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LLM in Commercial Law Dissertation Titled

‘Corporate Governance in South Africa: Progress and Challenges’

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CHKAND003

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Plagiarism

Research dissertation presented for the approval of senate in fulfilment of part of the requirements for the degree of Masters in Commercial Law in approved courses and minor dissertation. The other part of the requirements for this qualification was the completion of a programme of courses.

I Hereby Declare that I have read and understood the regulations governing the submission of Master of Laws dissertations, including those relating to length and plagiarism, as contained in the rules of the University and that this dissertation conforms to those regulations.

Signature_____ Date_____

DEDICATION

To my Late Mother Elina Tembo Chakanika

ABSTRACT

Generally, the 1990's have been classified by various jurisdictions as a period that has seen tremendous growth and activity in the area of corporate governance. Corporate governance came in at the right time to provide some form of insulation from the various economic shockwaves suffered in the corporate market thereby ensuring that the newly established economic growth was maintained. It must be noted that corporate governance has continued to register steady growth around the world over the years.

However, this growth has been accompanied by various problems which if left unchecked may lead to breakdowns in the corporate world as will be illustrated by this dissertation.

South Africa is one of the fastest emerging economies of the world and this rapid economic growth has been largely attributed to the adoption of the King codes and the various corporate governance structures. Against this background, this dissertation will begin by discussing the major changes that have been made from the King II report to the King III report.

The driving forces behind this dissertation are contained in chapters three and four as these chapters will seek to ascertain some of the major progresses and challenges that have been scored in the area of corporate governance. Therefore, these problems and developments that will be identified by this dissertation will be compared with those that are being faced by different jurisdictions around the world paying much emphasis to the United Kingdom, United States of America and Asia in an effort to seek clarity as to what is currently happening on the international scene. Furthermore, it will take a critical look at how these countries have fostered growth of corporate governance whilst at the same time looking at how they have dealt with the various challenges.

The concluding part of this paper will give a summarised version of the dissertation and make some recommendations that can help to strengthen South Africa's corporate governance systems and structures into more effective and efficient frameworks.

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Cassandra Musonda, my fiancé, my love words cannot come close to describing how thankful I am for your undying love, support, patience, advice and care which know no season. You are truly heaven sent.

To my Dad, siblings and relatives, words are not enough to show my appreciation you for always believing in me, standing by my side in good times and bad. Your words of encouragement have pushed me to achieve my goals.

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ACRONYMS AND ABBREVIATIONS

AGM	annual general meeting
CEO	chief executive officer
CFO	chief financial officer
CRO	chief risk officer
CSR	corporate social responsibility
EGM	extraordinary general meeting
ESG	environmental, social and governance
EU	European Union
FSB	Federation of Small Businesses
FTSE	Financial Times Stock Market
GAAP	Generally Accepted Accounting Principles
IFRS	International Financial Reporting Standards
IoD	Institute of Directors
IT	Information Technology
OECD	Organisation for Economic Co-operation and Development
SEC	Securities and Exchange Commission
SMEs	small and medium sized enterprises
SOX	Sarbanes-Oxley Act of 2002

TABLE OF CONTENTS

	Page
DEDICATION.....	I
ABSTRACT.....	II
ACKNOWLEDMENT.....	III
ACRONYMS AND ABREVIATIONS.....	IV
CHAPTER 1: STATEMENTS, OBJECTIVES, DEFINATIONS	
AND CHAPTER OUTLINE.....	1
1.0 Introduction.....	1
1.1 Statement of problem.....	2
1.2 Objectives and value.....	3
1.3 Defining Corporate Governance.....	3
1.4 principles of good corporate governance.....	5
1.5 Chapter Outline.....	5
CHAPTER 2: LEGAL BASIS OF CORPORATE GOVERNANCE	
AND COMPLIANCE.....	7
2.0 Introduction.....	7
2.1 Regulatory framework of corporate governance	
In South Africa.....	7
2.1.1 Creation of committees' vis-à-vis corporate	
Governance.....	11
(a) <i>Audit Committee</i>	11
(b) <i>Risk Committee</i>	12
2.1.2 Why is regulation necessary?.....	12

	Page
2.1.3 The role played by the stock market in South Africa.....	13
2.1.4 Codes of best practice.....	14
2.2 Interconnection between corporate governance and the law.....	16
2.3 Conclusion.....	18
CHAPTER 3: EVOLUTION FROM KING II TO KING III:	
DEVELOPMENTS AND GAINS.....	19
3.0 Introduction.....	19
3.1 Case for corporate governance.....	19
3.2 The Salient changes from King II to King III.....	22
3.2.1 Inclusive stakeholder relationships.....	22
3.2.2 Scope of application.....	24
3.2.3 Integrated reporting and disclosure.....	25
3.2.4 Risk Management.....	26
3.2.5 Information Technology.....	27
3.3 Overall progress from King II and beyond.....	28
3.3.1 Legal framework.....	29
3.3.2 Enforcement and strengthening institutional Capacity.....	33
3.3.3 Shareholder rights.....	35
3.3.4 Corporate social responsibility as a Shareholder issue.....	39
3.3.5 Financial Reporting Standards and Disclosure.....	40

	Page
3.3.6 Media and Public involvement in	
Corporate governance.....	42
3.4 Conclusion.....	43
CHAPTER 4: CHALLENGES FACED IN IMPLEMENTATION	
AND ENFORCEMENT OF CORPORATE	
GOVERNANCE..... 44	
4.0 Introduction.....	44
4.1 weaknesses in rules, regulations and audit	
Systems.....	45
4.2 Flawed corporate laws.....	47
4.3 Key corporate governance concepts not	
defined.....	48
4.4 Independence of regulators.....	51
4.5 Inefficient and ineffective judicial system.....	52
4.6 The voluntary nature of corporate governance	
Codes.....	53
4.7 Heavy reliance on regulatory bodies for	
Enforcement.....	54
4.8 Complacent natures of shareholders.....	56
4.9 Compromised quality of leadership and	
Related matters.....	56
4.10 Disclosure issues.....	58
4.11 Entrenched management.....	59
4.12 Conclusion.....	59

	Page
CHAPTER 5: CONCLUSION AND RECOMMENDATIONS..	61
5.1 Conclusion.....	61
5.2 Recommendations.....	65
BIBILOGRAPHY.....	67

University of Cape Town

CHAPTER 1

STATEMENTS, OBJECTIVES, DEFINATIONS AND CHAPTER OUTLINE

1.0. Introduction

Corporate governance is the underlying principle upon which the gamut of a company's corporate existence rests. At the turn of the 21st century, most economies in the world had undergone transformation in the area of Corporate Governance and how a company's affairs should be governed. However, the pace at which this transformation was achieved had been hindered by the legal and social norms including institutions which were deeply entrenched in these economies.¹ The importance of good corporate governance principles cannot be over emphasised as it provides investors with a sense of security knowing that their money will be safeguarded and managed in the best interest of the company.² This sense of security that comes with good corporate governance makes countries safe havens for foreign direct investment which leads to massive capital inflows into those economies thereby promoting growth.³ Countries that have relaxed in the implementation of good corporate governance principles have paid a very high price that has resulted in financial scandals and meltdowns of major multinational companies which in turn has caused negative ripple effects on their economies. It must be noted that poor corporate governance does not always produce adverse effects as those which were experienced in the financial downfall of major companies such as Maxwell, Enron and Parmalat.⁴ However, the server consequences suffered by these companies provide a valuable lesson of what might go wrong when poor corporate governance structures are in place. Various economies have continued being under siege from corporate disasters and meltdowns despite the multiplicity

¹ Luke Nottage *et al Corporate Governance in the 21st Century: Japan's gradual transformation* (2008) 1.

² Brian Coyle *Corporate Governance* (2010) 1.

³ Ramani Naidoo *Corporate Governance: An essential Guide to South African Companies* 2ed (2009) 11.

⁴ Brian Coyle (note 2) 7.

of good governance codes which has created doubts in the minds of various stakeholders as to the efficacy of such codes.⁵

Corporate governance legislation has gained worldwide application meaning that the various hurdles and barriers continue being experienced cannot be isolated to one particular jurisdiction. Despite the many challenges faced, the concept of corporate governance is now seen to cut across all the sectors of business and as such it is essential that its application should be spread across these sectors without discrimination. Against this background, it is justifiable and timely to conduct this research in order to pin point where the major problems lie and at the same time improve on the successes that have been scored.⁶

1.1 Statement of problem

Corporate governance has become so appealing in nature that almost every entity in the world strives to be associated with some if not all of the principles of good governance. Some situations demand the mandatory application of these principles whilst in most cases, entities are encouraged to adopt these principles and bring their internal structures and systems to conform to corporate governance.⁷ Therefore, it is difficult to detach a company's operations from the principles of good corporate governance. Despite the popularisation of corporate governance in most jurisdictions of the world, it is difficult to measure with certainty the levels of progress and challenges being faced due to the diverse nature of its application from one jurisdiction to another.⁸ It against this background that this paper endeavours to take a critical look at the origins of South Africa's corporate governance structures, their current positions on the international scale and the course it is taking for the future. It is from this view that the various developments and hurdles affecting corporate governance need to be

⁵ Ramani Naidoo (note 3) 3.

⁶ Brian Coyle (note 2) 5.

⁷ This is the approach that was adopted by the King III report.

⁸ Luke Nottage *et al* (note 1) 4.

ascertained in order to weigh how much progress has been achieved and the obstacles that have been faced since 1994 when the first King report was published to date. It is worth noting that 18 years have passed since corporate governance was first introduced in South Africa and this makes it timely to critically look at the entire system in order to judge its overall performance.

1.2 Objectives and value

The importance of this paper lies in the fact that this area of study has not received much attention and is rarely investigated by many scholars. It is therefore crucial to evaluate the various aspects of a company's existence in order to take stock of the gains and losses suffered in the area of corporate governance with the ultimate aim of making a meaningful contribution to the effectiveness and efficiency of corporate governance systems in South Africa. Furthermore, this dissertation takes a comparative approach of some of the major corporate governance economies with the existing South African framework with the intention of providing some insight into areas that still require major reconstruction and how other jurisdictions have dealt with this area of study.

1.3 Defining corporate governance

Over the last 10 years corporate governance has continued to grow from strength to strength and its importance transcends the political, social and economic life of companies. It is a concept that continues to change with time and responds to various social, political and economic stimuli.⁹ Various commentators have continued to describe corporate governance as a term that is devoid of an exact definition, 'something –like love and happiness'- of which the essential nature is known, but the difficulty comes in clothing it

⁹ Ramani Naidoo (note 3) 3.

with the precise words which can give it an accurate definition.¹⁰ As a result, its definition poses great challenges in that it is difficult to set its exact boundaries and have a globally accepted definition. Generally, corporate governance is defined as ‘the appropriate board structures, processes and values to cope with the rapidly changing demands of both shareholders in and around their enterprises.’¹¹

However, for the purposes of this dissertation, the definition of corporate governance offered by Ramani Naidoo will be adopted as the working definition as it provides as follows:

Corporate governance regulates the exercise of power (that is, authority, direct and control) within a company in order to ensure that the company’s purpose is achieved (namely the creation of sustainable shareholder value, the *raison d etre* of most for-profit companies)...the practice by which companies are managed and controlled.¹²

The above definition seems to be definitive in nature and satisfies South Africa’s corporate governance needs in that it encompasses the various aspects of corporate governance.¹³ It must be noted that other definitions of corporate governance have not completely departed from the above working definition as they tend to show various similarities in various aspects. For instance Jean Jacques Du plessis *et al* defines corporate governance as follows:

The system of regulation and overseeing corporate conduct and balancing the interests of all internal stakeholders and other parties (external stakeholders, governments and local communities) who can be affected by the corporation’s conduct, in order to ensure responsible behaviour by corporations and to achieve the maximum level of efficiency and profitability for a corporation.¹⁴

Therefore, what comes out clearly from the above definitions is that corporate governance is concerned with the manner in which a company is controlled and most importantly to what end. It emphasises sustainability of

¹⁰ Jean Du Plessis *et al Principles of Contemporary Corporate Governance* (2011) 3.

