Knowledge Checks: Multiple Choice Questions and Solutions

ETHICS AND GOVERNANCE

Version 16a

Contents

Questions

Module 1

Question 1.1

Which **three** of the following are traditionally recognised as being attributes of a profession?

A the service ideal
B extensive preparatory education
C substantial financial remuneration
D application of professional judgment

(EG ID 1.1)

Question 1.2

Which **three** of the following features are included in the concept of 'service ideal'?

A the efficient and effective use of society's resources
B the provision of accounting-related services as cheaply as possible
C the pursuit of excellence in accounting practice by the individual professional accountant
D the responsibility to behave in a manner that maintains the good reputation of the profession

(EG ID 1.2)

Question 1.3

Which **one** of the following describes the way that accounting interacts with society and organisations?

A Accounting can change society's behaviour through changes in accounting policy.
B Accounting responds to the needs of society and as such reacts to change rather than creating change.
C Accounting is not appropriately placed to make changes in society because accountants are more interested in making money than in seeking what is best for society.
D Accounting involves recording and reporting useful information, and, as such, it should remain impartial and objective and not be concerned about people, organisations and societies.

(EG ID 1.3)

Question 1.4

Which **one** of the following **best** describes professional judgment?

A the acquisition of knowledge through a formal educational process
B the ability to diagnose and solve complex, unstructured 'values-based' problems
C practical experience that ensures the accounting role can be completed in a professional manner
D problem-solving and the ability to apply the right technical solution despite pressure or social ideals

(EG ID 1.4)

Question 1.5

Which **one** of the following is a likely implication for the accounting profession following the collapse of large companies such as Enron, HIH Insurance and Lehman Brothers?

A an increase in the profession's autonomy
B increased regulation and greater scrutiny by the regulators
C a tendency for the community to have more faith in the accounting profession
D a further reduction in the number of large accounting firms resulting from a merger process

(EG ID 1.5)

Question 1.6

The corporate collapses of the early 2000s and those that occurred during the Global Financial Crisis had some important common themes that we must understand if, as professionals, we are to assist in preventing their recurrence.

Which **three** of the following were common themes of the corporate collapses?

A They were the result of directors abusing their trust.
B The collapses were not associated with incentive payments and greed.
C They had a negative impact on the credibility of the accounting profession.
D They demonstrated a willingness of corporations to engage in risks that were not fully understood.

(EG ID 1.6)

Question 1.7

Which **three** of the following statements correctly describes a profession?

A Professions exist mainly to serve society.
B Professions are strictly regulated by external bodies.
C Professions have a substantial degree of independence and autonomy.
D Professions are given permission to provide services to the public through some regulatory process.

(EG ID 1.7)

Question 1.8

Accounting meets the traditional attributes of a profession by upholding which **three** of the following?

A achieving in all circumstances the best outcome for the client
B specialist skills and experience supported by a well-founded body of knowledge
C professional judgment to diagnose and solve complex, unstructured values-based problems
D a service ideal in which the reliable quantifying and reporting the basic facts of economic life serves the public interest

(EG ID 1.8)

Question 1.9

The multi-dimensional role of the professional accountant in a mid-sized business includes generating value through which **three** of the following?

A managing risk and measuring performance
B managing costs through rigorous budgeting and forecasting
C looking for external opportunities to invest the capital of the business
D creating and implementing management information systems to bolster strategy and decision-making

(EG ID 1.9)

Question 1.10

The Professional Accountants in Business (PAIB) Committee of IFAC has identified a multi-dimensional role for accountants in generating value for business including which **three** of the following?

A managing risks
B upholding integrity
C creative accounting
D establishing a common 'performance language'

(EG ID 1.10)

Question 1.11

John and his supervisor Elizabeth work as auditors for a hedge fund. When they finalise their annual audit the valuation of the company is far higher than John expected, and he suspects Elizabeth has inflated the valuation to please management and ensure their bonuses.
What should John do?

A Confront Elizabeth regarding his suspicions.
B Nothing, his responsibility is to the company.
C Report his suspicions to the hedge fund's senior management.
D Report his suspicion to the General Manager Professional Conduct (GMPC) of CPA.

(EG ID 1.11)

Module 2

Question 2.1

Which **one** of the following advertising strategies is allowable for members of CPA Australia under its ethical rules?

A Outlining the qualifications of the firm's partners.
B Indicating that a favourable taxation ruling is likely.
C Including unsubstantiated endorsements from leading business people.
D Comparing your services as superior to those of your major competitors.

(EG ID 2.1)

Question 2.2

Which **one** of the following statements is **not** a relevant reason for an accountant to liaise with their predecessor when accepting a professional assignment?

A It is a matter of professional etiquette.
B To avoid the appearance of solicitation.
C To determine whether the professional fees charged were adequate to avoid threats to due care.
D To identify whether there are professional reasons why the appointment should not be accepted.

(EG ID 2.2)

Question 2.3

Which fundamental principle of professional and ethical conduct is described by the phrase 'having the courage to pursue one's convictions'?

Select which **one** of the following is correct.

A integrity
B objectivity
C confidentiality
D professional competence and due care

(EG ID 2.3)

Question 2.4

Which **one** of the following describes a heuristic approach to decision-making?

A Decisions are based on decision rules or rules of thumb.
B Decisions are in compliance with an ethical code of conduct.
C Decisions are based on the application of an ethical decision-making model.
D Decisions are based on a deontological approach that considers intentions to be important.

(EG ID 2.4)

Question 2.5

In a conflict of interest situation, to **whom** is the accountant's first obligation?

A the client
B the public
C themselves
D the government

(EG ID 2.5)

Question 2.6

In which **one** of the following situations is the duty of confidentiality most likely to be breached?

A When information is disclosed in a court of law.
B When information is disclosed in response to a formal investigation by CPA Australia.
C If the accountant obtains authorisation from the client before disclosing the information.
D If information is disclosed after the accountant has resigned from their position with the employer.

(EG ID 2.6)

Question 2.7

Which **three** of the following are fundamental principles of professional conduct as outlined in the *Code of Ethics for Professional Accountants*?

A integrity
B public interest
C professional behaviour
D professional competence and due care

(EG ID 2.7)

Question 2.8

When may gifts made to an accountant within a workplace setting be accepted?

Select which **one** of the following is correct.

A When they are significant in value.
B If they are intended to encourage unethical behaviour.
C When they are made in the normal course of public relations.
D When you are authorised by your senior management to give an expensive gift to the external accountant.

(EG ID 2.8)

Question 2.9

What type of threat is most likely to arise when a client with a dominant and persistent personality attempts to influence an accountant's professional judgment?

Select which **one** of the following is correct.

A advocacy
B familiarity
C self-interest
D intimidation

(EG ID 2.9)

Question 2.10

Which **one** of the following statements regarding utilitarianism is correct?

A Utilitarianism is a deontological theory focused on consequences.
B The decision-maker focuses on the outcomes or consequences to themselves.
C Utilitarianism is a version of egoism and is focused on the outcome of the decision, not the intention.
D Utilitarianism aims to maximise benefits to the greatest number of people both in the short and long term.

(EG ID 2.10)

Question 2.11

Which **one** of the following statements is **most** likely to lead to an effective code of ethics in a corporate organisation?

A If leadership reflects management's personal values.
B When the unwritten code of ethics is effective in influencing behaviour.
C If the rules on ethical behaviour in the code of ethics are prescriptive and explicit.
D When management behaviour is congruent with the principles of the corporate code of ethics.

(EG ID 2.11)

Question 2.12

Professional independence is a subset of which **one** of the following pairs of fundamental principles?

A integrity and due care
B integrity and objectivity
C integrity and professional competence
D objectivity and professional behaviour

(EG ID 2.12)

Question 2.13

Which **one** of the following statements is correct in regard to earnings management?

A It occurs only when profit is low.
B It is the result of professional judgment.
C It is the practice of maximising earnings.
D It represents the manipulation of reported earnings.

(EG ID 2.13)

Module 3

Question 3.1

Which of the following are **key** corporate factors driving the need for better governance? Select which **three** options are correct.

A the growth in shareholder activism
B the requirement to access lower-cost debt and equity finance
C higher levels of individual taxation dissuading potential shareholders
D increasing competition making high levels of performance harder to achieve

(EG ID 3.1)

Question 3.2

Which **one** of the following is **not** a function of the board of a large public company?

A the selection of auditors
B monitoring the CEO's performance
C managing the day-to-day operations of the corporation
D the oversight of management in the application of policies and guidelines about the principal risks faced by the company

(EG ID 3.2)

Question 3.3

A board committee is **best** described as a subset of the board formed to achieve which **one** of the following outcomes?

A enhance the effectiveness of the board
B report to shareholders on specific issues
C enable directors to reduce their individual liability
D being independent by having exclusively independent directors

(EG ID 3.3)

Question 3.4

Which statement **best** describes the view taken by Nobel Prize-winning economist Milton Friedman in relation to companies?

