as to the sustainability of the corporate governance structures and current corporate strategy especially whether enough demand for its laboratory services will exist post-pandemic and whether risks associated with the new markets make MDL over exposed and vulnerable. The Corporate Secretary has also advised the Board on the inadequacies of the current board structure, remuneration of directors which appears haphazard and determined by the Executive Chairman. There is also need for Board reappointments to be based on performance as determined by a formal board evaluation. The Board has only one committee named Executive Committee composed of the Executive Chairman, the COO and the other executive directors which meets only to discuss those issues the Board feels need to be allocated more time than what is available during its infrequent Board meetings. The Board lacks a formal charter and Board work plan and most board meetings are impromptu and attended by whoever is available without quorum requirements. This has been such a challenge for the regional non-executive directors who rarely attend board meeting.

While MDL has recognised the need to have the foreign directors from the regional markets who have influence and medical experience in their home countries, the corporate secretary has pointed out that the Board needs to be directly accountable to the shareholders of MDL. He has also recommended that a Governance and Compliance Audit and a Board Evaluation be conducted whose aim will be to advise the Board on best practices in corporate governance.

Required:

As an Accredited Governance Auditor and with reference to the scenario discussed above, discuss changes to governance structure that you would recommend for MDL. (10 marks)

- (a) Describe the role of Non- Executive Directors in MDL. (10 marks)
 - (b) Explain the scope of a board evaluation that should be conducted by MDL. (10 marks)
 - (c) Elaborate the responsibilities of the Remuneration Committee in improving the governance of MDL. (10 marks)
- (Total: 40 marks)**

QUESTION TWO

- (a) Governance audit criteria are benchmarks used to evaluate the subject matter in a governance audit. Explain the various sources of governance audit criteria. (5 marks)
 - (b) Explain the role of a compliance officer in governance and compliance risk management. (5 marks)
 - (c) Governance audit approaches and reports should not only address management and shareholder interests. Identify four other stakeholders of an organization and determine their different uses of a governance audit report. (5 marks)
- (Total: 15 marks)**

QUESTION THREE

- (a) Discuss the professional principles that bind a governance auditor and his engagement team while conducting a governance audit. (4 marks)
 - (b) Before accepting a governance audit assignment, a governance auditor is required to carry out due diligence concerning his independence. Explain three independence compliance requirements for an auditor. (3 marks)
 - (c) Efficient governance audits require adequate planning. Highlight the importance of Governance Audit Planning. (4 marks)
 - (d) The Current Governance Audit File (CGAF) - contains information and audit evidence relating to the current period under review, the purpose of which is to support the opinions and statements made in the audit report. Discuss four typical contents of CGAF. (4 marks)
- (Total: 15 marks)**

QUESTION FOUR

- (a) Explain the issues that are likely to be highlighted in a management letter in the conduct of a governance audit. (4 marks)
 - (b) Explain four methods of collecting governance audit evidence that can be used to form a governance audit opinion. (4 marks)
 - (c) Explain three possible impacts of a qualified governance audit report. (3 marks)
 - (d) Discuss the challenges organizations a likely to face in implementing governance and compliance audit recommendations. (4 marks)
- (Total: 15 marks)**

QUESTION FIVE

- (a) A Governance Audit Report presents a report on circumstances prevailing within the defined audit period and immediately after the period of audit. Discuss four post governance audit events that a governance auditor may include in the governance audit report. (5 marks)
 - (b) Discuss the professional responsibilities of a Peer Reviewer in governance auditing. (5 marks)
 - (c) The ICS Champions of Governance (COG) Award is a voluntary best practice award for excellence in governance to organizations and individuals who have exhibited the highest standards of practice of good governance. Explain the parameters that are evaluated in the ICS COG Award. (5 marks)
- (Total: 15 marks)**