¹¹ Bob Garratt *Thin on Top: Why Corporate governance matters and how to measure, manage and improve board performance* (2003) 12.

¹² Ramani Naidoo (note 3) 3.

¹³ These areas include checks and balances on the exercise of powers, compliance with legal and regulatory regimes, risk management and accountability.

¹⁴ Jean Jacques Du Plessis *et al* (note 10) 10.

a corporation as a viable entity whilst at the same time sustaining the environment within which it operates.

1.4 Principles of good corporate governance

The term corporate governance is commonly used in the day to day activities in the corporate world however; as has been earlier mentioned the difficult part comes in dressing the term with a clear cut definition. Despite the differences in definitions, corporate governance possesses standard canons that do not change and have uniform application everywhere in the world. For instance, all shareholders should be treated equally whether they are minority or majority shareholders.¹⁵ The board of directors is given the enormous task of acting on behalf of the company whilst at the same time being answerable to the various shareholders for their deeds.¹⁶ In order to conform to the tenets of good corporate governance the tasks carried out by the board should be done in an open manner so as to ensure that information is disseminated clearly to the public and the various stakeholders thereby ensuring transparency of the entire process.¹⁷ Therefore, in ensuring that most entities entrench corporate governance principles, the board of directors should act fairly and remain accountable to the stakeholders' whilst being responsible for their actions which should be done in a transparent manner.¹⁸

1.5 Chapter outline

Chapter two of this dissertation will discuss the legal basis of corporate governance and compliance. In order to achieve this objective, this chapter will be divided into two parts. The first part will deal with the regulatory

¹⁵ This is clearly exhibited by Section 62 of the Companies Act which provide for each shareholder to receive a notice of a meeting without giving special preference to majority shareholders.

¹⁶ Brian Coyle (note 2) 17.

¹⁷ Ibid.

¹⁸ Ibid.

framework of corporate governance in South Africa paying particular attention to the statutory structure, codes of corporate governance and the principles of good practice. This part section will bring out the hybrid nature of the South African corporate governance framework. The second part will deal with the link between corporate governance and the law. It shall be acknowledged that breach of a responsibility or fiduciary duty has the consequence of attracting liability and the sanctions are clearly provided by the law.

Chapter three will start by examining some of the major changes that were made from the King II report to the King III report. This will be achieved by taking a critical look at the particular aspects of the King III report that are distinct and stand out in the promotion of corporate governance. In essence this chapter will not look at all of the changes that were made but will mainly concentrate on the salient changes that were made. With regards to the comparative aspects, the dissertation will outline some of the progresses scored in the area of corporate governance in different jurisdictions, specifically England and USA will be drawn, which will be compared with those achieved in South Africa.

Chapter four of this paper will focus on the various challenges and obstacles that have been faced in the implementation and enforcement of corporate governance in South Africa. Comparative aspects will be made with other jurisdictions in order to achieve the objectives of this chapter.

Chapter five is the concluding part which sums up the entire dissertation and makes various recommendations on how to overcome some of the challenges identified with the aim of improving corporate governance performance in South Africa.

CHAPTER 2

LEGAL BASIS OF CORPORATE GOVERNANCE AND COMPLIANCE

2.0 Introduction

A company is created by the law therefore; its survival is dependent on the various governance structures that have been established by law. It is against this background that chapter two of this dissertation will endeavour to discuss the legal basis of corporate governance and compliance from the South African context. The first part will discuss the established corporate governance structures that are in place with emphasis on the main piece of legislation being the Companies Act of 2008.¹⁹ Thereafter, the need to regulate corporate governance will be looked into and how the codes of best practice form part of the whole matrix. The second part of this chapter will deal with correlation between the law and corporate governance bearing in mind the various corporate responsibilities and duties that the law creates.

2.1 Regulatory framework of corporate governance in South Africa

Corporate governance is a contemporary area of company law that provides a practical lens that can be used to test the various legal and regulatory structures in the environment within which a company exists and carries out its operations. It must be mentioned that corporate governance legislation will vary from one jurisdiction to another and as such the efficacy of the various governance structures will to a large extent depend on the legislation that is in place. According John Folsom:

Over the past twenty years, corporate governance has seen a surge in interest with regard to corporate responsibilities to society. Often these interests have not been embedded in statutes but instead have been implemented through guidelines and codes. The companies Act directly provides clear framework for the empowerment of stakeholders and includes a directive that companies operate to enhance not only shareholder profits

¹⁹ Act number 71 of 2008 was enacted on the 31st of March 2010 and will herein after be referred to as the Companies Act.

but also social welfare. To ensure that these purposes are fulfilled, the South African Government is [has] provided greater power in governance decisions than is typically found in most general corporate statutes.²⁰

Therefore, the above quote seems to suggest that enactment of the Companies Act has seen the implant of classical corporate regulation into the South African economy which has considerably raised the bar in the conditions for doing business while at the same time immensely fortifying the social and economic aims of the company.²¹

The growth of corporate governance in most major economies of the world has seen the establishment of various legal and regulatory regimes which are aimed at controlling, supervising and managing how corporations are governed. In essence, the effectiveness of these governance frameworks will to a large extent be dependent on the potency in the operations of these established structures.²² In South Africa, there is no single piece of legislation that can be singled out as being solely responsible for the regulation of corporate governance in that it tends to draw from numerous sources such as the various pieces of legislation²³, the regulations that are passed to supplement the enabling Act, listing requirements for those companies that are listed on the Johannesburg Stock Exchange²⁴ and the codes of best practice that seek to move with the ongoing trends of corporate governance on the international scene.²⁵ Therefore, the interaction and interdependence between the various pieces of legislation, regulations and codes of best practice in performing the regulatory functions of corporate governance has proved to be appropriate in the context of South Africa's company law in that this amalgamation has led to the growth and recognition of a hybrid system of regulation that is appropriately placed for the emerging South African economic needs. In addition to the law playing an integral part in navigation the course that a company's operations will

²⁰ John Folson 'South Africa moves to a global model of corporate governance but with important national variations' in Mongalo H Tshupo (ed) *Modern Company Law for a Competitive South African Economy* (2010) 219-247.

²¹ Ibid.

²² Ramani Naidoo (note 3) 27.

²³ The Companies Act being at the apex of them all.

²⁴ Herein after referred to as JSE.

²⁵ Ramani Naidoo (note 3) 28.

take, the memorandum of incorporation²⁶ spells out in clear terms the powers that a company can exercise by setting the limits and boundaries within which it may operate. This position has been clearly illustrated by section 15 of the Companies Act which provides that:

15(2) The Memorandum of Incorporation of any company may—

(a) include any provision—

(iii) imposing on the company a higher standard, greater restriction, longer period of time or any similarly more onerous requirement, than would otherwise apply to the company...

(b) contain any restrictive conditions applicable to the company, and any requirement for the amendment of any such condition...

(3) Except to the extent that a company's Memorandum of Incorporation provides otherwise, the board of the company may make, amend or repeal any necessary or incidental rules relating to the governance of the company in respect of matters that are not addressed in this Act or the Memorandum of Incorporation.²⁷

Therefore, from the above provision it clear to see that the memorandum of incorporation is a vehicle that is used in the interaction of the various duties and responsibilities of directors, shareholders and other parties who exist within and outside the company. In essence when dealing with corporate governance regulation, the important role played by the memorandum of incorporation cannot be overlooked in that it is not possible to delink it from the hybrid regulatory chain that exists.

The Companies Act plays a pivotal role as corporate governance legislation in that it provides for the birth, creation of various types of companies and defines the assortment of right and obligations that will flow from the company's corporate nature as a separate legal entity. In an effort to enhance corporate governance, the Companies Act goes a step further in

²⁶ This is the constituting document of the company. This is a document that can be couched in the standard form or in can be tailored according to the company's needs. Furthermore, it may contain provisions that are not encompassed by the Act and it may modify those provisions that may not be altered.

²⁷ Section 15 of the Companies Act 71 of 2008.

specifying the various offences that can be committed by the company and its prescribed officers and the penalties that will attach to such offences.²⁸

In order to have sound corporate governance structures, a number of principles will have to be enshrined in legislation. The Companies Act clearly spells out these principles as it provides for responsibility, accountability and transparency which cannot be unhinged from one another due to the interdependent roles they play in enhancing good corporate governance. For instance, the principle of responsibility comes out clearly when the Act provides that all the matters or business of the company will be taken care of by the board of directors.²⁹ This is an onerous task which if not properly handled, might have adverse effects on the company's operations and productivity. However, the Companies Act steps in to allay these concerns by allowing for the creation of committees whose main objective will be to assist the board of directors in carrying out their obligations. Section 72 of the companies Act provides as follows:

72(1) Except to the extent that the Memorandum of Incorporation of a company provides otherwise, the board of a company may—

(a) appoint any number of committees of directors; and

(b) delegate to any committee any of the authority of the board.³⁰

The fact that the above provision empowers the board of directors to delegate its jurisdiction to the committees, neither means that it has renounced its fiduciary duties to these committees nor does it have the effect of watering down or diminishing the said fiduciary duties. This position is fortified by the King III report which provides that 'the board should delegate certain functions to well established committees but without abdicating its own responsibility.'³¹

²⁸ Section 77 attaches liability on directors and prescribed officers while Chapter 9 of the Act provides for the various offences and penalties.

²⁹ Section 66.

³⁰ Section 72.

³¹ *The King Code of Governance Principles* (King III report) Principle 2.23 available at <http://www.library.up.ac.za/law/docs/king111report.pdf> [accessed on 20th October 2012].

2.1.1 Creation of Committees vis-à-vis corporate governance

It is worth noting that the creation of committees is a clear manifestation of the efficacy of good corporate governance in that the various roles and responsibilities played by the board will be complimented by the various committees thereby ensuring that the company achieves its maximum productivity whilst at the same time ensuring that the company is run ethically and effectively.

(a) Audit Committee

Every company should strive to have in place an independent audit working group that effectively carries out its functions.³² This committee seems to settle in well with good corporate governance principles in that the individuals who compose it will be independent and sufficiently specialised to carry out audit functions. Of course it goes without saying that one of the major challenges faced with the principle of accountability is when it comes to settling on how the director's will be made accountable and over what period of time. The Act provides a solution to this problem in that a company will be required to have its annual financial statements audited every year.³³ In addition, King III further makes provision for the audit committee to convene as frequently as two times in a financial year for the purpose of supervising the integrated reporting.³⁴ From the above it is clear to see that the Act is not only riddled with various principles of good corporate governance which has the net effect of embracing them as codified principles.

³² Ibid Principle 3.1.1 makes it mandatory for all companies that are either owned by the state or are listed on the JSE to have established audit committees while it is highly recommended for all other Companies.

³³ Section 84 which will be presented at the company's Annual General Meeting.

³⁴ King III (note 31) Principles 3.1.4 and 3.4.

(b) Risk Committee

The management of a company is vested with the board of directors and as such a corollary of this responsibility is the taking of risks for the purpose of ensuring that the company is productive and remains profitable. The risk committee plays an integral part in the risk management process of any organisation as it is specifically appointed for the purpose of assisting the board in carrying out its responsibilities that relate to risk.³⁵ In essence, the management of risk is vital to good corporate governance in that it will ensure the growth and sustainability of the company by identifying risks through a logical process of decision making, gauging the value of risk and adequately diminishing or eliminating the risk.³⁶

It is worthy of note that the audit and risk committees are not the only committees that are provided for as there are other committees such as the remuneration committee which will look into the remuneration policies of the company by outlining the various remuneration packages and ensuring that directors are fairly awarded.³⁷ Additionally, the nomination committee will be tasked with the responsibility of advising the board as to the appropriate candidates to be appointed as directors of the company.³⁸

2.1.2 Why is regulation necessary?

One of the main objectives of the company is to provide a conducive regulatory environment that is predictable and productive to the company's needs.³⁹ Primarily, regulations are required for the purpose of rectifying or correcting imperfections that may exist within the enabling act or the environment within which the company operates. Professor Ballantine, a Californian legislative drafter in the 1930s had this to say:

³⁵ King III (note 31) Principle 4.3.