A Companies are an integral part of society and, as such, should adopt the highest ethical principles.
B Companies, as part of society, should act in the interests of harmonisation of society and the environment.
C Companies should detach themselves from the environment and focus on maximising the benefits to society.
D Companies must obey community rules and should focus on maximising returns to shareholders by appropriate means.

(EG ID 3.4)

Question 3.5

Which **one** of the following is an important concern in the OECD Principles of Corporate Governance (2015)?

A directors' rights
B regulators' rights
C shareholders' rights
D triple bottom line accounting

(EG ID 3.5)

Question 3.6

The California Public Employees' Retirement System (CalPERS), (a US pension fund manager), has had an impact on corporate governance internationally, due to which of the following?

Select which **two** options are correct.

A It requests its members not invest in shares.
B It assists companies in which it invests to appoint directors.
C It supports good corporate governance through investing in companies that practise it.
D It informs the international business community that it has opinions on corporate governance practices in companies in which it invests.

(EG ID 3.6)

Question 3.7

Which of the following are characteristics of the market-based system?

Select which **three** options are correct.

A Bonds and loans are the most important source of finance in this system of corporate governance.
B Dispersed investors require reliable and adequate information flows in order to make informed investment decisions.
C Regulation is intended to ensure relatively complete information for investors and to prevent privileged groups of shareholders sharing information only among themselves.
D Bank finance has tended to be short-term, and banks have tended to maintain arm's-length relationships with corporate clients. Equity finance has been more important as a means of developing companies.

(EG ID 3.7)

Question 3.8

France and Italy are the European countries with the smallest ownership of company shares by financial institutions. Which of the following conditions prevail?

Select which **three** options are correct.

A Corporate governance systems in these countries emphasise consensus rather than competition.
B In France, the role of CEO and chair are combined in the role of the *président directeur général* (PDG), who is strongly accountable to the board.
C In France, the majority of shares have traditionally been owned by non-financial enterprises, which reflects an elaborate structure of cross and circular ownership.
D Stable investment shields managers from the short-term pressures of the market by making a change in corporate control a more difficult feature. This may be conducive to long-term, relation-specific investments, but it also weakens pressures to maximise performance.

(EG ID 3.8)

Question 3.9

Which of the following are characteristics of corporate governance in East Asia?

Select which **three** options are correct.

A Institutional investors have a significant effect on standards of governance.
B Disclosure and transparency are often limited, so it is more difficult for the legal and regulatory authorities to take action if they are inclined to do so.
C On the boards of companies, there is often no clearly defined role for non-executive directors, and lack of knowledge of the obligations and functions of company officers is widespread.
D Decision-making bodies are often not effective in carrying out their formal roles. Sometimes they are unable to exercise their rights, and boards are co-opted by the dominant shareholders.

(EG ID 3.9)

Question 3.10

For companies located in East Asia, which **one** of the following is **not** an important objective when developing more robust modes of governance?

A allowing business networks to strengthen their position
B clarifying and strengthening internal control structures within firms
C developing training and information programs to improve the understanding of corporate governance procedures and issues
D strengthening external monitoring and control through improvements in the legal framework, enhanced by regulatory agencies and greater disclosure of information

(EG ID 3.10)

Question 3.11

Which **one** of the following statements **best** describes characteristics likely to be found in agency relationships?

A An agent will find it relatively easy to achieve the best interests of the principal in most agency relationships.
B It is necessary to monitor an agent extensively, even where that agent voluntarily assumes the imposition of high bonding costs.
C Agents who are highly bonded will be expected to try to maximise the returns of their principal and will be expected also to seek returns for themselves.
D Agents will often not provide sufficient signalling to principals. It is principally this factor that results in principals finding it necessary to engage in and pay for monitoring.

(EG ID 3.11)

Question 3.12

Which **one** of the following would **not** be an example of an agency cost?

A audit fees
B dividends
C delegated authorities
D information asymmetry

(EG ID 3.12)

Question 3.13

Which of the following can be considered opportunistic residual loss behaviour by an agent?

Select which **two** options are correct.

A purchase of an expensive painting for the managing director's office
B investing in technology that will substantially reduce short-term profit, but yield returns in the longer term
C suspending negotiations with a potential acquisition target because it would not enhance shareholder wealth
D delaying maintenance expenditure in order to meet current profit targets as this will result in profit-related bonuses for a manager

(EG ID 3.13)

Question 3.14

South Ltd has a remuneration policy of paying a bonus to senior managers of 0.1 per cent of profits above a target profit of $50 million. The maximum bonus payable is $750 000. South's reported profit forecast is $40 million per year for the next two years. According to agency theory, which of the following would be the **most** likely management actions?

Select which **two** options are correct.

A Defer maintenance expenditure, saving $2 million in expenses.
B Undertake all preventative maintenance in the current year, reducing profits by $6 million.
C Bring forward a review of asset values, resulting in an asset write-down of $12 million against current profits.
D Capitalise research and development expenditure, which would have been expensed, resulting in an increase to profits by $3 million.

(EG ID 3.14)

Question 3.15

Stakeholder theory is **best** described as being based on the presumption that the corporation has direct concerns about its relationships with

A the corporate regulator.
B the directors of the corporation.
C the shareholders of the corporation.
D a wide range of groups that affect and/or are affected by the corporation.

(EG ID 3.15)

Module 4

Question 4.1

Which **one** of the following would be the **best** way for a shareholder (not being an institutional shareholder) to become involved in the corporate governance of a listed corporation in which they own shares?

A by taking an active interest and an active role in the management of the corporation
B by voting through proxy or by attendance at the general meetings of the corporation
C by selling their shares on the market because the corporation fails to pay dividends at an appropriate level
D by overruling board decisions, including through votes against the board in relation to non-binding shareholder votes

(EG ID 4.1)

Question 4.2

Which **one** of the following statements **best** describes an independent director of a listed corporation?

A a non-executive director who holds 20 per cent of the shares in the corporation
B an executive director who is a CEO but who receives no additional remuneration for being on the board
C a non-executive director who receives a flat fee for being a director and who accepts no additional consulting, advisory or performance-related fees
D a full-time employee of a bank who is appointed to the board at the request of the bank (a major lender to the corporation) and is instructed by the bank to always vote in the interests of the corporation's shareholders

(EG ID 4.2)

Question 4.3

Mr Smith is a director of a corporation. He is aware that the corporation is about to announce the appointment of a high-profile industry leader to chair its board. Mr Smith suspects that this may affect the price of shares in the corporation. He mentions the imminent appointment to his friend, Mr Jones, who immediately purchases shares in the corporation, which increase in value once the announcement of the chair is made.

Which **one** of the following options **most** accurately reflects the legal position of Mr Smith and Mr Jones?

A Mr Smith is potentially liable for insider trading, but Mr Jones is not.
B Mr Jones is potentially liable for insider trading, but Mr Smith is not.
C Both Mr Smith and Mr Jones are potentially liable for insider trading.
D Neither Mr Smith nor Mr Jones is potentially liable for insider trading.

(EG ID 4.3)

Question 4.4

Which **one** of the following is **least** likely to be relevant in determining whether an agreement between a corporation and consumer is unconscionable?

A whether undue influence was applied to the consumer
B whether the consumer was able to understand the documents used
C the difference in the strength of the bargaining power of the parties
D the extent to which the corporation drove a 'hard and tough' bargain

(EG ID 4.4)

Question 4.5

Listed corporations are required to meet continuous disclosure requirements. This requirement is designed to ensure a fully informed market and, as such, also assists in reducing the risks of insider trading.

Which **one** of the following situations is most likely to result in the **greatest** risk of insider trading?

A An entity held information that would have a material effect on the price of its securities and immediately disclosed it to the stock exchange.
B An entity held information that a reasonable person would not expect to have a material effect on the price of its securities and so immediately notified the stock exchange.
C An entity is in confidential discussions regarding a proposed takeover that would have a material effect on the price of its securities, but decides not to notify the stock exchange until the negotiations are complete.
D An entity has been ordered by a court to pay a significant fine, which, if paid, would have a material effect on the price of its securities. However, as the entity is going to appeal the decision, it decides not to notify the stock exchange.

(EG ID 4.5)

Question 4.6

Which **one** of the following statements is **not** correct in relation to legal compliance programs?

A Compliance programs can help promote ethical behaviour and a quality focus within the corporation, leading to a lower likelihood of breaching legislation.
B A breach of legislation will probably lead to lower employee morale and higher employee turnover, thereby increasing the knowledge gap within the corporation.
C Having a compliance program posted on the corporation's intranet site is sufficient to protect the corporation and its directors from breaches of legislation by employees.
D A breach of legislation will likely lead to an investigation by the regulatory bodies, and such activities will divert resources away from the entity's profit-making objective.

(EG ID 4.6)

Question 4.7

If a supplier induces or insists on the minimum price at which a reseller should sell or advertise the supplier's products, this is referred to as

A price-fixing.
B exclusive dealing.
C unconscionable conduct.
D resale price maintenance.

