### Part (d) Discuss your concerns, from an ethical perspective, with regard to
(i) Ms Pearson’s behaviour in investigating the possibilities in investing in the manufacture of organic fertilizers

Indications of a self-interest threat to the fundamental principles could apply to the following (1 - 11):

1. Ms Pearson is a CA(SA) in business and, as such, she is required to comply with the SAICA Code of Professional Conduct.  
   Marks: 1

2. Ms Pearson shared detailed confidential information about the company which she acquired as a result of her position in the company with outsiders. The information was the most recent internal management accounts. She did not have proper and specific approval of the Board to do so.  
   Marks: 1

3. This may be an indication that this is a self-interest threat to the fundamental principle of confidentiality.  
   Marks: 1

4. Ms Pearson’s behaviour may thus cause harm to the company if the outsiders use the confidential information obtained inappropriately.  
   Marks: 1

5. Ms Pearson’s professional behaviour is questionable – which requires that CAs comply with relevant laws and regulations and not bring the profession in disrepute.  
   Marks: 1

6. Ms Pearson has brought into question her integrity as she previously did not disclose to the Board she was engaging with her brother’s business.  
   Marks: 1

7. Ms Pearson seems to have compromised her sound business judgement because of bias towards her brother. The result may be a conflict of interest because it is Ms Pearson’s brother.  
   Marks: 1

8. This breach may be an indication that Ms Pearson’s actions are not in line with the fundamental principle of objectivity.  
   Marks: 1

9. Ms Pearson appears to have recommended to the Board of Directors that there is not a need to consider an impairment loss with respect to the fertiliser plant. She is responsible for representing facts accurately and completely in all material aspects (CPC 320).  
   Marks: 1

10. There was a significant drop in sales of fertiliser from 2017, Ms Pearson’s advice was incorrect and not in line with financial reporting standards.  
    Marks: 1

11. Ms Pearson incorrectly advising the Board may indicate breach of fundamental principles:
   a) She may be in breach of the principle of integrity as she may have wittingly misled the Board in order to present the financial statements of the company more favourably.  
      Marks: 1

   b) She may be in breach of the principle of professional competence and due care as she may have given the incorrect advice unknowingly due to a lack of professional competence.  
      Marks: 1

   c) She may be in breach of the principle of professional behaviour as she lacked professional competence and still ill advised the Board, her ignorance will discredit the profession. This could contravene section 29 of the Co Act which regards any party preparing or approving AFS knowing them to be materially false or misleading guilty of an offence.  
      Marks: 1

12. Ms Pearson is a director (CEO) and therefore has to adhere to sound governance principles of King III and the ethical values of leadership.  
    Marks: 1

13. Ms Pearson may have shared price sensitive information with third parties and may be in breach of:
   a) JSE listing requirements; and  
      Marks: 1

   b) Financial Markets Act (i.e. insider trading sections)  
      Marks: 1

14. As such she may be acting contrary to the Companies Act:
   • Section 75 – possible directors interest in contract.  
     Marks: 1
   • Section 76 – which requires her to act in good faith and in the best interests of the company.  
     Marks: 1
   • Section 22 – Reckless trading.  
     Marks: 1

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<table>
<thead>
<tr>
<th>Candidate</th>
<th>Marker</th>
<th>(d)(i)</th>
<th>(d)(ii)</th>
<th>(e)</th>
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<tr>
<td></td>
<td></td>
<td>8</td>
<td>8</td>
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**Available [22]**