³⁶ Greenfield Michael Risk Management: *"Risk as a Resource"* Virginia: Langley Research Centre available on <http://www.mightystudents.com/essay/Risk.Management.essay.97765> [accessed on 8th October 2012].

³⁷ King III (note 31) Report Principle 2.25.2.

³⁸ Ibid Principle 2.19.1.

³⁹ Section 7(i).

The primary purpose of corporation law is not regulatory. They are enabling Acts, to authorise businessmen to organise and operate their business, large or small, with the advantage of corporate mechanism. They are drawn with the view to facilitate management of business and adjustment to the needs of change.⁴⁰

Against this background, it can be said that the Act enables and authorises the creation of companies while the various pieces of regulations will be drawn up for the purpose of assisting the enabling Act. In essence, there are various changes that will occur in the environment within which the company operates, as such in order for the existing legal framework to easily and quickly adopt or adjust to these needs; various regulations will need to be in place to assist the law to move with the winds of change.⁴¹ The Companies Act mandates various agencies and regulatory bodies to pass regulations which are aimed at assisting the operation of companies and protecting the interests of various investing parties.⁴² These regulatory bodies include the takeover regulation panel, the competition commission and the Securities and Exchange Commission.⁴³ The states' right to regulate corporate behaviour is clearly exercised through regulations.

2.1.3 The role played by the Stock market in Corporate Governance.

With the growth of international trade and commerce, most countries in the world have well established stock markets which are regulated by rules of conduct for those companies which may wish to trade their shares on the stock exchange. Various market forces have been seen to play a pivotal role in the enforcement of corporate governance in that these principles are not codified by statutory law but draw their efficacy from customs of trade. In South Africa, the JSE holds the exchange licence in terms of the Securities Services Act.⁴⁴ This entails that any company that has a desire to trade its shares on the JSE would have to apply to be listed in addition to complying

⁴⁰ Jane Dine *The Governance of Corporate Groups* (2000) 11.

⁴¹ Ramani Naidoo (note 3) 28.

⁴² Ibid.

⁴³ Ibid.

⁴⁴ Act 36 of 2004.

with the various rules and listing requirements⁴⁵ before it can be allowed to list its shares on the stock market.⁴⁶ The JSE is a highly organised system of trading in listed securities which in effect gives the trading public some sense of confidence to freely trade in the securities of such a company.⁴⁷ It strives to uphold the tenets of good corporate governance principles in that the listing requirements are constantly reviewed and updated in order to be in line with the trends that emerge on the international markets. Furthermore, the importance that is attached to the JSE listing requirements is seen through the punishment that follows directors who will be held liable in their individual capacity or by virtue of their position as directors for not complying with the said listing conditions.⁴⁸ To some extent, the JSE listing requirements seems to act as a harmonising factor in terms of the various corporate governance principles and international practices.

2.1.4 Codes of best practices

During the late 1980s and early 1990s, the need to have good corporate governance principles in place was first observed in the UK due to the financial meltdown which was suffered by major multinational corporations such as the Maxwell group of companies. This situation has given impetus to the growth of corporate governance which has seen an overhaul of corporate and securities legislations of most emerging economies thereby formulating a more transparent and adjustable system. The UK being the leading proponent of corporate governance in the world saw the publication

⁴⁵ These requirements are stricter, more demanding and require more extensive duties of disclosure of certain information.

⁴⁶ *JSE Listing Requirements* (2003) Listing Requirement 1.2 available at https://www.jse.co.za/...JSE_-_Listings_Requirements/service_issue_1 [accessed on 23rd October 2012].

⁴⁷ Cassim *et al Contemporary Company Law* 2ed (2011) 76.

⁴⁸ A fine of R1,000,000 (One million Rands) is imposed by the JSE Listing requirements.

of the Cadbury Report in 1992 which was reported as being 'a landmark in thinking on Corporate Governance.'⁴⁹

In 1994 South African was not excluded as it responded favourably to these emerging trends that were being experienced on the international scene in the area of corporate governance. It is against this backdrop that the Institute of Directors were stimulated to publish the King I report which was the first ever corporate governance code. This report was revised in 2004 which saw the publication of the King II report and a further revision was made to King II in 2009 which saw the birth of the King III report that is currently being used. The King III report was published as a response to the new Companies Legislation.⁵⁰

In many parts of the world, most corporate governance codes are modelled either on the basis of a shareholder approach or an enlightened shareholder approach to corporate governance.⁵¹ However, the South African code of corporate governance departed from this conventional but yet prescriptive mode by adopting an entirely new and unique mode that stands out amongst most corporate governance codes in the world. The distinction of this code lies in the fact that it is based on an all inclusive stakeholder approach which will not only consider the interests of the shareholders but will seek to strike a balance between the interests of all the concerned stake holders of the company. This approach has proven to be conducive and favourable to the needs of the South African emerging economy.⁵²

The codes of best practice that exist in most jurisdictions are voluntary in nature in that companies will be encouraged to apply and adopt the said codes voluntarily. However, although the codes maybe voluntary in nature, they are made to apply mandatorily to companies that are listed on the stock exchange in addition to the various other stringent rules which are

⁴⁹ Brian Coyle (note 2) 23.

⁵⁰ King III (note 31) 2.

⁵¹ Brian Coyle (note 2) 47.

⁵² Ibid.

set out by the listing authorities.⁵³ Compliance in the South African context connotes that the company should be able to furnish all the necessary documentation that will show the extent to which the codes and guidelines are being applied. In an event that the company fails or diverts from applying the code, a written explanation that states the reasons for such a diversion will amount to compliance.⁵⁴ The world over, hybrid systems of corporate governance are emerging resulting in most aspects of corporate governance being legislated of course this is in addition to the various voluntary codes of governance and principles which are already in place. The hybrid nature of corporate governance is seen clearly in the Companies Act which derived various principles of good governance from the recommendations that were made in the King II report and some from common law thereby resulting into a formidable corporate legislation that strives to meet society's needs.⁵⁵ In addition the JSE listing requirements also plays its part by ensuring the independence of directors and provides a clear distinction between the roles of the chief executive officer and the chairman of the board.⁵⁶ Therefore, the development of corporate governance codes of practice is as a result of consented efforts by various countries and various other interested players in the corporate world.⁵⁷

2.2 Interconnection between corporate governance and the law

The law is a golden thread that runs through every aspect of a company's existence and as such corporate governance will not be exempted or immune from associating with it. A company is a creation of statute accordingly; all of its dealings and operations will be regulated on one hand by the law and on the other hand by the memorandum of incorporation

⁵³ Brian Coyle (note 2) 36.

⁵⁴ This is what is referred to as the 'apply or explain' doctrine.

⁵⁵ Ramani Naidoo (note 3) 29.

⁵⁶ *Guide to the JSE Listing Requirements: The Boardroom Brief Series* (June 2003) 9 available at <https://www.deloitte.com/assets/.../JSE%20Listings%20Requirements.pdf> [accessed on 28th October 2012].

⁵⁷ Some of these players include the stock exchange, investors, and associations of directors including the international community at large.

document. A consequence that flows from this is that corporate governance cannot exist in a vacuum as its sustainability will greatly depend on the law which creates an inseparable bond between the two aspects.

The fact that corporate governance deals with the way in which a company's affairs are governed entails that the responsibility to perform this momentous task is placed squarely on the shoulders of the directors of the company who will be required safeguard the rights and address the various concerns of the stakeholders whilst at the same time being answerable to the company's shareholders.⁵⁸ This position seems to be a clear justification as to why companies should be regulated by the law in addition to complying with the established codes of best practice. Furthermore, the nexus between corporate governance and the law tends to come out prominently in the established structures and processes of the company which are absorbed in the corporate governance function for the purpose of ensuring that appropriate checks and balances are in place. This interconnection is a safeguard that insulates the company from mismanagement which may be occasioned by the directors. In essence the connection will ensure that directors carry out their duties and responsibilities in line with the guidelines set by the law.⁵⁹ The courts have not taken a leading role in ensuring that corporate governance principles are enforced owing to the fact that it is an area of the law that is fairly novel and has not seen a lot of litigation in the recent past. However, as corporate governance continues to gain ground around in most parts of the world, the courts' involvement in settling disputes that arise out of corporate governance issues is definitely set to increase. This position has been fortified by King III report which provides that 'the more established certain governance principles become. The more likely, the court would regard conduct that conforms with [to] these practices as meeting the required standard of care.'⁶⁰ Therefore in addition to the standard of conduct that has been set by the companies Act and the common law, corporate governance

⁵⁸ Brian Coyle (note 2) 35.

⁵⁹ King III (note 31) 5.

⁶⁰ Ibid.

raises these standards through the various principles, practices and codes.⁶¹

2.3 Conclusion

In conclusion, this chapter has demonstrated that the regulation of corporate governance in South Africa does not emanate from a vacuum nor is it confined to only one piece of legislation but it is drawn from various sources. It has further been seen that the effectiveness of corporate governance in any environment will largely depend on the legal structures that are currently in place in that jurisdiction. In essence the principles of corporate governance cannot be delinked from the law as the two go hand in hand in that corporate law creates various corporate structures and allows for the creation of various legal relationships between various competing interests. It is my view that the law just like corporate governance impacts positively on various aspects of human life such as social, economic, cultural and the environment within which the company operates.

⁶¹ Ibid.

CHAPTER 3

EVOLUTION FROM KING II TO KING III: DEVELOPMENTS AND GAINS

‘The release of King III is a useful addition South Africa’s corporate governance livery and its more flexible “apply and explain” approach is to be welcomed. In most areas, King III represents a major improvement over its predecessor. In other areas, it is hoped that practice notes will be issued to resolve confusion about the practical application of some of its principles.’ Ramani Naidoo⁶²

3.0 Introduction

The first part of this chapter creates the case for corporate governance by giving a background of some of the factors that have acted as catalysts to its growth and development all around the world. The second part goes on to discuss some of the notable changes that have been made from King II to King III bearing in mind that these are not the only changes that were made. The third part of this chapter compares the progresses and successes that have been registered between South Africa and the International world whilst the final part will draw a conclusion of this chapter.

3.1 Case for corporate governance

The existence of a good corporate governance regime is an issue that continues to raise great concern all around the world and is relentlessly gaining more ground with the passing of each year. Various stakeholders have risen up and made their voices heard by calling for companies to exhibit corporate governance at the highest levels through transparency and reporting. The impetus of such requirements was due to the financial scandals that rocked the United Kingdom in the early 1990’s.⁶³ The famous Maxwell Saga is notably one of the greatest financial scandals of all times. Robert Maxwell who was at the helm of the Maxwell group of companies

⁶² Ramani Naidoo (note 3) 267.

⁶³ As a result of bad accounting and fraudulent reporting which saw the disappearance of various company assets.

devised a dangerous scheme of playing ‘*Russian Roulette*’ with the subsidiaries and various assets of his group of companies around the world which made it very difficult and almost impossible to ascertain the profitability of the said subsidiaries. His scheming nature and trickery way of conducting his businesses infiltrated the United States stock exchange market with so much ease where he made billions of dollars through the sale of shares which were far less than their net worth.⁶⁴ Such financial manipulation of the stock market was attributed to the existing porous laws that allowed foreign companies to trade in their shares without being subjected to stringent disclosure rules and procedures.⁶⁵ The justification in placing greater emphasis on transparency in corporate governance and uplifting the reporting standards has been due to the continued collapse of dominant companies in the market and has been summed up as follows: ‘such lapses in corporate governance have uplifted the need for independent audits, independent opinions and independent ratings on corporate governance principles and processes within companies.’⁶⁶

Therefore in response to the various concerns that had been raised in the UK, the Cadbury report was first published in 1992 which was seen as a landmark corporate governance regime.⁶⁷ In this vein, the UK has risen to the status of pioneering the growth of corporate governance structures around the world as various countries use it as a bench mark to record corresponding developments.⁶⁸ The existing corporate governance framework in the United Kingdom has experienced extraordinary movements and changes which have seen over six working groups being instituted between 1992 and 2010.⁶⁹ From this, a perception can be drawn

⁶⁴ Market watch ‘*Maxwell Saga bad accounting aided fraud*’ available at <https://www.nytimes.com/1991/12/08/business/market> [Accessed on 5th October 2012].