(EG ID 4.7)

Question 4.8

In Australia, in common with most countries, which of the following are specifically required by law to become a company director?

Select which **two** options are correct.

A to be fully certified as a company director
B to be a natural person of at least 18 years of age
C to have specific qualifications in appropriate business disciplines
D to be a person not currently disqualified from managing a corporation

(EG ID 4.8)

Question 4.9

Disqualification of a director or an officer of a company in Australia, in common with most countries, occurs because of some legally defined commercially unacceptable behaviour or relevant legal wrongdoing. Which of the following are specific wrongs leading to disqualification?

Select which **three** options are correct.

A financial market misconduct
B responsibility for multiple insolvencies
C exercising business judgment that leads to very substantial losses for the firm
D civil and criminal wrongs in relation to anti-competitive conduct in markets for goods and services

(EG ID 4.9)

Question 4.10

When shareholders are dissatisfied with the remuneration packages proposed for a company's executives, they can move to 'spill the board'.

In this process, which **two** of the following statements are correct?

A It enables a clean sweep of the existing board.
B It increases the power of independent shareholders.
C It requires a minimum of 25 per cent of eligible shareholders to vote against the remuneration report.
D It requires a minimum of 25 per cent of eligible shareholders to vote in favour of the resolution to spill.

(EG ID 4.10)

Question 4.11

Various arguments are forwarded for increasing the proportion of women on boards, from equal opportunity to increasing the diversity of perspectives, knowledge and backgrounds to increasing share value, as noted in the Credit Suisse report.

Which **one** of the four countries below is **most** likely to see the greatest board gender diversity?

A France
B Australia
C Malaysia
D the United Kingdom

(EG ID 4.11)

Module 5

Question 5.1

Which of the following are correct in respect of the Global Compact?

Select which **three** options are correct.

A The Global Compact seeks to encourage the integration of its principles into responsible business practice.
B The Global Compact focuses on the international protection of human rights.
C The Global Compact exists to limit the private sector in the management of the risks and opportunities in the environmental, social and governance realms.
D The principles within the Global Compact are based, in part, on the International Labour Organization's 'Declaration on Fundamental Principles and Rights at Work'.

(EG ID 5.1)

Question 5.2

Which **one** of the following is **not** correct in relation to organisational legitimacy?

A Organisational legitimacy draws on the idea of a social contract.
B Organisational legitimacy may be utilised to manipulate public perceptions of an organisation.
C Organisational legitimacy afford organisations a clean slate to pursue their fiduciary duty to shareholders.
D Organisational legitimacy suggests that the survival and growth of corporations is dependent on the delivery of socially desirable ends.

(EG ID 5.2)

Question 5.3

Which **one** of the following describes the theory that organisations will take action to manage perceptions in order to maintain their position and benefits?

A ethical theory
B normative theory
C legitimacy theory
D stakeholder theory

(EG ID 5.3)

Question 5.4

Which **one** of the following courses of action by organisations is **not** considered relevant by Lindblom (1994) to obtain, maintain or repair legitimacy?

A manipulate perception by deflecting attention from the issue of concern
B change the perceptions of the public, but not the organisation's actual behaviour
C educate and inform the public about actual changes to the organisation's behaviour
D change the internal expectations of its performance, as management usually has unreasonable expectations

(EG ID 5.4)

Question 5.5

Which of the following refer to the practice of corporate accountability?

Select which **three** options are correct.

A It is driven by regulation.
B It involves reports highlighting social and environmental performance.
C It involves informing stakeholders of anything they wish to be informed about.
D It illustrates the importance of an understanding of principles of governance for accountants.

(EG ID 5.5)

Question 5.6

Which **one** of the following applies to social sustainability?

A It is the role of government.
B It is facilitated through increasing globalisation.
C It involves addressing the needs of all relevant existing stakeholders.
D It revolves around resource use in a way that promotes long-term benefits.

(EG ID 5.14)

Question 5.7

The international community has become increasingly concerned with the adverse consequences of climate change and as a result has proposed which of the following initiatives?

Select which **three** options are correct.

A requiring countries to begin reducing emissions
B agreeing to legally binding reductions in greenhouse gases over set periods of time
C determining strictly the specific means by which developed and developing countries achieve their targets
D requiring countries to measure, account for and report their aggregate emissions of greenhouse gases

(EG ID 5.7)

Question 5.8

Corporate accountability is evolving to include wider definitions of the responsibilities and accountabilities of corporations. These new accountabilities are widely acknowledged as which of the following?

Select which **three** options are correct.

A job sustainability
B social sustainability
C economic sustainability
D environmental sustainability

(EG ID 5.8)

Question 5.9

The World Business Council for Sustainable Development (WBCSD) has emphasised that environmental issues have an impact on a company's profitability, for example, through which of the following?

Select which **three** options are correct.

A the additional costs associated with going green
B plant write-offs as a result of changes to clean production capacity
C clean-up costs or fines for non-compliance with environmental regulations
D revenue effects of market growth or decline due to changes in customer preferences for environmentally sustainable products

(EG ID 5.9)

Question 5.10

Reducing risk is an incentive for transparent environmental and social reporting because

A CSR reporting allows users to identify, assess and manage these risks.
B CSR reporting, in itself, is a clear indication a company is alert to the risks.
C once CSR risks are disclosed the company has fulfilled its duty to accountability.
D once the risks have been disclosed it becomes the investor's responsibility to invest in the company recognising the risks involved.

(EG ID 5.10)

Question 5.11

What is an 'externality'?

Select the **one** option that is correct.

A external resources essential for economic activity without which the company could not operate
B anything external to the company that impacts on the company, such as a natural disaster or storm
C external free goods that economic entities may exploit for the generation of wealth at will as they are by definition free
D an impact that an existing entity has on parties that are external to the organisation where such external parties did not agree or take part in the actions causing, or the decisions leading to, the costs or benefit

(EG ID 5.11)

Question 5.12

Reporting for social, environmental and sustainability issues involves which of the following?
Select which **three** options are correct.

A imagination
B monetisation
C quantification
D narrative reporting

(EG ID 5.12)

Question 5.13

Which of the following are among the potential limitations of traditional financial reporting?

Select which **three** options are correct.

A the scope of reporting
B the focus upon the entity
C the emphasis on intangibles
D the focus on short-term results

(EG ID 5.13)

Solutions

Module 1

Question 1.1

Correct answer: A, B and D

The correct answers are Options A, B and D. These are all attributes that are accepted as being necessary to identify a profession, as shown in the list from the study guide reproduced below:

- systematic body of theory and knowledge;
- extensive education process for its members;
- ideal of service to the community;
- high degree of autonomy and independence;
- code of ethics for its members;
- distinctive ethos or culture;
- application of professional judgment; and
- existence of a governing body.

Option C is not an attribute. Remuneration levels may well be superior for those in professions but the existence of superior levels of remuneration is not an attribute of a profession. Achieving high income may be an outcome that some non-professionals achieve but it is in no way an attribute applying only to professions and many professionals do not achieve high incomes.

You can review this topic area in the study guide under the section titled 'What is a profession?'.

Question 1.2

Correct answer: A, C and D

Options A, C and D are correct: they are all identified as components of the service ideal.

Option A is linked to the quote by Willmott (1990), which states that:

> Accounting is perceived to present information in a reliable and comparable form by quantifying and reporting the basic facts of economic life, thereby monitoring past performance and facilitating rational, efficient decision making in respect of the generation and allocation of resources.
>
> In performing this role, accounting is widely understood to serve the public interest (Willmott 1990, p. 315).

Option C is linked to the idea that individual accountants are responsible for maintaining and updating their knowledge and skills, and applying them with competence and due care in the best interest of society.

Option D is linked to the notion that members of a profession are expected to behave ethically and for the best interest of society.

Option B is incorrect. One perspective of the 'service ideal' is to provide accounting-related community services 'free' of charge. However, this is not the same as providing services as cheaply as possible. While this may at first appear generous and benevolent, it may not be sustainable and eventually force cost-cutting that could adversely affect the provision of due care.

You can review this topic area in the study guide under the section titled 'An ideal of service to the community'.

Question 1.3

Correct answer: A

The correct answer is Option A. Accounting policies will influence how information is recorded, reported and analysed. This in turn will affect important and significant decisions about resource allocation by a variety of stakeholders including investors, governments, lenders and managers. As such, the way we use and implement accounting influence how societies behave.

Option B is incorrect. While accounting may respond to change based on needs of society, it also plays a role in shaping society.

Option C is incorrect. Accounting has an underlying ethical framework that properly permits accounting to be involved in social change. Accountants, as professionals, are not 'just interested in making money' but have a broader responsibility to serve the public interest.

Option D is incorrect. While accountants are often expected to act in an impartial and objective manner, accounting itself is not purely a technical activity. As a result of accounting information, decisions are made—by investors, governments, managers and other stakeholders—and significant social consequences result. Therefore, accounting is more than just its technical characteristics. It must be understood within the social framework and we must recognise and understand the social changes that accounting will effect.