**Maximum [8]**

**Total for Part (d)(i) [8]**
<table>
<thead>
<tr>
<th></th>
<th>Part (d) (ii) The audit senior’s actions after reviewing the minutes of the directors’ meeting held on 5 January 2017.</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>The audit senior shared <strong>confidential information</strong> he/she obtained as <strong>part of the audit team</strong> with his/her friend at Eating Green.</td>
<td>1</td>
</tr>
</tbody>
</table>
| 2. | The audit senior, as a trainee accountant, must comply with  
  - The SAICA **Code of Professional Conduct (CPC)** for Chartered Accountants; and  
  - The quality control procedures (**ISQC1/ISA220**) that are put in place by the audit firm. | 1     |
| 3. | The audit senior has breached the SAICA CPC with respect to the following:  
  - He/she was in possession of confidential information as a **result of his/her involvement in the audit** of Gas-to-Liquids, which was shared without **proper or specific authority** (140.1)  
  - He/she is **intending to use the information to gain a personal** advantage as he/she shared such information in order to gain recognition by the client or audit manager (140.1).  
  - He/she did not consider whether the person **to whom** the information being disclosed **was appropriate**, such as a friend (140.8). | 1     |
| 4. | By **unilaterally acting** in a manner that aims to secure a compliance certificate from Eating Green, the audit senior has in effect taken on the **role of management** of Gas-to-Liquids. | 1     |
| 5. | The fact that the audit senior is trying to use the information for his/her own recognition is an indication that he/she is not acting with **integrity**. | 1     |
| 6. | **AP Act 46** divulging confidential information could lead to legal liability as this is a negligent act. | 1     |
| 7. | Given the ethical transgressions the audit senior could **place the profession in disrepute**, due to not acting with **professional behaviour**. | 1     |

Maximum [7]  

**Communication skills – appropriate style** | 1     |

| Total for part (d)(ii) [8] |       |
Part (e) Prepare a brief memorandum highlighting the current business risks facing Gas-to-Liquid. Summarise the risks under the following four categories below:

<table>
<thead>
<tr>
<th>MEMORANDUM FORMAT</th>
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<tbody>
<tr>
<td><strong>1</strong> New head office</td>
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<tr>
<td>1.1 A new head office is an <em>unproductive asset</em> and will reduce profitability through <em>increased depreciation and operational costs</em>.</td>
<td>1</td>
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</tbody>
</table>
| 1.2 Given the economic conditions, this extra cost could result in:  
  (a) Undue *pressure/unforeseen cost of move* on the businesses profitability (e.g. liquidity) and result in business with higher than normal risk being accepted to meet targets.: and  
  (b) *Going concern risk*, as company may not be in a position to financially support these capital expenses. | 1 |
| 1.3 The purchase of the property exposes the business to:  
  (a) Increased *market risk* arising from underlying property prices; and  
  (b) Increased *financial risk* depending on how the property was financed, through either increased gearing or reduced liquidity. | 1 |
| 1.4 Head office is located in Midrand which is far from its major operations. There is a risk of *lack of oversight by management* with what is happening on the ground. This may lead to incorrect decision-making, which gives rise to *strategic and/or operational risks*. | 1 |
| 1.5 The move to Midrand could result in the following business continuity risks such as:  
  (a) Loss/damage/unauthorised access to information/equipment;  
  (b) Increased staff turnover due to moving to an inconvenient location;  
  (c) Distracting staff/staff morale during the current circumstances; and | 1 |
| 1.6 Given the economic climate in SA, the acquisition could result in an undesired *perception by stakeholders* (i.e. employees) on the financial status of the company. This may result in *labour disputes* if wages demands are not met. Furthermore, this could result in *reputational risk* if the disputes are not managed properly. | 1 |