⁶⁵ Ibid.

⁶⁶ *Understanding Governance* available at <https://www.docstoc.com> [Accessed on 12th November 2012].

⁶⁷ Championed by Lord Cadbury (the report included a code of best practices known as the Cadbury code).

⁶⁸ Brian Coyle (note 2) 36.

⁶⁹ Which include Cadbury report 1992, Myners Report 1995, Greenbury 1995 (remuneration of directors), Hampel Committee 1998 (composition of the board and role of directors), combined code on corporate governance 1998 (listed companies), Higgs Report 2003 (role of non executive directors), Smith Report commissioned by the financial reporting council

to some extent that the UK is still trying to find its proper footing in the realm of corporate governance but this is a matter which is open to further debate.

In 1992, South Africa stepped up to the challenge by establishing a working group called the King Committee⁷⁰ which was headed by retired Judge Mervin King. The terms of reference of this committee were to consider various issues pertaining to the promotion of corporate governance systems and structures in South Africa. Naidoo seems to put this into perspective when she says that:

...the King committee was formed...to consider amongst other issues of financial reporting and accountability, good governance practice concerning the responsibilities of directors and auditors and a code of ethical conduct for south African enterprises.⁷¹

In essence the King committee was vested with the mammoth task of nurturing and guiding the growth of corporate governance from one stage to another and ensuring that this growth was from strength to strength. This can be clearly seen from the expansive nature in which the terms of reference were drafted. The authoritative nature of the King committee can be clearly seen through the confidence that has been vested in this group to produce three consecutive reports and the subsequent enactment of the Companies Act in 2008. Throughout the world, South Africa is being used as a model of strong and stable good corporate governance principles because its development has been marshalled by only one committee which has provided for continuity thereby giving the committee a greater depth of understanding of the needs of society from one report to the next whilst at the same time gaining the public's confidence.⁷²

(FRC) for guidance for audit committee, Revised combined code 2010 (UK corporate governance code).

⁷⁰ Instituted under the auspices of the South African Institute of Directors (IoD).

⁷¹ Ramani Naidoo (note 3) 32.

⁷² King committee has controlled the process of putting in place a corporate governance frame work from 1992 to 2010.

3.2 The salient changes from King II to King III

Various changes have been recorded from King II to King III, however this dissertation will place emphasis on the most important and noticeable changes that were made.

3.2.1 Inclusive stakeholder relationships

During the apartheid era, various sanctions were imposed on South Africa that resulted in the country being secluded from taking part in various issues on the international scene. With the advent of democracy in 1991, South Africa experienced a complete change in its political, social and economic sectors which was coupled with the re-entrance of the country on to the international corporate market and world economies.⁷³ Paramount on the terms of reference of the first king report in 1994 was to advocate for the highest corporate governance standards in South Africa. King I not only emphasised final and regulatory elements of corporate governance but went a step further to promote an integrated procedure and techniques to achieving good governance bearing in mind the various stakeholders to corporate governance.⁷⁴ Since 1994, the country has undergone a steady transformation in its political, social and economic environment which has seen the need to comprehensively revamp the existing corporate and securities legislation in order to create a more flexible and transparent regime for the various stakeholders which in turn made it necessary to update the King report.⁷⁵ When drafting the King I report, the committee ascertained the duty for companies to admit that they share a special bond with both the society and the environment within which they perform their

⁷³ *King Committee on Corporate Governance: Executive Summary of the King Report* (2002) 6 available at

<https://www.library.ufs.ac.za/.../King%20II%20Report%20Exec%20summary.pdf> [Accessed 1st November 2012].

⁷⁴ Mervyn King *King Report on Corporate Governance for South Africa* available at

https://www.mervynking.co.za/downloads/CD_King2.pdf [Accessed on 1st November 2012].

⁷⁵ Luke Nottage *et al* (note 1) 1.

functions.⁷⁶ This concept is what has become fondly referred to as the triple bottom line which has entrenched its roots firmly in most corporate governance codes of the world as it entails that a company should not only look at achieving the highest levels of profitability but instead try to achieve some form of equilibrium between the social, economic and environmental performance.⁷⁷ The idea of the triple bottom line was given precedence in the King II report as being part of good corporate governance which provides that ‘there is a move from the single bottom line to the triple bottom, which embraces the economic, environmental and social aspects of the company’s activities.’⁷⁸ This position was fortified by the King Committee which provided that:

Successful governance in the world in the 21st century requires companies to adopt an inclusive and not exclusive approach. The company must be open to institutional activism and there must be greater emphasis on sustainable or non-financial aspects of its performance. Boards must apply the test of fairness accountability, responsibility and transparency to all acts or omissions and be accountable to the company but also responsive and responsible towards the company’s identified stakeholders. The correct balance between conformance with governance principles and performance in an entrepreneurial market economy must be found but will be specific to each company.⁷⁹

King I and II emphasised the need to have an all inclusive stakeholder approach. The King III report goes a step further and gives a detailed explanation of this approach in that a board of directors in carrying out their functions must give consideration to what is in the best interest of the company bearing in mind the various legitimate interests and anticipations of the stakeholders. This approach seeks to isolate the need to champion the interests of the shareholder at the expense of the best interests of the company and the various other players. For the first time governing stakeholder relationships have been given the prominence it deserves in the King III report which provides that:

⁷⁶ *King committee on Corporate governance* (2002) 6 available at https://http://www.ecgi.org/codes/documents/executive_summary.pdf [Accessed on 18th October 2012].

⁷⁷ John Folsom (note 20) 222.

⁷⁸ Mervyn King (note 74) 5.

⁷⁹ *Ibid.*

- 8.3. The board should strive to achieve the appropriate balance between its various stakeholder groupings, in the best interests of the company
- 8.3.1. The board should take account of the legitimate interests and expectations of its stakeholders in its decision-making in the best interests of the company.⁸⁰

3.2.2 Scope of application

On one hand, the King II report was limited in its range of application as it only applied to companies that were listed on the JSE, Banks, Financial and Insurance bodies and public sector entities and agencies that were operating under the umbrella of the Public Finance Management Act.⁸¹ On the other hand, companies that were not covered by this umbrella were advised to contemplate applying the code in relation to the various corporate governance principles whilst at the same time the various stakeholders were encouraged to observe how companies were applying the various principles laid down by the code.⁸² King III report has cast the net wider than its predecessor in that it captures all the companies regardless of their character, size and manner in which it has been formed. This position was fortified by the King committee which provides that

We have drafted the principles so that every entity can apply them and in so doing achieve good governance. All entities should apply the principles in the code and consider the best practice recommendations of the report. All entities should by way of explanation make a positive statement about how the principles have applied or have not been applied. This... will allow stakeholders to comment...on the quality of ...governance.⁸³

In essence, the corporate governance principles enshrined in the King III report are drafted in such a fashion that enables an entity to be deemed

⁸⁰ King III (note 31) principle 8.3.

⁸¹ *The King Code of Governance Principles* (2002) principle 1.1 available at http://www.icsaglobal.com/assets/files/pdfs/BusinessPractice_and_IQS_docs/studytexts/corporategovernance2/w_CorpGov_6thEd_StudyText_Appendix4.pdf [Accessed on 13th November 2012].

⁸² *Ibid* principle 1.2.

⁸³ *IoD King Code of Governance for South Africa KING III* (2009) 33 available at <https://www.books.google.co.za/books?isbn=0702184772> [Accessed on 3rd November 2012].

as having complied with the principles if it explains how certain principles have been applied.

The JSE has embraced the King III report as being an integral part of its listing requirements. This imposes a mandatory application of all areas of the King report on all those companies that are listed on the JSE failure to do so such companies must explain why the King report has not been applied in their annual reports and accounts.⁸⁴ Therefore, a company's stakeholders are placed in a position of making the final call in terms of being compliance officers tasked with the responsibility of informing the board whether or not the recommended practices are being observed.

3.2.3 Integrated reporting and disclosure

Another notable distinction between King II and King III is that King II demanded companies implement sustainability reporting as a major feature of corporate governance. Ever since 2002 when the second edition of the King report was published, South Africa as a country has grown from strength to strength as an emerging market economy which in turn has had the ripple effect of making sustainability reporting as a pre-requisite to good corporate governance. Coupled with this economic growth has been the continued mistrust of major companies by society which questions the intentions and business practices of these companies. In addition the efficiency of sustainability reporting had continued to raise serious concerns among various players of corporate governance in that it did not meet their expectations and was viewed as not being cost effective.⁸⁵ These and other concerns have been very persuasive in moving entities to report not only on their total performance into a uniquely novel era of reporting in corporate governance in that the old type of reporting which placed primary focus on

⁸⁴ JSE LISTING REQUIREMENT 3.84 available at https://www.jse.co.za/...JSE_-_Listings_Requirements/service_issue_1. [Accessed on 23rd October 2012].

⁸⁵ *King unveils world first integrated reporting guidelines* 25th July 2011 available at https://www.icsa.co.za/documents/latentnews/IRCMedia_Release.pdf [Accessed on 7th November 2012].

financial information was inadequate to satisfy the desires of the various stakeholders and shareholders included.⁸⁶ These views expressed the need to revamp and revitalise sustainability reporting. It is against this background that King stated:

An integrated report is not simply bolting the sustainability report to the financial report. It incorporates, in clear language, material information from these and other sources to enable stakeholders to evaluate an organisations performance and to make an informed assessment about its ability to create and sustain value.⁸⁷

Therefore a major achievement that has been scored by King III was to go a step further than just sustainability reporting but to place emphasis on the annual integrated report that takes a bird's eye view of the effects that a company is likely to have on the social, environmental and economic fronts.⁸⁸

3.2.4 Risk management

The area of risk management has received more attention in King III as opposed to King II. The South African economy, like most of the world's major economies, has seen the need to manage risk associated with doing business as this has been identified as an important aspect of any company's existence in that it is an area that requires a pragmatic approach in trying to alleviate such risks. As a result, this has transpired in approaching risk from a systematic and more integrated view thereby transforming risk associated with doing business into an opportunity.⁸⁹ King III stepped up and apportioned the daunting task managing risk to the board of directors who should have in mind the risk associated with the various strategies and policies which they are about to implement

⁸⁶ Ibid (King added that the old form of reporting was short term).

⁸⁷ Ibid.

⁸⁸ King III (note 31) Principle 9.

⁸⁹ Reginald Haman 'A new Wave of Risks'. Article based on presentation delivered by Vergotine on behalf of Reginald Haman at the ERM Africa Conference on 13 and 14 March 2008.

furtherance of the company's objectives. This position has been fortified by Naidoo who adds that:

The board's role in the control of risk has increased greatly in King III. The board is responsible for risk governance while management is responsible for risk management strategy approved by the board. The board therefore is responsible for the overall efficiency of risk management, although management remains responsible for implementation.⁹⁰

Therefore, King III attaches great importance to the management of risk because it has become apparent that in order for a company to achieve its long term objectives whilst remaining sustainable as a viable entity, the taking of risks will be inevitable. This justifies the need to harness and manage risk at a higher level such as codifying it in the corporate governance code as a principle of good corporate governance.