You can review this topic area in the study guide under the section titled 'Social impact of accounting'.

Question 1.4

Correct answer: B

The correct answer is Option B. This description of professional judgment is provided in the materials and attributed to Becker (1982).

Option A is incorrect. Becker (1982) states that acquisition of knowledge is important but not enough to identify a person as a professional, who also needs to be able to diagnose and solve complex problems.

Option C is incorrect. Practical experience is identified as being important in both professional and non-professional environments, so this is not seen as a distinguishing characteristic.

Option D is incorrect. Problem-solving is important, but professional judgment is more than applying technical solutions, and involves being able to identify value conflict in relation to complex social values that can regularly apply to decisions. Professionals are expected to choose the outcome that best meets the social ideal.

You can review this topic area in the study guide under the section titled 'Application of professional judgment'.

Question 1.5

Correct answer: B

Examples of increased regulation and greater scrutiny are shown by changes to laws such as Sarbanes–Oxley Act 2002 in the US, and CLERP 9 Act in Australia. Accounting standards are now backed by law, and auditors must apply the code of ethics as it has legislative application.

Option A is incorrect. The profession's autonomy will be decreased (not increased) as higher levels of external regulation are put in place.

Option C is incorrect. The community will have less faith (not more faith) in the accounting profession as a result of these issues.

Option D is incorrect. While the number of large accounting firms decreased in the early 2000s from five to four, Arthur Andersen collapsed in the wake of its own scandal arising from the Enron affair. It did not merge with any other accounting firm.

You can review this topic area in the study guide under the section titled 'Credibility of the profession'.

Question 1.6

Correct answer: A, C and D

The correct answer is Options A, C and D. The key reason that remuneration practices are being queried strongly following the GFC is because executives were taking huge risks that they did not understand (and boards were not correcting this) in order to gain inflated bonuses—which is greed just as much as frauds in cases like Enron (Options A and D). The credibility of the accounting profession was also called into question (Option C).

Option B is incorrect because the corporate collapses in the early 2000s and those that occurred during the GFC did involve highly evident levels of greed—including substantial frauds in the early 2000s.

You can review this topic area in the study guide under the section titled 'Credibility of the profession'.

Question 1.7

Correct answer: A, C and D

The correct answers are Options A, C and D: all describe attributes of a profession. Professions serve society, provide a service through a regulatory process, and have a substantial degree of independence and autonomy.

Option B is incorrect. While some professions may be strictly regulated by external bodies, this is not the case with all professions. The accounting profession is not strictly regulated by an external body, since this would place undue constraints upon the exercise of professional judgment. However, the profession has moved from self-regulation to co-regulation with external bodies.

You can review this topic area in the study guide under the section titled 'What is a profession?'.

Question 1.8

Correct answer: B, C and D

Options B, C and D are correct because accounting involves specialist skills, a service ideal and judgment.

Option A is incorrect because accounting does not pursue the best outcomes for the client in all circumstances, as this might not be in accordance with regulation or law, or the public interest.

You can review this topic area in the study guide under the section titled 'Attributes of the accounting profession'.

Question 1.9

Correct answer: A, B and D

Options A, B and D are all correct because creating information systems, managing costs and managing risks are all parts of the role of the accountant in a mid-sized business.

Option C is incorrect because external investment of the capital of the business is a role associated with the CEO, CFO and Board of directors.

You can review this topic area in the study guide under the section titled 'Accounting in small and medium enterprises (SMEs)'.

Question 1.10

Correct answer: A, B and D

Options A, B and D are correct as they are all part of the PAIB's definition of the accountants' role.

Option C is incorrect because, over time, 'creative accounting' has become synonymous with distortion of the company accounts in the interest of concealing rather than revealing problems.

You can review this topic area in the study guide under the section titled 'Accounting in small and medium enterprises (SMEs)'.

Question 1.11

Correct answer: A
The correct answer is Option A. As specified in the module, 'The complainant should first attempt to resolve the matter directly with the CPA Australia member'—in this case Elizabeth.

Option B is not correct as a CPA's primary duty is to the public, not to their employer, as specified in the module:

> Accounting information is relied on heavily by people who make significant decisions about the allocation of resources. Accountants, therefore, serve the public interest by creating and distributing information that conveys a clear and accurate picture of an entity's financial performance, financial position and other relevant issues.

The public duty of CPAs is further discussed in Module 2.

Option C is incorrect, because John should attempt to resolve the matter with Elizabeth first as discussed under Option A. Furthermore, John suspects managerial influence may be responsible in part for the inflated evaluation. The auditor's independence should be maintained.

Option D is incorrect. While John's duty is to report Elizabeth's behaviour to the MPC of CPA, this is only after the initial required attempt to resolve the matter with Elizabeth himself. If her response is not satisfactory he 'must lodge a written complaint providing all necessary details, supported by documentary evidence'.

You can review this topic area in the study guide under the sections titled 'Accountants as members of a profession'—'Public interest or self-interest?' and 'The profession's regulatory process'—'Professional discipline'—'Regulation of member conduct'.

Module 2

Question 2.1

Correct answer: A

Answer A is correct. There is no prohibition on detailing your qualifications.

Generally, members in public practice are permitted to advertise or obtain publicity for their services provided that the content or nature of such advertising or publicity is not false, misleading or deceptive, and does not in any other way reflect adversely on the profession.

Options B, C and D are incorrect. These practices are examples of unsubstantiated claims, or false, misleading or deceptive advertising or making disparaging remarks about members of the profession.

Members must be honest and truthful and should not:
- make exaggerated claims for services offered, qualifications possessed or experience gained; or
- make disparaging references or unsubstantiated comparisons to the work of another (s. 250.2).

You can review this topic area in Module 2 in the section titled 'Marketing professional services (s. 250)'.

Question 2.2

Correct answer: C

Option C is correct and not identified as a relevant reason for communicating with the former accountants.

Options A, B and D are incorrect because they are all discussed as relevant reasons for communicating with the former accountant as follows:

It has long been considered a matter of etiquette for a proposed successor to communicate with his or her predecessor before accepting a professional assignment. Solicitation occurs when a member takes another accountant's client without first informing the former accountant.

Therefore, communication with the former accountant serves as an effective safeguard to avoid the appearance of solicitation. Communication also provides the proposed successor accountant with the opportunity to ascertain whether there are professional reasons why the appointment should not be accepted.

You can review this topic area in Module 2 in the section titled 'Professional appointment (s. 210)'.

Question 2.3

Correct answer: A

The correct answer is Option A.

The APESB code (s. 110.1) defines integrity as follows:

> The principle of integrity imposes an obligation on all Members to be straightforward and honest in all professional and business relationships. Integrity also implies fair dealing and truthfulness.

The study guide also points out that integrity requires strength of character and the courage to pursue one's convictions, otherwise good intentions may not be sufficient.

In short, integrity includes honesty and the courage to pursue one's good convictions.

Option B is incorrect as it refers to the ability to remain impartial, independent, without bias, and free from conflicts of interest. While objectivity is linked to honesty and being true, courage of convictions is more closely linked to integrity.

Option C is incorrect as it refers to the ability to not disclose information.

Option D is incorrect as this refers to ability and diligence rather than honesty, truthfulness and courage.

You can review this topic area in Module 2 in the section titled 'Integrity (s. 110)'.

Question 2.4

Correct answer: A

The correct answer is Option A. People will seek easily understood decision-making rules. That is, they develop heuristic approaches to decision-making. Heuristics simply means dealing with problems by using decision rules or using 'rules of thumb' (a broadly accurate guide or principle, based on practice rather than theory—similar to using your thumb to measure something rather than a specific measuring tool). Decision rules are a convenient way of reducing the number of alternatives that must be evaluated. A heuristic approach to decision-making is one that simplifies the process by establishing easy-to-follow rules of thumb.

Option B is incorrect because compliance with an ethical code is based on a structured conceptual framework approach that identifies threats to fundamental principles and then uses safeguards to reduce those threats to an acceptable level.

Option C is incorrect because the application of an ethical decision-making model is a way of avoiding the 'satisficing' that occurs when decision rules, or rules of thumb, are used. The problem with satisficing is that it is limited to the individual's background, previous experience, memory, knowledge and perceptions. Ethical decision-making models provide a more systematic approach to problem resolution.

Option D is incorrect because a deontological approach is a specific framework from which to evaluate an ethical decision based on intentions rather than a 'rule of thumb', which is less structured or considered.

You can review this topic area in Module 2 in the section titled 'Ethical decision-making models'.

Question 2.5

Correct answer: B

The correct answer is Option B. In cases where the accountant has obligations to more than one stakeholder, the question arises as to whom the accountant owes their primary loyalty. The accountant's primary duty is not to the client or the employer, but to the public. Therefore, the emphasis of the public interest extends to those beyond the needs of an individual client or employer. In public practice, it is tempting to assume that the accountant–client relationship is central to the function of accounting. In this view, no-one else matters but the client. Similarly, in the accountant–employer relationship, it may be presumed that accountants owe their primary loyalty to their employers. Both views are not correct.