**2 Natural gas operations**

Natural gas operations applicable to Mossel Bay and Canada

| 2.1 Highly *specialised* and complex extraction and production processes increasing the *operational risks and/or reducing profitability* due to:  
  (a) Limited availability of *specialised equipment* required to complete the process;  
  (b) Scarcity of highly *skilled resources* needed to complete the process;  
  (c) High costs/penalties/reputational damage in case of *non-compliance with laws and regulations*;  
  (d) High costs/penalties/reputational damage in case of *non-compliance with health and safety regulations*;  
  (e) Exposure to *natural disasters* disrupting/stopping production; and  
  (f) Exploration projects require *substantial capital investment*. | 1 |
| 2.2 Natural gas reserves are *estimated by geologists*, resulting in the risk that reserve levels of natural gas under the sea bed are lower than estimated, *reducing the expected life-time profitability* of the cash-generating unit. | 1 |
| 2.3 The growing *demand* for clean and *environmentally friendly* energy products reduces the market demand for oil and gas products. | 1 |
| 2.4 The increased technological advancements being experienced throughout the exploration, extraction and production processes could *lower the barriers* to entry and operational costs for new entrants and competitors, creating price *pressures on the market and reducing the viability* of the existing operations. | 1 |
| 2.5 Increased risk of *insufficient provisions* for rehabilitation costs, in respect of which there may be uncertainty until the costs are actually incurred. | 1 |
| 2.6 Burning of natural gas results in the release of carbon dioxide, which could lead to global warming and negatively impacting the *carbon footprint*. | 1 |
| 2.7 Disruptions in production arising from *global activists’ protests* could result in lost revenue and reputational damage. | 1 |
**Natural gas operations specific to South Africa**

2.8 SA has a high degree of **labour unrest** in the oil and gas sector which increases the risk of disrupted production and which could in turn impact sales levels.  

2.9 Natural gas prices are **determined by the international markets** and denominated in USD, increasing **market risk** due to foreign exchange movements between the ZAR and USD currency pair and further by the **global supply and demand levels** that drive the natural gas price.  

2.10 Replacement **equipment is sourced from Germany**, increasing the risk of **production delays** resulting in **lost revenue and increasing market risk** relating to the ZAR and € currency pair movements.  

2.11 Given the **location of the operations**, access to its markets could be disrupted where adequate storage and transport capabilities are not available, resulting in lost sales and customer goodwill.  

**3 Fertilizer and explosives operations**

3.1 The volatile nature of the product and reduced demand for fertilizers increase the risk that the business will require **specialised storage/distribution facilities/skilled staff**, and that supply chain disruption could impact sales and increase operating costs.  

3.2 Limited application of products **outside their core markets (agriculture and mining)** increases the risk of redundancy and earnings volatility.  

3.3 **Loss of clients/key client** increases the risk of lower than expected earnings due to lower revenue and high fixed costs arising from depreciation and maintenance costs. If significant this could be a **going concern risk**.  

3.4 An **increased number of new clients** could increase price pressures, and operational complexities and distribution costs could lower profit margins.  

3.5 Going concern risk due to the increase in **activist pressure/increase in demand for more environmentally friendly products**.  

3.6 Due to the nature of products being produced there is a risk of **health and safety hazards** occurring and claims arising as a result thereof together with **reputational risk**.  

3.7 Exposure to **natural disasters or unforeseen events** (flooding/draught/fire etc.) would have a direct impact on profitability (e.g. disruptions in production).  

3.8 Risk on non-compliance with **laws and regulations** impacting profitability due to possibly penalties being levied/reputational risk.  

**4 Canada Liquid Gas operations**

See above “natural gas operations applicable to Mossel Bay and Canada” for business risks applicable to both the Mossel Bay and the Canadian operations. Candidates can obtain marks under either of these categories.  

4.1 Operational profits generated in Canadian dollars could give rise to **market risk** with regard to the ZAR and CAD currency pair movements.  

4.2 The **remoteness of this operation from Midrand office** may result in the management of CLG operating fairly autonomously. This increases the risk that:  

a) Should their **decisions not be sound**, the group will be exposed to sizeable financial losses and other adverse consequences (e.g. reputational risk); and  

b) The **level of oversight by head-office** may be limited, which increases the risk that **fraud** may be perpetrated by the CLG management, also exposing the group to financial losses.  

4.3 Risk of mismanagement as a result of the decisions management are making in respect of the impairment.  

Any other valid point  

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<th>Available [51]</th>
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<tr>
<td>Maximum [20]</td>
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<td>Communication skills – logical argument</td>
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