3.2.5 Information technology

Information technology has been viewed as the driving force behind the industrial revolution thus cannot be unhinged from the concept of good corporate governance as it provides the much needed value addition to promote corporate governance. IT is seen as a mechanism that strives to promote the various contributions of executives in the decision making process and adherence to the best practices.⁹¹ Furthermore, it is perceived as a factor that extends the intrinsic value of stimulating the interest of various decision makers by making full use of the prospects that are offered such as the internet and the market economies. This position has been fortified as follows:

The affordance of information technology can empower executives to promote a participative and stakeholder welfare environment in decision making of corporate governance, where various stakeholders can be informed, participate to some level, and raise awareness of their best interests.⁹²

⁹⁰ Ramani Naidoo (note 3) 279.

⁹¹ Sheryl Elizabeth Abraham 'Information Technology, an enabler in Corporate Governance', Corporate Governance, (2012) Vol 12 Iss: 3pp 281-291 available at <https://www.emeraldinsight.com/Journals.htm?Articles> [Accessed on 14th November 2012].

⁹² Ibid 285.

Furthermore, in order for the board of directors to make informed decisions various pieces of information need to be computed and manipulated for that specific purpose. This will in turn lead to the creation of various data bases within the company structure that will assist in the detection of fraud in data of a corporate nature.

The King committee realised the importance that information technology plays in the management of any entity and thus introduced a complete chapter on the management of Information technology in the third King report which was a novel feature. The extensive use of IT in the emerging market clearly justifies its inclusion in the report which has gone a step further to link it with the management of risk. As such the Board is vested with the responsibility of management of IT systems through the risk committee that should ensure the integrity of a company's information and data whilst at the same time securing IT systems. Naidoo adds that 'a framework that supports the effective management of information resources...to facilitate the achievement of corporate objectives. The focus on the measurement and management of IT are appropriately controlled.'⁹³

Therefore, a board must be able to make decisions that will in turn be effectively communicated to the various stakeholders; IT plays an integral part in corporate governance in that it extends the ambit of such communications beyond the visible boundaries and systems of corporations.⁹⁴

3.3 Overall progress from King II and beyond

It is undisputable that corporate governance structures all over the world have undergone significant transformation. However, it must be noted that there is no hard and fast rule or empirical formula that can be used to gauge the progress and successes that have been scored in the area of corporate governance. Therefore this dissertation will seek to examine the

⁹³ Ramani Naidoo (note 3) 236.

⁹⁴ Sheryl Elizabeth Abraham (note 91) 287.

progress from a theoretical context by looking into the successes scored in the areas of the legal frameworks, implementation or enforcement, shareholder rights, disclosures and board of directors.

3.3.1 Legal framework

Massive reforms to corporate governance and corporate laws have been necessitated by the need to have in place a more market-driven governance system. In addition, 'updates to the regulations and guidelines, listing requirements and corporate governance codes have been comprehensively revamped.'⁹⁵ For instance, the UK has experienced a complete overhaul of its corporate and securities legislation into a regime that is more pliable and transparent for all the major stakeholders of the company. The UK's Companies Act of 2006 has been said to be the most extensive and self contained piece of corporate legislation to have ever been promulgated by parliament as it seeks to promote among other things regulations that relate to auditing of financial statements with a view of achieving good corporate governance.⁹⁶ The Act envisages the board to be at the top of the decision making process with their responsibilities formally cut out by the available governance structures. Furthermore, it acknowledges that the relationships between the shareholders, directors, management and other stakeholders are only stabilised where an effective governance structure is in place.⁹⁷ Therefore, the board should act in such a way that is most likely to promote the success of the company for the benefit of its members as a whole.⁹⁸ A further gain that has been registered is through the United Kingdom Listing authority rules and transparency rules that incorporate various corporate

⁹⁵ OECD, *Corporate Governance in Asia: Progress and Challenges*, (2011) 9 Available at <http://dx.doi.org/10.1787/9789264096790-en> [Accessed on 8th November 2012].

⁹⁶ 'Corporate Law in the UK after Recent Reforms: The Good, the Bad and the Ugly,' CURRENT LEGAL PROBLEMS, (2010) Vol. 63, pp 315-374, Oxford University Press, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1635732 [accessed on 8th November 2012].

⁹⁷ Ibid.

governance principles to be complied with by companies which are listed on the stock market.⁹⁹

A number of EU directives have also been promulgated by the European commission, with regards to corporate governance principles, in Brussels which are applicable to all EU member states.¹⁰⁰ These directives impose strict requirements for companies to publish businesses for those companies that trade their shares on the regulated market. The directives impose further requirements to have in place audit committees and to establish measures that will ensure that these auditors operate independently with the highest levels of ethics.¹⁰¹ This is without a doubt a step in the right direction in promoting good corporate governance principles on the international scene.

USA has not been left behind as its main achievement in the area of corporate governance was registered with the enactment of the Sarbanes – Oxley Act¹⁰² which was in response to the major financial scandals that were being experienced between 2001 and 2002.¹⁰³ The act applies to both US and Non US companies that have traded their shares on the US stock exchange. The SOX imposes personal liability on the CEO and Financial officers¹⁰⁴ of a company for any inaccuracies that maybe recorded in the financial statements. The SOX acted as a cradle for corporate governance in that it provided for the promotion of whistle blowing function among several other corporate governance principles. The importance of this function was clearly manifested at Enron in 2001 when a whistle blower exposed the various glaring financial irregularities.¹⁰⁵ The whistle blowing function has become a very effective corporate governance mechanism that is used to

⁹⁸ Companies Act 2006 (UK) section 172.

⁹⁹ Brian Coyle (note 2) 36.

¹⁰⁰ Directive 2009/102/EC of the European Parliament and Council of 16th September 2009 in the area of company law available at <https://eur-lex.europa.eu/lexuriserve/LexUrisev.do?Uri=CELEX:32009L0102:EN:NOT> [Accessed on 10th November 2012].

¹⁰¹ Brian Coyle (note 2) 35.

¹⁰² Herein after referred to as SOX.

¹⁰³ ENRON being the notable one and peculiar to the United States of America.

¹⁰⁴ Herein after referred to as CFO.

¹⁰⁵ Brian Coyle (note 2) 222.

expose the most flagrant breaches of corporate governance principles. A case in point relates to the story of Michael Woodford who was a former CEO of Olympus Corporation in Japan who discovered and blew the whistle about the various financial irregularities in the corporation. Despite being fired for going public with his findings, the rewards were greater as the board chairman together with two other executives were found guilty of offences relating to accounting fraud.¹⁰⁶

As a result of the political reforms that have been experienced in South Africa, various corporations inevitably had to be exposed to a different era of political management which in turn had a ripple effect on the market and regulatory system.¹⁰⁷ South Africa as an emerging economy has been in a hurry to implement corporate governance principles which has resulted in major gains being recorded on a number of fronts and the major changes that have been experienced can be attributed to the road to democracy chosen by the country. It is worth noting that corporate governance frameworks vary from one jurisdiction to the next as the existence of such frameworks will largely depend on various factors that may be peculiar to such an economy. In South Africa, the market has been singled out as a major factor that has helped to shape the corporate governance regime. This position has been clearly fortified as follows

Market discipline imposed through falling equity prices has led to radical changes in corporate governance structures and conduct, among others the dismantling of the mining finance houses. Undoubtedly one element of South Africans equity culture, widespread executive share compensation brought home the impact of market disenchantment. But the leading role was played by sovereign institutional investors who robustly criticised corporate structures, governance and performance upon their return to South African Markets in 1994.¹⁰⁸

¹⁰⁶ Bryan Burrough 'The C.E.O who shocked Japan Inc' *The New York Times* (1st December, 2012) available at http://www.nytimes.com/2012/12/02/business/exposure-the-story-of-a-british-whistle-blower-in-japan.html?_r=0 [Accessed 5th December 2012].

¹⁰⁷ Malherbe S and Segal N *Corporate governance in South Africa* (2001) 3 available at http://www.tips.org.za/files/Corporate_Governance_in_South_Africa.pdf [Accessed on 23rd October 2012].

¹⁰⁸ Ibid.

Therefore, it is clear from the above quotation that the conditions that are prevailing in the market have served as a catalyst for change in that it ties in with the legal framework in order to make the South African market a conducive investment destination whilst at the same time creating a hub of good corporate governance. Progress in the area of legislative reform was scored with the promulgation of the Companies Act¹⁰⁹ which has the promotion of corporate governance standards and transparency as one of its major highlights.¹¹⁰ The companies Act strives to promote corporate governance principles in that it provides the need for the accountability by the board of directors to the company's shareholders and goes further to elevate transparency as a pre-requisite to good corporate governance.¹¹¹ In addition the Act under section 159 has given birth to a full gamut of protection to any person who is classified and defined as a whistle blower. This provision is similar to the corporate governance feature that is greatly celebrated in the US SOX Act.

In 2011 another major development was achieved with the promulgation of the Companies regulations which provided inter alia for the enhancement of accountability and transparency in terms of addressing the qualifications of the audit committee and the company secretary.¹¹² The new regulations have resulted in palpable changes in the conduct of business in the market as they provide for the enhancement of various regulatory agencies coupled with various enforcement mechanisms such as Alternative Dispute Resolution, the complaints commission and the companies commission all of which have been classified as major progresses in the area of corporate governance in South Africa.

Furthermore, the JSE listing requirements make it mandatory for all listed companies to apply the King III code and its principles. This requirement is also similar to that which exists in the UK Listing rules.

¹⁰⁹ No.71 of 2008.

¹¹⁰ Section 7(b)(iii).

¹¹¹ Chapter 3 Sections 84-94 deal with auditors, audit committees and company secretary who are the officers of the company that ensure that principles of good corporate governance are observed.

¹¹² Companies regulations, (2011) Regulations 42-44.

Therefore, some of South Africa's backlogs in terms of the levels of disclosure as compared to the practices that are prevalent have been eliminated due to the enhanced Listing rules and accounting standards.¹¹³ It can thus be said that South Africa's legislative framework has achieved tremendous progress and its stable nature has been attributed to the importation of various corporate governance principles from different jurisdictions in addition to the clear set of guidelines, recommendations and conditions by the King committee.

3.3.2 Enforcement and strengthening institutional capacity

Internationally, there has been increased enforcement capability in the area of corporate governance with most jurisdictions registering an increase in the creation of quasi-governmental institutions or bodies that operate separately with the sole purpose of implementing and supervising of corporate governance frameworks. Some of the notable examples include the financial Reporting Council in Hong Kong China, Philippines Stock Exchange, an Enforcement division at the Bursa Malaysia and Audit oversight Boards in Korea and Malaysia.¹¹⁴

In the US, the SOX also has made efforts to strengthen the various private supervisory mechanisms ranging from company's external auditors, audit committees, external counsel, market scrutinisers and not forgetting the whistle blowers who are seen as the 'new kid' on the corporate governance block. Therefore by strengthening the monitoring capacities of these various instruments, the Act is pursuing the possibility of detecting illegal and inappropriate activities.¹¹⁵

With the publication of the King II report on corporate governance in 2002, South Africa has seen the strengthening of institutional capacities by

¹¹³ Malherbe S and Segal N (note 107) 4.

¹¹⁴ OECD (note 95) 9.