Option A is incorrect. As stated above, the client or employer may appear to look like the central focus, but they are not.

Option C is incorrect. A professional must focus on the public interest, which may require ignoring self-interest.

Option D is incorrect. The primary responsibility is to the public, not the government.

You can review this topic area in Module 2 in the section titled 'The public interest—Ethics in practice'.

Question 2.6

Correct answer: D

The correct answer is Option D. The duty of confidentiality does not end with the termination of the professional–client or professional–employer relationship. The duty continues even after such relationships have been terminated (s. 140.6). Generally, the duty of confidentiality is relieved only when disclosure is required by law, or there is a professional duty or right to disclose.

Option A, B and C are incorrect because they are not breaches of confidentiality as they are identified in section 140.7. Options A and C are linked to 140.7 (a). Option B is linked to 140.7(c)(ii).

The following are the circumstances listed in s. 140.7 in which disclosure of confidential information may be appropriate:

a. Disclosure is permitted by law and is authorised by the client or the employer;
b. Disclosure is required by law, for example:
    i. Production of documents or other provision of evidence in the course of legal proceedings; or
    ii. Disclosure to the appropriate public authorities of infringements of the law that come to light; and
c. There is a professional duty or right to disclose, when not prohibited by law:
    i. To comply with the quality review of a member body or professional body;
    ii. To respond to an inquiry or investigation by a member body or regulatory body;
    iii. To protect the professional interests of a member in legal proceedings; or
    iv. To comply with technical standards and ethics requirements.

Under AUST140.7.1, members considering disclosing confidential information without consent are advised to first obtain legal advice.

You can review this topic area in Module 2 in the section titled 'Confidentiality (s. 140)'.

Question 2.7

Correct answer: A, C and D

The correct answer is Options, A, C and D. The three principles—integrity, professional behaviour, and professional competence and due care—are fundamental principles of the Code of Ethics for Professional Accountants. The public interest, although pivotal to understanding the Code, is not listed in the Code as a fundamental principle. The Code of Ethics identifies the following in section 100.5.

Fundamental Principles

100.5 A Member shall comply with the following fundamental principles:

a. Integrity—to be straightforward and honest in all professional and business relationships.
b. Objectivity—to not allow bias, conflict of interest or undue influence of others to override professional or business judgments.
c. Professional competence and due care—to maintain professional knowledge and skill at the level required to ensure that a client or employer receives competent Professional Services based on current developments in practice, legislation and techniques and act diligently and in accordance with applicable technical and professional standards.
d. Confidentiality—to respect the confidentiality of information acquired as a result of professional and business relationships and, therefore, not disclose any such information to third parties without proper and specific authority, unless there is a legal or professional right or duty to disclose, nor use the information for the personal advantage of the Member or third parties.
e. Professional behaviour—to comply with relevant laws and regulations and avoid any action that discredits the profession.

You can review this topic area in Module 2 in the section titled 'Part A of the Code—General application of the Code'.

Question 2.8

Correct answer: C

The correct answer is Option C. When the offer of a gift or hospitality is considered insignificant and not intended to encourage unethical behaviour, and is made in an open manner, the accountant may conclude that the offer is made in the normal course of public relations without the specific intent to influence decision-making or to obtain information. In such cases, an accountant may decide that any threat to compliance with the fundamental principles is at an acceptable level and they may accept the offer (s. 260.2).

Option A is incorrect. A gift that is too personal or expensive may be perceived as a bribe. If the gift is significant, it is the opposite of what is stated as being acceptable (i.e. when the gift or hospitality is insignificant).

Option B is incorrect. Offers of inducements, particularly those that appeal to friendship or loyalty, may unduly influence actions or decisions, encourage illegal or dishonest behaviour, or may be made in order to obtain confidential information.

Option D is incorrect. Members under pressure from within the employing organisation, such as from a superior, may be expected to offer inducements to subordinate the judgment of another individual or organisation, influence a decision-making process or obtain confidential information (s. 350.5). There are no safeguards that can mitigate such threats to an acceptable level, so the member should not offer an inducement to improperly influence the professional judgment of a third party (s. 350.7).

You can review this topic area in Module 2 in the sections titled 'Gifts and hospitality (s. 260)' and 'Inducements (s. 350)'.

Question 2.9

Correct answer: D

The correct answer is Option D. Section 100.12 describes an intimidation threat:

> e. Intimidation threat—the threat that a Member will be deterred from acting objectively because of actual or perceived pressures, including attempts to exercise undue influence over the Member.

Table 2.4 'Examples of threats—Accountants in business' provides this statement as an example of an intimidation threat. This is linked to section 300.12 in the Code of Ethics, which states that:

> Examples of circumstances that may create intimidation threats for a Member in Business include:
>
> - A dominant personality attempting to influence the decision making process, for example with regard to the awarding of contracts or the application of an accounting principle.

Options A, B and C are incorrect. Although other types of threats may also arise in this situation, the type directly linked to this example is intimidation rather than self-interest, advocacy or familiarity.

You can review this topic area in Module 2 in the section titled 'Threats (s. 100.12)', specifically Table 2.4 'Examples of threats—accountants in public practice and business'.

Question 2.10

Correct answer: D

The correct answer is Option D. According to the utilitarian (or utility) principle, determining good from bad, or right from wrong, depends upon whether an act or decision produces the greatest benefit for the greatest number of people. The utilitarian approach to moral judgment and problem-solving is a relatively straightforward process that relies on five basic steps:

1. Identify and articulate the ethical problem(s).
2. Identify all available courses of action that will resolve the situation.
3. Determine the foreseeable costs and benefits (short and long term) associated with each option.
4. Compare and weigh the ratio of good and bad outcomes associated with each option.
5. Select the option that will produce the greatest benefit for the greatest number of people.

Option A is incorrect. Utilitarianism is a teleological theory that focuses on consequences, whereas deontological theories focus on intentions.

Option B is incorrect. It describes egoism, where the focus is on oneself, rather than the greatest number of people.

Option C is incorrect. Utilitarianism is a separate teleological theory that focuses on the greatest number of people; it is not a version of egoism, which considers consequences to one's self.

You can review this topic area in Module 2 in the section titled 'Teleological theories (consequential)'.

Question 2.11

Correct answer: D

The correct answer is Option D. Top-tier management is considered the most influential factor in setting organisational values, which in turn determines the culture that influences members' behaviour. Generally, the more ethical the culture of an organisation, the more ethical employee behaviour is likely to be. While the ethical culture of an organisation might be formally expressed in the form of written policies and a code of ethics, its effectiveness is subject to the actions of management. Leadership is so influential that unethical behaviour from management will render the code ineffective. Therefore, the code of ethics is more likely to be effective when management behaviour is congruent with the principles of the code.

Option A is incorrect. Leadership should reflect the values of the organisation, rather than personal values (although it is desirable that these values are aligned). One purpose of a code of ethics is for creating a system of managing values. It is a major step in resolving any conflicts between an employee's personal values and expected ethical approaches in undertaking the business of the organisation.

Option B is incorrect. An unwritten code of ethics is less likely to be effective than a clearly written code that is clearly linked to senior management actions.

Option C is incorrect because having prescriptive and explicit rules by themselves, without management acting in a similar manner, will only have a limited effect on employees.

You can review this topic area in Module 2 in the section titled 'Factors influencing decision-making'.

Question 2.12

Correct answer: B

The correct answer is Option B. Integrity, objectivity and independence are interdependent principles, with independence considered a subset of the first two. Where independence was once a separate fundamental principle of professional conduct, it has now been transformed into a set of detailed and technical rules (contained in ss. 290 and 291 of the Code) that support the principles of integrity and objectivity. This is not intended to undermine the significance of independence, but rather to highlight its intrinsic relationship with integrity and objectivity.
In sum, independence is equated with an attitude of objectivity (no bias, impartiality) and integrity (honesty).

Options A, C and D are incorrect. Although they describe certain fundamental principles, they are not regarded as the foundations of independence.

You can review this topic area in Module 2 in the section titled 'Independence—Audit, review and other assurance engagements (ss. 290–1)'.

Question 2.13

Correct answer: D

The correct answer is Option D. Earnings management consists of actions that deliberately increase or decrease current reported earnings in order to achieve a preferred outcome.
The management of a company may, for example, favour the adoption of earnings management practices in order to mislead shareholders about the underlying economic performance of the company or to influence contractual outcomes that depend on reported accounting numbers.

The remaining options are only partially correct, as they are vague statements that may be true only in particular circumstances.

Option A is incorrect as it may occur in all circumstances. Earnings management may also occur when profit is high to smooth-out earnings over time.

Option B is incorrect as it usually involves ignoring professional judgment, and using methods and approaches that achieve the desired outcome, rather than the appropriate outcome.

Option C is incorrect because maximising earnings is generally an appropriate action. Earnings management does not always involve maximising earnings; it may also involve reducing earnings to a desired level. It involves achieving outcomes through inappropriate action.

You can review this topic area in Module 2 in the section titled 'Preparation and reporting of information (s. 320)'.

Module 3

Question 3.1

Correct answer: A, B and D

Options A, B and D are all described in the study guide as key factors driving the need for better corporate governance.

Option C is incorrect because higher taxation is a government initiative, not the result of company actions or performance.

You can review this topic area in the study guide under the section titled 'Global push for improved governance'.

Question 3.2

Correct answer: C

The correct answer is Option C managing the day-to-day operations of the corporation.
In *AWA Ltd v. Daniels* (1992) 10 ACLC 933, Rogers CJ concluded that the role of the board in modern companies is to set policy and organisational objectives (performance) and then ensure that adequate controls and review procedures are in place (conformance) to ensure effective implementation by management (performance).

However, Rogers CJ observed that the board is not in place to actually run the business itself. That part of the governance process is delegated to the CEO, although the board must remain informed and is responsible for taking timely action where fundamental CEO failures arise. Rogers CJ stated:

> The board of a large public corporation cannot manage the corporation's day-to-day business. That function must by business necessity be left to the corporation's executives. If the director of a large public corporation were to be immersed in the details of day-to-day operations, the director would be incapable of taking more abstract, important decisions at board level (© State of New South Wales through the Department of Justice, p. 1013).

Options A, B and D are incorrect because they all refer to roles that should be performed by the board.

You can review this topic area in the study guide under the section titled 'Components of corporate governance'—'The board'.

Question 3.3

Correct answer: A

The correct answer is Option A. The effectiveness of the board, and particularly of non-executive directors, is likely to be enhanced by the establishment of appropriate subcommittees of the board, usually simply referred to as 'committees'. These committees enable the distribution of workload to allow a more detailed consideration to be given to important matters, such as executive remuneration and external financial reporting.

Option B is incorrect because committees report to the overall board, not directly to shareholders.

Option C is incorrect because these committees do not reduce the responsibility of the board as a whole and care needs to be taken to ensure that all those concerned understand their functions. It is important to note that normally the board of directors is still responsible for decisions made by the committees.

Option D is incorrect because an independent committee may be beneficial, but this is not the sole purpose of setting up a committee. A committee will focus on a particular area such as audit or remuneration.

You can review this topic area in the study guide under the section titled 'Committees of the board'.

Question 3.4

Correct answer: D

The correct answer is Option D. Milton Friedman was of the view that 'there is one and only one social responsibility of business—to use its resources and engage in activities designed to increase its profits so long as it engages in open and free competition without deception or fraud'.

Options A, B and C are incorrect. They do not correctly describe Milton Friedman's view, as described above.

You can review this topic area in the study guide under the section titled 'Regulators'.

Question 3.5

Correct answer: C

The correct answer is Option C. The OECD in its Principles on Corporate Governance has concentrated on the duties of the board to the shareholders and stakeholders. The OECD Principles specify six core principles and the second focuses specifically on the rights of shareholders.

1. Ensuring the basis for an effective corporate governance framework;
2. The rights and equitable treatment of shareholders and key ownership functions;
3. Institutional investors, stock markets, and other intermediaries;
4. The role of stakeholders in corporate governance;
5. Disclosure and transparency; and
6. The responsibilities of the board.

Options A, B and D are incorrect. None of these items are identified in the six core principles above.

You can review this topic area in the study guide under the section titled 'OECD Principles of Corporate Governance'.

Question 3.6

Correct answer: C and D

Options C and D are correct. The California Public Employees' Retirement System (CalPERS) is an extremely large institutional investor that invests the pension funds for many people (over 1.6 million) in the state of California. This quote describes their philosophy on corporate governance.

> We believe good corporate governance leads to better performance. We seek corporate reform to protect our investments. The corporate governance team challenges companies and the status quo—we vote our proxies, we work closely with regulatory agencies to strengthen our financial markets, and we invest with partners that use corporate governance strategies to earn value for our fund by turning around ailing companies (CalPERS 2011).

CalPERS has been a prominent voice and has clearly stated its position on corporate governance. It considers better corporate governance by profit earning corporations as a way of attaining better value from the companies in which it and other shareholders invest. It does so by using disclosure at public and private levels to achieve results for its beneficiaries.

Options A and B are incorrect. CalPERS does not request its members not to invest in shares, it also doesn't state that it assists companies to appoint directors.

You can review this topic area in the study guide under the section titled 'Institutional shareholders'.

Question 3.7

Correct answer: B, C and D

Option B is correct because the market-based system of corporate governance involves numerous, independent investors requiring sufficient reliable information flow for informed decision making.

Option C is correct because regulation in a market-based system of corporate governance is intended to ensure that information is equally dispersed between all shareholders and not concentrated within privileged groups.

Option D is correct because equity finance is considered important for developing companies. Bank finance is less central, because it tends to be short term and maintains arm's-length relationships with corporate clients (Nestor & Thompson 2000, p. 7).

Option A is incorrect. Debt finance is not the main source of finance. Rather it comes from shareholders who typically contribute capital in the form of equity—and equity finance is the most important long-term financing mechanism in market-based (outsider) systems.

You can review this topic area in the study guide under the section titled 'Market-based systems'.

Question 3.8

Correct answer: A, C and D

Option A is correct because as distinct from the Anglo-Saxon systems of corporate governance found in the United Kingdom and United States that emphasise competition, systems in France and Italy emphasise consensus and cooperation.

Options C and D are correct because France and Italy are the European countries with the smallest ownership of company shares by financial institutions. The majority of shares have traditionally been owned by non-financial enterprises, which reflects an elaborate structure of cross and circular ownership. That is, companies own one another's shares in a circular relationship. No external party can readily gain entry to the network, or seize control of any entity in the network, and all of the member companies support one another against outsiders.

Another distinguishing feature of France is the concentration of ownership, which is higher than in any other Group of Seven (G7) industrialised country with the exception of Italy. In France, half the firms are controlled by a single investor who owns the absolute majority of capital.

Option B is incorrect. While the *président directeur général* (PDG) position does combine the role of CEO and chair, they are strongly independent and hence their accountability to the board is limited. In particular, the role of boards' non-executive directors is muted, and business tends to be dominated by the PDG.

You can review this topic area in the study guide under the section titled 'Relationship-based systems—European approaches'.

Question 3.9

Correct answer: B, C and D

Options B, C and D are correct. In the past, the boards of directors of companies in Asia have often served little more than a nominal role. The role of non-executive directors has frequently been relatively unimportant and consequently boards have not always exercised strong control over executives (including executive directors) and the relationships that exist between the corporation and third parties.

Boards have been (and often still are) effectively dominated by majority shareholders. A result is that disclosure and transparency are often minimal, making it more difficult for investors and regulatory authorities to have adequate knowledge about corporate activities. Furthermore, in the past, institutional shareholders and fund managers have not been significant in Asian markets, so the extent of external monitoring by powerful institutions is only recently becoming a powerful force for better corporate governance.

Option A is incorrect because institutional investors are relatively weaker in East Asia, and they are not yet exerting significant influence over standards of corporate governance—although with rapid growth in Asia, this is beginning to change. For example, there is rapid growth in pension funds in some Asian countries, which will have an impact. Further, increasing direct foreign investment by offshore pension funds and their like will undoubtedly also create a pressure for change.

You can review this topic area in the study guide under the section titled 'Relationship-based systems—Asian approaches'.

Question 3.10

Correct answer: A

The correct answer is Option A. The pattern of business networks is a dominant part of corporate governance in East Asia.

It probably needs to become relatively less important in the interests of improved governance, according to principles such as those of the OECD. Arguably, it is the interests of minority shareholders, which require greater representation in corporate decision-making.

Options B, C and D are all incorrect as they are identified as important objectives for developing more robust governance systems as outlined in the study materials as follows.

The reform process will take different paths in different countries, but the main principles and objectives can be outlined as:

- ensuring clear and effective financial control structures within firms;
- developing external monitoring and control, with improvements in the legal framework, regulatory agencies and disclosure environment; and
- advancing training and development programs to encourage the understanding of corporate governance procedures and issues.

You can review this topic area in the study guide under the section titled 'Relationship-based systems—Asian approaches'.

Question 3.11

Correct answer: C

The correct answer is Option C. It is correct that agents who are highly bonded will be expected to try to maximise the returns for their principal. The objective in choosing highly bonded agents is to find people who show an affinity with the goals of the principal and a willingness and the professional skills to succeed in achieving the goals of the principal. It is nonetheless expected that a highly bonded agent will also seek returns for themselves. Ideally, where (remuneration-policy-based) incentives encourage agents to seek their own rewards, they will also achieve rewards for the principal.

Option A is incorrect because an agent will find it relatively difficult, rather than relatively easy, to achieve the best interests of the principal in most agency relationships. It is accepted that many agents will act in their own interests—meaning that agents will also tend to act for themselves when acting for the principal. Further, even where an agent is highly bonded (to the principal and the principal's goals) by having assumed substantial costs in the form of personal bonding costs, that agent may find it difficult to understand clearly the principal's goals and mode of operations.