¹¹⁵ 'Enron's Legislative aftermath Some Reflections on the deterrence Aspects of the Sarbanes-Oxley Act of 2002' available at <https://www.Law.columbia.edu/Law-economicstudies> [Accessed on the 12th November 2012].

the introduction of various bodies that focus on re-enforcing the enforcement capabilities of the Act thereby enhancing good corporate governance principles. The companies commission is the body that plays a supervisory role in ensuring that the Act is complied with. Cassim *et al* fortify this position by adding that:

Any person including stakeholders ranging from the company secretary, shareholders, directors, trade unions or employee representatives may lodge complaints with the Companies Commission, the companies commission may also act on its own initiative [as] it may investigate alleged contraventions of the act and may appoint an investigator or inspector to investigate the complaint.¹¹⁶

In the US, the Sarbanes –Oxley Act which was enacted after the Enron scandal in 2002 imposes stiff criminal sanctions on directors of a company for any business transactions that may be perceived as being questionable.¹¹⁷ The SOX Act has increased criminal penalties imposed on the Chief Executive officer and financial officer for any inaccuracies in the financial statements on the company thereby making these officers personally liable in addition to any other civil liabilities that may be attached.¹¹⁸

The South African Companies Act has moved from an extensive highly criminalised Act to a more flexible and decriminalised Companies Act. The Act is not completely devoid of any criminal sanction in that these seem to be specifically reserved for grave offences and contravention of the Act. Cassim *et al* adds that ‘the object of decriminalising company law is not to trivialise the importance of effective sanctions for non-compliance but instead to ensure more effective enforcement.’¹¹⁹ Therefore the main aim is to reduce criminal sanctions but instead rely more on non-criminal remedies such as administrative fines. Thus decriminalisation has been singled out as a more effective means of enforcing the Act which is peculiar to the South Africa corporate governance needs.

¹¹⁶ Cassim FHI, *et al Contemporary Company Law* 2ed (2012) 24.

¹¹⁷ *The Wall Street Journal*, Thursday 24th June, 2010 available at <https://www.online.wsj.com/article/SB10001424.html> [Accessed on the 12th November 2012].

¹¹⁸ Brian Coyle (note 2) 37.

¹¹⁹ Cassim FHI *et al* (note 116) 24.

3.3.3 Shareholder rights

The 21st century is fondly referred to as the computer age. This is because the last decade has experienced an accelerated rate of technological growth. Coupled with these changes has been the adoption and increased use of these technological innovations by individuals, business houses and the society at large.¹²⁰ Corporate governance has achieved major gains in the use of technology which is being utilised to promote shareholder participation. The physical presence of board members is no longer a pre-requisite to holding a meeting as technology has enabled the various shareholders to participate through electronic means. The enactment of the Companies Act in 2008 has codified the participation of a director through electronic means by providing for the following:

73(3) except to the extent that this Act or a company's Memorandum of Incorporation provides otherwise-

- (a) a meeting of the board may be conducted by electronic communication; or
- (b) one or more directors may participate in a meeting by electronic communication,

So long as the electronic communication facility employed ordinarily enables all persons participating in that meeting to communicate concurrently with each other without an intermediary, and to participate effectively in the meeting.¹²¹

From the above provision it is clear to see that the Act has achieved its intended purpose of promoting corporate governance by making the participation in meetings more flexible and easy for the members. In addition, technology plays a pivotal role in the dissemination of information to the shareholders and stakeholders by the use of emails or other updates that maybe made on the company's websites.

In Asia there is a moving trend towards promoting the active participation of shareholders in the governance process. For instance, there

¹²⁰ Mail & Guardian, *The promise of Technology in South Africa* available at <https://www.thoughtleader.co.za/leeroychetty/2012/05/21/the-promise-of-technology-in-SA/> [Accessed on the 13th November, 2012].

¹²¹ Section 73.

has been the formation of minority shareholder groupings in Malaysia that act as watchdogs and provide a stage aimed at initiating collaborative shareholder activism issues that relate to unethical or management practices that do not instil a sense of confidence in the public in particular for companies that are listed.¹²²

In the US and the UK, the voices in the area of shareholder activism are becoming louder and louder as major companies have become accustomed to this growing trend in that it is seen as an integral part of achieving accountability. An important weapon in the activist's arsenal is a readiness to use the public domain as a forum for initiating change. Therefore whether economies are strong or weak there is a growing trend for shareholders in publicly listed companies to make their views known. The wave of shareholder activism has been encouraged by changes in the UK corporate laws which have effectively assisted the shareholders to strike a balance between management and themselves as the scale seems to be firmly tilted in favour of the owners.¹²³

The area of shareholder activism is slowly but surely gaining ground in South Africa as most shareholders are encouraged to take up the responsibility that comes with the ownership of shares by opening relevant channels of dialogue with the managers of the company.¹²⁴ Therefore activism demands that the shareholder should carefully pay attention to what is happening within the company and engage the company by putting into use their powers and rights vested in them by virtue of their position as shareholder. Shareholder activism has continued to set trends in South Africa's corporate world as operations of companies that are listed on the JSE are continuously placed under a magnifying glass. The former finance minister Trevor Manuel had this to say:

¹²² OECD (note 95) 10.

¹²³ *Shareholder activism: guide to shareholders Rights* available at https://www.taylorwessing.com/uploads/EX.siruplmgmt/shareholder_activism-guide_to_shareholder_rights.pdf. [Accessed on 14th November, 2012].

¹²⁴ CGF Research Institute (PTY) Ltd *Understanding governance, Shareholder and Stakeholder activism* (issue 51) available at <https://www.docstoc.com/docs/19600007/understandinggovernance> [Accessed on 14 November, 2012].

Be alive in your power, develop a checklist of good corporate citizenship, attend general meetings, vote and understand your rights and obligations. My invitation to each of you, perhaps as a first step in your own shareholder activism, is to collaborate, to develop and publicize the checklist. It is the least you owe yourself and future generations.¹²⁵

Therefore it can be said that shareholder activism is a gain that has been recorded as it brings shareholders to realise the bargaining power which attaches with the ownership of such shares and as such it can be used as an agent of change in an instance where one is dissatisfied with the way in which certain issues are being managed.¹²⁶ In essence, where a company's performance does not seem to match the various expectations of society and the shareholders, the net effect is that such a company is likely to suffer significant consequences due to the robust attacks that will be made on management and its governance processes through the media, demonstrations and consumer boycotts which may be used as some of the mechanisms to achieve of stakeholder activism.¹²⁷

Corporate governance codes and principles that exist globally have strived to mould the norms of society in relation to the corporate structures, procedures and behaviours that will be deemed to be appropriate to that society's needs.¹²⁸ Derivative actions in the UK will not generally be upheld under the rule in *Foss v. Harbottle*¹²⁹ if such an action was brought by a minority shareholder unless the conduct complained of amounts to 'fraud on the part of the minority'. Only then can a minority enforce the company's rights.¹³⁰ The enactment of the Companies Act in South Africa has added a breath of new life in the remedy of derivative actions as this type of action will not only be confined to the company itself but is extended to cover various other stakeholders. A new feature that seeks to promote corporate governance in this area has been the extension of the right to commence an

¹²⁵ Ibid.

¹²⁶ Shareholders who believe that the board is not acting in their best interests can in extreme cases remove the said board of directors.

¹²⁷ CGF Research Institute (note 123).

¹²⁸ Examples of such principles' are those contained in the OECD and the UK corporate governance codes.

¹²⁹ (1843) 67 ER 189.

¹³⁰ Explanatory notes on UK Companies Act (2006) 73 available at <https://www.en.wikipedia.org/wiki/Derivative-suit#cite-note-6> [Accessed on 18th November 2012].

action on behalf of the company by various stakeholders who may be affected by its business. Section 165 has been couched in a non restrictive manner in that the shareholders are no longer the only plaintiffs who can sue on behalf of the company but allows for a wide range of interested parties to commence an action.¹³¹

Another corporate governance feature that is related to derivative actions that came out from the enactment of the Companies Act is in the area of class actions. Although class actions are a foreign phenomenon to South African common law, reforms to various pieces of legislation have seen the importation of this form of this form of remedy as being part of the current common law. This position is clearly fortified by the Companies Act which provides that:

157(1) When, in terms of this Act, an application can be made to, or a matter can be brought before, a court, the Companies Tribunal, the Panel or the Commission, the right to make the application or bring the matter may be exercised by a person-

- (a) directly contemplated in the particular provision of this Act;
- (b) acting on behalf of a person contemplated in paragraph (a), who cannot act in their own name;
- (c) acting as a member of, or in the interest of, a group or class of affected persons, or an association acting in the interest of its members; or
- (d) acting in the public interest, with leave of the court.

From the above provision it clear to see that various players are placed in an advantageous position of forming groups or classes that are aimed at putting all of their efforts in trying to obtain some form of remedy for issues such as consumer rights violations they might have suffered within the prevailing corporate and commercial world of business.¹³² Therefore class actions are a major achievement in corporate governance as they arm citizens with the much needed 'fire power' that can be used against an organisation that is being managed by directors who are not sufficiently

¹³¹ Some of these include employees, trade unions, directors and any other stakeholders who may be affected by the company's actions.

¹³² CGF Research Institute (PTY) Ltd *Class Actions in South Africa*, available at <https://www.cgfresearchinstitute.com/portals/274/docs/classActions1.pdf> [Accessed on 12th November 2012].

equipped to handle the various corporate challenges that exist in the environment within which corporations exist.¹³³

3.3.4 Corporate Social Responsibility as a shareholder issue

The concept of corporate social responsibility is a corporate governance concept that has continued to spread its tentacles internationally. However, it is worth noting that there are variations as to how it is applied and dealt with from one jurisdiction to the next. The EU has linked the operation of a business vis-à-vis its stakeholders with the integrated and social concerns which maybe experienced in the currency of running such business operations. In the Green paper on CSR the EU stated that ‘ CSR is not only fulfilling legal expectations, but also going beyond compliance and investing more in human capital, the environment and the relations with stakeholders.’¹³⁴

In the UK, CSR concerns have made a lot of progress with some voluntary groups of UK companies such as the Business in the community taking up the mantel in promoting CSR principles that companies should treat employees fairly and with respect, operate in an ethical way and with integrity, respect basic human rights while sustaining the environment for future generations and encourage companies to be responsible neighbours in the communities within which they operate.¹³⁵ For example:

In 2010 retailer Marks & Spencer announced a new list of ethical and environmental commitments up to 2020, and its intention to become one of the world’s most environmentally friendly retailers by 2015. An initial list of 100 five-year ethical and environmental targets had been announced in 2007, including the aim of becoming carbon neutral and eliminating landfill waste and the company expected to achieve its targets....its targets for 2020 including sourcing all food, clothing and home items from sustainable or ethical sources such as the fair-trade scheme and trying to persuade its

¹³³ Ibid.

¹³⁴ *Green Paper promoting a European framework for CSR* [COM/2001/0366] available at <https://www.eur-Lex.Europa.eu/smartapi/cgi/sga-> [Accessed on 12th November 2012].

¹³⁵ Brian Coyle (note 2) 235.

clothing suppliers, especially in India, to pay a living wage to its employees, but without adding costs for the consumer.¹³⁶

South Africa has not lagged behind in this regard as CSR has not only become a recurring topic in debates and conversations but also a palpable effort by various entities. The corporate governance guidelines, standards, codes and principles are contained in an all inclusive state of the art 'tool box' known as the King report which is highly recommended for companies that are doing business within the country. The progress that has been registered in the area of corporate governance has been summed up as follows:

The launch and growth of the JSE social responsibility index (JSE SRI) in 2001... informs investors and market agents about corporate social responsibility policies and practices of listed companies, encouraging investors to support "friendly" companies and pushing corporations to reinforce their environmental, social and governance initiatives. Responsible investment is a relatively new concept (Dow Jones sustainability index were introduced in 1999 and the FTSE4Good index series was launched in 2001).¹³⁷

South Africa has done well for itself in this area in that among the various emerging markets, it has taken the leading role in registering major gains as it was the first economy that launched the Sustainability index followed by Brazil in 2005.¹³⁸ In this regard it is clear to see that South Africa is in the forefront in the development of corporate governance principles.

3.3.5 Financial reporting standards and disclosure

The 21st century has without a doubt come with major challenges such as the adverse effects of globalisation on the capital markets which have necessitated the need to merge the 'locally Generally Accepted Accounting Principles(GAAP) with International Financial Reporting Standards

¹³⁶ Ibid.

¹³⁷ Consultancy Africa Initiative *Corporate Social Responsibility in South Africa: More than a nice intention*, available at <https://www.consultancyafrica.com/index.php?option=com-content> [Accessed on 10th November 2012].