Although such highly bonded agents may do their very best to act for the principal, as a result of their incorrect insights or judgment, they may not necessarily achieve outcomes the principal would have wanted to achieve for themselves.

Option B is incorrect. The proposition that it is necessary to monitor an agent extensively, even where that agent voluntarily assumes the imposition of high bonding costs, is incorrect. Monitoring will probably always be necessary so that any residual losses are identified (as far as possible) and can then be explored with a view to minimising their future impact. However, where an agent is highly bonded, then the risk that the agent may engage in 'self-seeking' behaviour will be smaller.

This diminishes the risk of residual loss and should be reflected in the principal having less need to engage in extensive monitoring (and having lower monitoring costs). It is partly for this reason that highly bonded agents may receive increased remuneration (remuneration not being an agency cost but part of the contract or payment framework that creates an agency).

Option D is incorrect. It is not correct to say that it is principally signalling failures that result in principals finding it necessary to engage in and pay for monitoring. The risk that this may occur is one factor (hence, the need for auditing of signals) but there are other more fundamental reasons.

Principals want to know whether agents are achieving the outcomes they require and which the principals (in theory) could achieve themselves. Agency theory assumes that agents (especially poorly bonded agents) will act in their own interest. A principal who is not close to the agent will demand monitoring in order to be informed about the performance of the agent—allowing good understanding of poor performance by agents and the reasons for this poor performance.

You can review this topic area in the study guide under the section titled 'Agency theory'.

Question 3.12

Correct answer: B

The correct answer is Option B. Dividends are not defined as a cost of the agency relationship. They are the cash return to shareholders for their investment. They may be affected by the level of agency costs—that is, the level of profits available to shareholders may be reduced by the addition of audit fees (a monitoring cost), management laziness (a residual loss item) and expenditure authorisations that would be classed as monitoring cost by the principals.

Options A, C and D are incorrect as they are all examples of agency costs.

You can review this topic area in the study guide under the section titled 'Agency issues and costs'.

Question 3.13

Correct answer: A and D

Option A is correct because something that would not enhance shareholder wealth would be opportunistic residual loss behaviour.

Option D is also correct because it is providing a benefit for the manager (agent), but not for the organisation.

Option B is incorrect because although investing in alternative technological development might cause a reduction in short-term profit, it is justifiable if it makes a significant contribution to long-term returns, which would be in the organisation's best interests.

Option C is incorrect because avoiding the purchase of an organisation that reduces shareholder wealth is in the best interests of both the principal and the agent, and therefore is not opportunistic residual loss behaviour.

You can review this topic area in the study guide under the section titled 'Agency issues and costs'.

Question 3.14

Correct answer: B and C

The correct answer is Options B and C. Options A and D will not be sufficient to result in South Ltd reaching the $50 million target profit level this year. It is, therefore, likely that management will instead attempt options B and C to increase expenses in this year (this is sometimes described as 'taking a bath'), which will decrease expenses next year and so increase the chance of hitting the profit target in the following year.

You can review this topic area in the study guide under the section titled 'Agency theory'.

Question 3.15

Correct answer: D

Option D is the correct answer because stakeholder theory takes into consideration a wider range of groups that can affect, or are affected by, the corporation.

Option A is incorrect as while stakeholder management will recommend a relationship with the corporate regulator, this is only one among many relationships, and stakeholder theory attempts to avoid the problems that regulation addresses by maintaining positive relationships with all stakeholders.

Option B is incorrect as while stakeholder management will recommend a relationship with the directors of the corporation, this is not necessarily privileged over other important stakeholder relationships.

Option C is incorrect. The method of management privileging shareholder interests is the shareholder theory of management, not the stakeholder approach.

You can review this topic area in the study guide under the section titled 'Components of corporate governance'—'Stakeholders'.

Module 4

Question 4.1

Correct answer: B

The correct answer is Option B. It is appropriate for shareholders to vote by proxy (someone votes on their behalf as directed by the shareholder or with the permission of the shareholder) or by attendance at the annual general meetings of the corporation. This is the best way for shareholders to be involved in corporate governance processes.

Option A is incorrect because shareholders in a listed corporation may take an active interest in their shareholding in a number of ways—based on information made available to shareholders. However, this information would not permit a shareholder to take an active role in the management of the corporation. This is exactly as the law provides because shareholders elect a board of directors that manages on their behalf, including through the selection of executives and the delegation of powers to those executives. There would be chaos if every shareholder in a listed corporation could actively manage the company. In small (non-listed) corporations, it is common for shareholders to become involved in management.

Option C is incorrect. In selling their shares, shareholders remove themselves from the organisation and thus remove their capacity to influence the organisation's governance.

Option D is incorrect because shareholders will not normally have any ability to overrule board decisions, as boards make decisions where empowered and normally do not make decisions where shareholders have the right to vote. Where the board is not empowered to decide a matter, then it recommends shareholders should vote in a certain way at general meetings.

If the shareholders do not follow the board's recommendations, this is not to be regarded as the shareholders overruling the board. There is a mechanism by which shareholders can indicate displeasure with the board by way of what is called a non-binding vote. This is most apparent in respect of executive remuneration, where shareholders can voice their dissent regarding the board's decisions on executive salaries. Though such non-binding votes by shareholders indicate dissent, they may not necessarily change the salaries of executives—they could merely demonstrate that the shareholders disagree at that time.

You can review this topic area in the study guide under the section titled 'Representation'.

Question 4.2

Correct answer: C

The correct answer is Option C. A non-executive director who receives a flat fee for being a director and who accepts no additional consulting, advisory or performance-related fees satisfies fully the requirements of independence as seen in the ASX CGC guidelines and in the UK FRC Corporate Governance Code.

Option A is incorrect because a non-executive director who holds 20 per cent of the shares in the corporation has a strong personal interest in the corporation. Independence is not an absolute concept and it is the board's responsibility to determine independence.

Option B is incorrect because an executive director who is a CEO, but who receives no additional remuneration for being on the board, will not be independent. An employee will never be independent from the point of view of shareholders. Such a person has too many ties (including incentive payments) to satisfy any notion of independence.

Option D is incorrect because a person appointed to the board (with initial appointment by the board) at the request of a major lender of a corporation, is one of many circumstances where the person appointed would be termed a 'nominee director'. Note that all director appointments to the board (i.e. made by the board before reference to shareholders) must eventually be approved by a majority shareholder vote. Such a vote will usually be required to take place (as mandated by the company constitution) at the next general meeting held by the company—so if there is no earlier meeting, then this would (at the latest) take place as part of the voting at the next general meeting of the company. Nominee directors, like all directors, are required to act in good faith in the interest of the company as a whole and to use their power as directors for proper purposes in relation to the company as a whole. The legal expression 'company as a whole' means the shareholders of the corporation as a body of persons who own the corporation.

Despite the common legal duty of all directors towards the shareholders as a whole, some directors are considered independent and others are not. The fact that the employee has been told by the employer (the bank) that they should vote in the interests of the shareholders in no way changes the fact that they are on the board as a result of the major commercial interest that exists between the corporation and the bank. The employee's opinion that they are independent is irrelevant. The board (on which they are a director) has the responsibility to determine independence and it is impossible that the employee is independent.

You can review this topic area in the study guide in the solution to Question 4.3, where the role of independent directors on remuneration committees is discussed.

Question 4.3

Correct answer: C

The correct answer is Option C. Mr Smith is potentially liable because he is an 'insider', and is in possession of information that is not generally available, but which, if it were generally available, might have an impact on the market price of securities in the corporation. Mr Smith has also communicated the information to another person, and it is arguable that he knew, or ought reasonably to have known, that Mr Jones would or would be likely to purchase shares in the corporation on the basis of this information. Mr Jones is also an insider because he is in possession of information not generally available to the public and has purchased shares in the corporation.

Options A, B and D are incorrect as both Mr Smith and Mr Jones are potentially liable for insider trading.

You can review this topic area in the study guide under the section titled 'Insider trading'.

Question 4.4

Correct answer: D

Option D is correct because driving a 'hard and tough' bargain is **not** listed as a factor in determining unconscionability.

Options A, B and C are incorrect because they display factors that define unconscionability.

The tests for unconscionable conduct in the case of an ordinary domestic agreement include the following:

- What was the relative strength of the bargaining power of the corporation and the consumer?
- Were the conditions imposed on the consumer reasonably necessary to protect the legitimate interests of the corporation?
- Was the consumer able to understand all of the documents used?
- Was any undue influence or pressure exerted on, or were any unfair tactics used against, the consumer?
- Was the amount paid for the goods or services higher, or were the circumstances under which they could be acquired more onerous, when compared to the terms offered by other suppliers?

Option A fails the fourth test (undue influence), Option B fails the third test (ability to understand) and Option C fails the first test (relative bargaining strength).