¹³⁸ Ibid.

(IFRS).¹³⁹ It is quite obvious that companies that adopt these IFRS are placed at an advantage over their various competitors due to the consistent nature in which their financial records will be produced. In essence, those companies that operate international outlets and branches have benefited immensely as the various offices use a standardised technique of reporting regardless of where they are situated which ties in with the other companies operations.¹⁴⁰

Another corporate governance initiative that has received a lot of praise which is peculiar to listed companies has been the adoption of rules that require the strengthening of precise and well timed announcements relating to price sensitive information. A classic example is provided by the Singapore Exchange Listing Rules which allow companies that issue their shares on the stock market to call for a halt in the trading of their shares for a period of up to three days in order to explain the rumours associated with such an issue and in addition to distribute any sensitive information relating to prices changes.¹⁴¹

Companies that are listed on the JSE have since 2005 been required to apply the IFRS.¹⁴² This has resulted in the extensive revamping of South African GAAP in an effort to standardise them with IFRS which in turn has resulted in GAAP ceasing to apply with effect from 1st December 2012.¹⁴³ Ultimately, all the entities that use GAAP are expected to migrate to start using either IFRS or IFRS for SMEs. Therefore, this is a milestone achievement in promoting corporate governance as it seeks not only to promote transparency but also accountability.

¹³⁹ OECD (note 95) 9.

¹⁴⁰ *The benefits and drawbacks of conversion from GAAP to IFRS* available at <http://www.articlesbase.com/accounting-articles/the-benefits-and-drawbacks-of-conversion-from-gaap-to-ifrs-1557114.html> [Accessed on 12th November 2012].

¹⁴¹ OECD (note 95) 9.

¹⁴² Ramani Naidoo (note 3) 36.

¹⁴³ Financial reporting available at <https://www.saica.co.za/TechnicalInformation/FinancialReporting/tabid/117/language/en-ZA/Default.aspx> [Accessed on 15th November 2012].

3.3.6 Media and public involvement in corporate governance

Various factors have been attributed to the development and growth of corporate governance in South Africa. The media and public demand for companies to exercise good corporate governance practices has been cited as one of the major agents of change and reform on this area. This is because the media has continued to play the role of a promoter and watchdog of corporate governance thereby being used as a tool for exposing all the issues relating to corporate governance whether such information is negative or positive.¹⁴⁴ Coupled with this has been the ever growing public demand for transparency and adherence to corporate governance principles by companies. Naidoo stresses this point when she adds that:

...investors and the public tend to keep a more watchful eye on the way companies are being run and, spurred on by shareholder activists and the media, are increasingly demanding greater accountability and better corporate citizenship from companies.¹⁴⁵

The media's role is not restricted to merely gathering corporate governance information that is in the public interest but goes further to disseminating such information to the various stakeholders. This function was clearly seen in November of 2012 when the global coffee giant, Starbucks Corporation was reported to be avoiding payments of corporate tax despite recording sales of nearly £400 million in the UK alone. Due to consumer power and public pressure to account to the inland Revenue the BBC business news caught on to the story and made screaming headlines which resulted in the firm admitting that it needed to pay more taxes in the UK.¹⁴⁶ This is a clear manifestation of how much power is wielded by the public and media when it comes to the development and growth of corporate governance.

¹⁴⁴ Ian W. Jones and Michael G. Pollitt *'who influences debates in business ethics? An investigation into the development of corporate governance in the UK since 1990'* (2001) ESRC Centre of business research, University of Cambridge working paper no.221.

¹⁴⁵ Ramani Naidoo (note 3) 20.

¹⁴⁶ *Tax: Starbucks in talks with UK's Revenue and Customs* available at <https://www.bbc.uk/news/business-20573208> [Accessed on 2nd December, 2012].

3.4 Conclusion

To sum up, this chapter has clearly demonstrated that South African Corporate governance structures have not remained stagnant from 1994 when the first King report was published up to date. It is said that the law changes and evolves in order to meet and satisfy the various needs of society and this has been clearly manifested by the three successive King reports which have responded favourably to changes in the society where they are applied and also to changes that have been experienced internationally. Most of the changes that have been recorded are without a doubt progressive in nature and have touched on various spheres of the economy which has had the effect of elevating South Africa to the top position in the world in terms of corporate governance.

CHAPTER 4

CHALLENGES FACED IN THE IMPLEMENTATION AND ENFORCEMENT OF CORPORATE GOVERNANCE

'if a country does not have a reputation for strong corporate governance practices, capital will flow elsewhere. If investors are not confident with the level of disclosure, capital will flow elsewhere. If a country opts for lax accounting reporting standards, capital will flow elsewhere. All enterprises in that country - regardless of how steady fast a particular company's practices maybe suffer the consequences.' Arthur Levitt¹⁴⁷

4.0 Introduction

The last decade has seen the evolution of corporate governance as a concept that transcends all the sectors of a company's operations and existence. As a result of the financial crisis that was experienced in the major economies of the world, various multinational corporations and banks went into bankruptcy which led to a loss of confidence by investors in the financial markets which in turn had a ripple effect of numerous withdrawals from the financial markets.¹⁴⁸ However, contemporary corporate governance principles are being used as a mechanism for restoring investor confidence in the markets that were adversely affected by the financial meltdown. A classic example was seen in 2003 when investors in the UK and USA were willing to pay up to 18% more for shares of a company that had established good corporate governance structures¹⁴⁹

The implementation of any programme at any level is always faced with challenges. The manner in which those challenges are tackled will determine how smoothly the implementation and enforcement process will be. It is against this background that this chapter seeks to determine the various challenges and obstacles faced in the enforcement and implementation of corporate governance. Firstly the obstacles to the execution of the legal

¹⁴⁷ Chris Mallin *'The Relationship between Corporate Governance, Transparency and Financial Disclosure'*: Selected Issues in Corporate Governance (2003) 9.

¹⁴⁸ In particular, overseas investors were the first ones to make a quick exit.

¹⁴⁹ 'Regional and Country experiences': Selected Issues in Corporate Governance (2003)

framework will be looked at. This will be followed by the various challenges faced by regulators and how the limited awareness of shareholder rights compound to this problem. Furthermore, various issues that deal with disclosure in terms of poor transparency and how the problems associated with the new accounting systems affect corporate governance structures. The last part will concentrate on the weaknesses that affect the board such as the lack of transparency which characterises the nomination process of board members in relation to SOE's, related issues such as unqualified candidates and the lack of knowledge of cumulative voting processes and then finally, a conclusion will be drawn.

4.1 Weaknesses in rules, regulatory and audit systems

Traditionally, corporate governance is seen as a new current that acts as a major driving force in the economic development of the world's emerging markets although in reality it seems to turn a blind eye to a wide range of topical problems that attach to development such as anti corruption, issues of poverty, creation of jobs, political reform, education and the media.¹⁵⁰

It is without a doubt that 18 years down the line; corporate governance is still faced with enormous challenges when it comes to the implementation and enforcement of its framework. Simply put, 'most growing economies that are in the process of transformation have been unable to consistently enforce the laws and strike a clear balance between the various rules and regulations that relate to corporate governance.'¹⁵¹ Therefore the major obstacle lies in how entities will ensure that the already existing laws are religiously adhered to and complied with.

Despite the existence of corporate governance structures in various world economies, loopholes have continued to manifest in these system thereby posing challenges to the efficiency and effectiveness of such

¹⁵⁰ Eric Hontz & Aleksandr Shkolnikov (ed) *'the intersection of public and private reform'*: Corporate Governance (2009) USAID the centre for international private Enterprise.

¹⁵¹ John O. Okpara *'perspectives on Corporate Governance challenges in Sub-Saharan African Economy'* Journal of Business & policy Research (2010) Vol.5 Number 1 110-122.

systems. The flowery nature of corporate governance has resulted into various entities having watertight and foolproof mechanisms and controls that are only existent on paper when in reality such controls are either very weak or at times even non-existent.¹⁵² In 2011, the financial markets in the UK were in a state of great disturbance and discontentment when UBS¹⁵³ suffered losses amounting to £ 2.3 billion at the hands of an employee who conducted fraudulent trading of the company's stock due to the various weaknesses and failures in the existing internal controls and systems.¹⁵⁴ Kweku Adoboli the rogue trader was convicted exactly three years after the bankruptcy of the Lehman brothers Bank which paints a grim picture as to the effectiveness of corporate governance.¹⁵⁵ The banking and financial sectors of any economy are very critical and need to be safeguarded with the most infallible corporate governance structures and control mechanisms as bankruptcy which is attributed to questionable management practices or unethical practices poses a threat to the shareholders, the public who deposit their money with such banks and the negative aftershocks will be felt more keenly by the economy ¹⁵⁶

The above situation has created precedent as to the weaknesses of corporate governance as the employee managed to conceal the fraud which went undetected even in the work of audits carried out on the banks financial statements which also raises further concerns as to the

¹⁵² Michael Webb 'Corporate Governance- Challenges, opportunities and Returns' (2006) The QATAR Corporate Governance Conference Doha 13-14 September 2006. Available at http://www.qfcra.com/publication/Corporate-Governance_Challenges_Opportunities_and_Returns.pdf [Accessed on 27th November 2012].

¹⁵³ a global firm that provides financial services.

¹⁵⁴ UBS: Rouge at the Bank provides a teaching moment available at <https://www.Jamesrpeter.com/hom/internal-controls-and-risk-manangement> [Accessed on 27th November 2012].

¹⁵⁵ Ibid.

¹⁵⁶ Rajesh Chakrabart *Corporate Governance in India-Evolution and Challenges* (2002) 20 collage of management Georgia tech available at <https://www.unpan1.un.org/intradoc/groups/public/.../UNPAN023826.pdf> [Accessed on 28th November 2012].

effectiveness of the audit processes. Some of the concerns that have been raised include the following:

A question could be posed...concerning the bank's reported 2010 payment of fees to Ernest & Young of 67.4 million Swiss Francs (\$59million) of which 58.5 million was classified as audit fees to obtain the latest annual version of the standard auditor's report.¹⁵⁷

The audit report was not received favourably by the various investors as it was riddled with opinions on the financial position of the bank that were not qualified or based on concrete evidence.¹⁵⁸ This position justifies why the independence of auditors has continued to come under attack as they are viewed as mere cronies of the board mainly interested in being retained for the next financial year thus operate at the whims and caprices of the management that appoints them.¹⁵⁹

4.2 Flawed Corporate laws

The corporate scandals that were being experienced the world over in the early 1990's acted as a trigger event for various jurisdictions to adopt and implement corporate governance laws, rules and regulations. In the USA, the most notable one was the Sarbanes-Oxley (SOX) which was promulgated in response to the collapse of major companies like Enron and WorldCom. Since its enactment, the SOX act has received praise the world over as being the first corporate governance legislation which is a model of a mature market economy. However, in recent years this act has continuously been the subject of criticism as it is said to have 'been rushed through both Houses of Congress with relatively little debate following the Enron failure.'¹⁶⁰ Therefore, 'Sarbanes-Oxley has manifestly not ameliorated the flaws persistent in the nation's corporate reporting and assurance

¹⁵⁷UBS: *Rouge at the Bank* (note 153).

¹⁵⁸ Ibid.

¹⁵⁹ John O. Okpara 'Corporate Governance in a developing economy: Barriers, Issues and Implications for firms' *Corporate Governance* (2011) Vol 11 iss2 184-199 available at <https://www.emeraldinsight.com/tk/htitem3> [Accessed on 29th November 2012].