You can review this topic area in the study guide under the section titled 'Unconscionable conduct'.

Question 4.5

Correct answer: D

The correct answer is Option D. The fact that the entity is likely to appeal a decision does not necessarily mean that the proceedings are incomplete or insufficiently definite. Further, the information would need to be confidential for the entity to delay disclosure, as it is specified that the information would have a material effect on the price of the securities, violating the third key test for insider trading.

Option A is incorrect as the entity disclosed immediately and the market was therefore informed—minimising any insider trading risks.

Option B is incorrect as the information was not material. If materiality were doubtful, then immediate disclosure would be prudent.

Option C is incorrect as the entity would be permitted to delay disclosure as it is acceptable for properly held confidential information to be kept confidential from the market.

You can review this topic area in the study guide under the section titled 'Insider trading'.

Question 4.6

Correct answer: C

Option C is the correct answer as just having a compliance program is not sufficient. Further, a compliance program should never be seen as just an education or training exercise—it must become part of both an integrated business system and the company's code of conduct.

Options A, B and D are all correct statements about legal compliance programs.

You can review this topic area in the study guide under the section titled 'Legal compliance and governance'.

Question 4.7

Correct answer: D

Option D is correct as resale price maintenance is a vertical arrangement (i.e. between supplier and buyer).

Option A is incorrect because price-fixing is a horizontal arrangement (i.e. between competitors).

Options B and C are incorrect because they do not relate specifically to arrangements between suppliers and resellers.

You can review this topic area in the study guide under the section titled 'Resale price maintenance'.

Question 4.8

Correct answer: B and D

Options B and D are specifically required.

Option A is incorrect because while boards would look for directors with appropriate experience and skills, there are no compulsory certifications required.

Option C is incorrect because while boards would look for directors with appropriate experience and skills, there are no specific educational qualifications.

You can review this topic area in the study guide under the section titled 'Board appointment and cessation'—'Appointment'.

Question 4.9

Correct answer: A, B and D

Options A, B and D make directors liable for disqualification.

Option C is incorrect because if a director exercises informed business judgment that leads to very substantial losses, normally the courts will not seek to hold the director liable for the losses or impose disqualification. The courts accept that business decision-making is complex and takes place in conditions of uncertainty, and if a director has exercised reasonable business judgment at the time this is acceptable behaviour even if the decision proves a wrong one.

You can review this topic area in the study guide under the section titled 'Board appointment and cessation'—'Disqualification'.

Question 4.10

Correct answer: B and C

The correct answer is Options B and C. Twenty-five per cent of eligible shareholders must vote against the remuneration to move for a spill, and this voting process gives greater voting power than usual to independent shareholders as key management personnel (KMPs) are not able to vote and KMPs generally hold a lot of shares.

Option A is incorrect as the managing director and two additional directors must be retained to maintain board continuity.

Option D is incorrect as a successful spill motion requires a minimum of 50 per cent of the eligible shareholders to vote in favour of the resolution, not 25 per cent.

You can review this topic area in the study guide under the section titled 'Board appointment and cessation'—'Two strikes rule–shareholders spill the whole board'.

Question 4.11

Correct answer: A

The correct answer is Option A. Like other European counties that have enacted mandatory minimums, the percentage of women on boards of large companies is around 40 per cent.

Option B is incorrect as Australian reforms have achieved only 20 per cent.

Option C is incorrect. Malaysia has set a 30 per cent target of women board members by 2016, lower than the European mandatory minimums.

Option D is incorrect. While the module does not specify the UK's percentage it is not one of the European countries that have enacted mandatory minimums.

You can review this topic area in the study guide under the section titled 'Diversity—fairness and performance'—'Board diversity'.

Module 5

Question 5.1

Correct answer: A, B and D

Options A, B and D are correct because they have all been identified within the module as being stated on the Global Compact website.

Option C is incorrect because the Global Compact seeks to assist in the management of risks and opportunities in the environmental, social and governance areas, not to limit the private sector from doing this.

You can review this topic area in the study guide under the section titled 'United Nations Global Compact'.

Question 5.2

Correct answer: C

The correct answer is Option C. Organisational legitimacy limits the scope within which an organisation may maximise shareholder returns in accordance with the expectations and requirements of other stakeholders.

Options A, B and D all apply to organisational legitimacy.

You can review this topic area in the study guide under the section titled 'Organisational legitimacy'.

Question 5.3

Correct answer: C

Legitimacy theory suggests that an organisation needs to appear to be legitimate, and will try and convince stakeholders that it is acting with an acceptable level of ethical and moral conviction while pursuing its main objective(s).

Options A, B and D are incorrect as they are more general theories, not specifically about managing perceptions.

You can review this topic area in the study guide under the section titled 'Organisational legitimacy'.

Question 5.4

Correct answer: D

Option D is correct because it refers to changing internal expectations. Lindblom (1994) suggests that organisations seek to obtain, maintain or repair legitimacy by changing the external expectations of their performance—possibly by demonstrating that specific societal expectations are unreasonable, as well as by educating and informing the public, or by deflecting attention from the issues of concern.

Options A, B and C are incorrect because they are all ways of changing external expectations of performance.

You can review this topic area in the study guide under the section titled 'Legitimacy theory'.

Question 5.5

Correct answer: A, B and D

Options A, B, and D are correct because they all relate to the practice of accountability.

Option C is incorrect because while it is right to be as accessible and open with stakeholders as possible, this is not an open-ended obligation to impart sensitive commercial information. Accountability is required in certain defined areas and duties such as in financial reporting and other critical areas where disclosure is required, but this does not cover all business matters where a degree of discretion may be required.

You can review this topic area in the study guide under the section titled 'The evolution of corporate accountability'.

Question 5.6

Correct answer: B

The correct answer is Option B. Increasing globalisation has enabled greater awareness of and hence accountability of organisations, for example as discussed in the study guide with reference to the collapse of the Rana Plaza building in Bangladesh.

Option A is incorrect as social sustainability is increasingly seen as business's responsibility where traditionally it was regarded as government responsibility.

Option C is incorrect as social sustainability regards future stakeholders in addition to existing stakeholders.

Option D is incorrect as social sustainability is a local as well as a global concern.

You can review this topic area in the study guide under the section titled 'Social sustainability'.

Question 5.7

Correct answer: A, B and D

Options A, B and D are all requirements of successive international community initiatives on climate change and reducing emissions.

Option C is incorrect because international agencies have left it to individual developed and developing countries to determine the best means by which to achieve their targets for emissions reductions.

You can review this topic area in the study guide under the section titled 'International initiatives on climate change'.

Question 5.8

Correct answer: B, C and D

Options B, C and D are all correct because environmental, social and economic sustainability are the three pillars of sustainable development.

Option A is incorrect because while economic sustainability does include managing business for the longer term within more stable economic systems, there will inevitably be innovation and change in contemporary business, and jobs for life will continue to become rare, though high employment rates should be feasible.

You can review this topic area in the study guide under the section titled 'Environmental sustainability', 'Social sustainability' and 'Economic sustainability'.

Question 5.9

Correct answer: B, C and D

Options B, C and D are correct because they are all environmental issues that WBCSD has emphasised as having an impact on a company's profitability.

Option A is incorrect because WBCSD makes reference to the costs of non-compliance and of plant write-offs due to emissions controls, but does not make reference to the costs of going green. While there may be further costs involved in exercising environmental responsibility these are often balanced by significant savings from waste reduction and other factors.

You can review this topic area in the study guide under the section titled 'Drivers of increased business accountability'.

Question 5.10

Correct answer: A

Option A is correct because the risks need to be identified, assessed and managed in order for them to be reduced.

Options B and C are incorrect because the commitment is to identify, assess and manage the risk, not to simply disclose the risk and do nothing further.

Option D is incorrect because the commitment is to identify, assess and manage the risk, not to pass the responsibility on to others.

You can review this topic area in the study guide under the section titled 'Risk management incentives'.

Question 5.11

Correct answer: D

Option D is the correct definition of externality as employed in the economic and environmental literature, that is, the impact of the entity on the external environment or parties.

Options A, B and C are incorrect because they imply that the resources and activities are external to the entity or are freely exploitable, rather than impacts on the external environment or parties.

You can review this topic area in the study guide under the section titled 'Externalities and potential for government intervention'.

Question 5.12

Correct answer: B, C, D

Options B, C and D are correct because quantification, monetisation and narrative reporting will all assist in giving a factual basis to reporting.

Option A is incorrect because imagination in this context could lead to exaggeration and false hopes for the company performance in social and environmental sustainability.

You can review this topic area in the study guide under the section titled 'What can be measured and reported?'.

Question 5.13

Correct answer: A, B and D

Options A, B and D are all correct because scope of reporting, focus on the entity and short termism are recognised limitations of traditional financial reporting.

Option C is not correct because financial reporting tends to ignore not emphasise intangibles. In this context an emphasis on intangibles would be a strength not weakness of accounting.

You can review this topic area in the study guide under the section titled 'Limits of traditional reporting'.