¹⁶⁰ Eric Hontz & Aleksandr Shkolnikov (ed) 'the intersection of public and private reform': *Corporate Governance* (2009) 4.

structures'¹⁶¹ as it seems to be a politically motivated placebo that is aimed at misleading the public into believing that it offers solutions to the various corporate governance challenges. In the wake of a series of corporate scandals that continue being experienced in the corporate world, corporate governance has come under immense scrutiny and attack by various players who feel that it offers a raw deal as it is viewed as not achieving the purpose for which it was intended. Put simply:

The more the cost of governance, regulation and compliance increases, and the bigger and more embedded in business life the governance industry becomes the harder it is to ask the question which really matters – will the current approach deliver the outcome we want?...the answer is an uncomfortable truth. There is huge scepticism about the current system, the principles which drive it and whether it will live up to the expectations of its supporters. If ever there was a clarion call for an industry to think seriously about where it is heading this is it?¹⁶²

The growth and development of corporate governance in most parts of the world has been hindered as a result of corporate laws which are imported from other jurisdictions and enacted into domestic laws with little or no modifications.¹⁶³ In the long run such actions of copying and pasting tend to become problematic as the original laws do not take into consideration the various motives and needs of the local communities. In the same vein, corporate governance principles have suffered the same fate of being uplifted from models of major economies and applied in there totally which tends to presents challenges when it comes to implementation and enforcement of these principles.

4.3 Key corporate governance concepts are not defined

Despite corporate governance receiving so much publicity internationally, it has without a doubt been riddled with difficulties when it comes to its smooth implementation and enforcement. Various jurisdictions have fallen

¹⁶¹ Sarbanes-Oxley, *ten Years After-Are we having fun yet?* Available at <https://www.Jamesrpeteron.com/hom/internal-controls-and-risk-management> [Accessed on 27th November 2012].

¹⁶² Anthony Hilton *Challenging Corporate Governance Structure: A summary of the main issues covered at the 2010 Airmic Conference Workshop.*

¹⁶³ OECD (note 95) 11.

in the trap of implementing corporate governance structures without considering the various problems and obstacles that will be faced in the process. Corporate governance principles are well thought out principles which if implemented timely are most likely to yield the best results. However there seems to be a trend around the world to implement the structures in a hurried manner so as to portray a picture of moving at the same pace as the international markets. Coupled with this has been the need to appease and advance the needs of the politicians who are in power. Asia has recorded massive gains in the area of legal and regulatory framework which has seen various updates to the laws and regulations which is in addition to the strengthening of various employee representative bodies.¹⁶⁴ However the insufficiency lies in the inability to give the precise meaning to a number of corporate governance concepts which in turn manifests in loopholes in the enforcement of corporate governance due to the uncertainty it causes.¹⁶⁵ It is note worthy that where key concepts are not defined, the end result is that the system will be filled with lacunae and this in turn leads to a lack of understanding of the major concepts that matter. This position was fortified as follows:

All jurisdictions surveyed reported the lack of understanding of a number of concepts such as “material transactions”, “independent board member”, “fiduciary duty” and “related parties” was noted as a major obstacle for the effective implementation of these concepts.¹⁶⁶

Therefore, it can be said that the smooth implementation of corporate governance has to some extent been hindered by such insufficiencies which have gone silently unnoticed since the inception of most corporate governance structures. Although it can be argued that such concepts do not necessarily need to be defined, their relevance tends to emerge when giving clarity to the definitions of the various duties and responsibilities that attach to the officers of the company.

In South Africa, most glaring loopholes have been sealed with the enactment of the Companies Act which clearly defines most of the major

¹⁶⁴ OECD (note 95) 11.

¹⁶⁵ Ibid.

¹⁶⁶ Ibid.

corporate governance concepts. However, this does not mean that such concepts have been simplified to such an extent that they can be easily understood by the ordinary citizenry in that the Act is still riddled with a number of complexities that would require the services of a lawyer in order to get a clear interpretation. For instance, part 5 of the Act provides for the various categories of fundamental transactions¹⁶⁷ but does not give full definitions which can be clearly or easily understood. This manifested through the complex nature in which amalgamations and mergers are defined which cannot be easily explained in terms of the Act.¹⁶⁸

The board is vested with the momentous responsibility of managing the affairs and business opportunities of the company whilst at the same time act as the nerve centre and guardians of corporate governance.¹⁶⁹ In order for the board to be in a position to effectively and efficiently perform the corporate governance tasks assigned to them, it is essential that the key concepts are clearly defined and understood. The Companies Act has gone a step further to incorporate and define a directors fiduciary duties which is a clear departure from placing reliance on the common law for clarification.¹⁷⁰ Furthermore, a director maybe declared delinquent or placed under probation by various persons who are given the right to make an application to court for such an order.

162 (2) A company, a shareholder, director, company secretary or prescribed officer of a company, a registered trade union that represents employees of the company or another representative of the employees of a company may apply to a court for an order declaring a person delinquent or under probation if-

(a) the person is a director of that company or, within the 24 months immediately preceding the application, was a director of that company; and

(b) any of the circumstances contemplated in-

(i) subsection (5) (a) to (c) apply, in the case of an application for a declaration of delinquency; or

¹⁶⁷ Which include disposals, amalgamations and mergers and schemes of arrangements sections 112-115.

¹⁶⁸ *Salient features of the New Companies Act 2008* (10th August 2011) available at <http://exchangesponsors.co.za/?p=455> [Accessed on 21st November 2012].

¹⁶⁹ Section 66 and Principle 2.1 King III report.

¹⁷⁰ Section 76.

(ii) subsections (7) (a) and (8) apply, in the case of an application for probation.¹⁷¹

With regards to the above provision, the Act seems to have fallen short in that these concepts (delinquent and probation) are not defined in the definition section of the Act or the main body of the section which leads to speculation and uncertainty thereby posing a challenge to the implementation of corporate governance. In essence, for the avoidance of doubt and in order to eliminate speculation, the Act should have gone a step further in addressing these issues to achieve some level of certainty.

4.4 Independence of regulators

All over the world corporate governance is seen to thrive in an environment that is well monitored and closely regulated. The need to have a foreseeable and adequate environment that will enable regulation of companies is enshrined in the Companies Act.¹⁷² A survey conducted by the Asian roundtable on corporate governance revealed that one of the major obstacles to implementation and enforcement has often been attributed to the regulators inability and capacity to compel the obedience of the existing regulations due to limited resources.¹⁷³ In addition to resource constraints, there are other non-resource problems that are general in nature which may be linked to monitoring and evidentiary issues that hinder the implementation of corporate governance.¹⁷⁴

South Africa, like most emerging corporate governance economies, faces major challenges when it comes to the independence of regulators and constraints relating to resources. This position was fortified as follow:

Although there are moves towards promoting coherence in the regulatory system, regulation in South Africa remains fragmented and contradictory in

¹⁷¹ Section 162.

¹⁷² Section 7(l).

¹⁷³ Andreas Grimminger *Corporate governance in Asia: Progress and Challenges*. Asian roundtable on corporate governance shanghai, 16th December 2010 available at <http://www.oecd.org/daf/corporateaffairs/corporategovernanceprinciples/46892816.pdf> [Accessed on 19th November 2012].

¹⁷⁴ Ibid.

many respects. Furthermore, difficulties arise in the administration of different forms of regulations.¹⁷⁵

In South Africa it has been widely accepted that dedicated regulators need to be in place in order to achieve the growing regulatory functions in corporate governance. However, in order to achieve some form of uniformity between the various regulators, their roles and responsibilities need to be clearly outlined although this is difficult with the various limitations faced in this area.

4.5 Inefficiency and Ineffective Judicial System

Another major challenge that has been faced in the implementation and enforcement of corporate governance in Asia has been attributed to the inefficiency, ineffectiveness and lack of specialisation on the part of the Judges in dealing with corporate Governance matters.¹⁷⁶ Corporate governance is an area that is not highly litigated owing to the novelty of the concept which in turn leads to most judges not being proficient and lacking the requisite knowledge on how to adjudicate on matters in this area. The ripple effect of this lack of knowledge by the Judges is that the public tend to lose confidence in the judiciary when it comes to dealing with corporate governance matters thereby slowly eroding corporate governance which is seen as a golden goose that cannot be enforced even by the courts.

In South Africa, the High Court enjoys widespread jurisdiction with 14 divisions which are situated in different provinces. Some of these divisions are specific in nature as they deal with matters that relate to income tax, labour matters, divorce matters, land claims including equity court amongst others.¹⁷⁷ Over the past 18 years, corporate governance has registered record growth and massive movements which has no doubt faced numerous

¹⁷⁵ SARF Concept DOCT SA Regulation forum Document available at <http://docs.google.com/viewer?a=v&qwww.saregulators.co.za/docs/word/regulators> [Accessed 19th November 2012].

¹⁷⁶ OECD (note 95) 12.

¹⁷⁷ The various divisions of the Hugh Court are available at <http://www.justice.gov.za/about/sa-courts.html> [Accessed on 6th January 2013].

challenges in implementation and enforcement. However, it is disheartening to realise that there is no single division in the high court that is specifically dedicated to deal with corporate governance matters despite the concept having been adopted in 1994. Great importance has been attached to corporate governance as it is not only an empirical concept but is grounded on theory and practicality. This position was fortified as follows:

Corporate governance in South Africa changed from being a “soft” mainly ethical issue to a “hard” issue, recognised as pivotal to the success and revitalisation of the country’s capital markets and ultimately, the prospects of the corporate economy.¹⁷⁸

The high benchmarks that have been set emphasise the need for enforcement however the challenge still lies in the inefficiency of the courts to deal with corporate governance issues. It can further be argued that because of the major hype that attaches to corporate governance, it surely deserves an established forum where any contentious issues may be litigated and adjudicated upon by experts.¹⁷⁹

4.6 The voluntary nature of corporate governance codes

Despite various corporate governance principles being codified into law by the enactment of the companies Act, various other principles still remain uncodified. It is a mandatory requirement for all companies listed on the JSE to apply the provisions of the King III code and report accordingly, but all other companies are merely encouraged to adopt and apply the various principles. Therefore, ‘there is no statutory requirement for companies to apply the principles or provisions of the voluntary code.’¹⁸⁰ Because corporate governance initiatives and codes are not legally enforceable owing to their voluntary nature, most companies and organisations have been very reluctant to adopt and apply these principles as they are viewed as not necessarily being part of the law and thus noncompliance would not attach

¹⁷⁸ Malherbe S and Segal N (note 107).

¹⁷⁹ The former members of the King committee would stand out as the best candidates to becoming judges in corporate governance courts.

¹⁸⁰ Brian Coyle (note 2) 36.

any legal sanctions. This notion makes it easy for companies to fail or simply neglect to adhere to the principles.

Furthermore, various entities perceive corporate governance as an additional and unnecessary burden which only adds to the long list of mandatory laws and rules that need to be complied with by the company and due to its voluntary nature, corporate governance is given little or no consideration at all. For various businesses, complying with corporate governance practices imposes financial challenges as the cost of complying with the various other laws is already high thus corporate governance is seen as an added unnecessary and yet cost to the operations of the company. This obstacle to the implementation of corporate governance was fortified by the Asian Roundtable which tried to address various corporate governance concerns such as ‘...how to make corporate governance initiatives legally enforceable, as companies are reluctant to adopt practices going beyond the laws, considering the costs of compliance as already high enough.’¹⁸¹

From the above position it clear to see that the voluntary nature of corporate governance codes around the world, such as the King III report, still pose a challenge to the effective implementation of corporate governance principles.

4.7 Heavy reliance on regulatory bodies for enforcement

Shareholders of the company are vested with the right to receive dividends from the company in the event that these are declared which is a return on their investment. In order to secure this investment, shareholders appoint the board of directors who will be answerable to them. A serious problem that has been faced by corporate governance has been the reluctance of shareholders to institute investigations and assert their rights when it comes to questionable actions of the director opting to place too much

¹⁸¹ Andreas Griminger (note 172).

reliance on the various regulatory bodies. This position was fortified by the Asian Roundtable which provided that ‘ the passive nature of shareholders paired with a habitual reliance on government bodies to detect wrong-doing and initiate investigations puts the burden of enforcement solely on government bodies.’¹⁸²

This is also true for South Africa despite major calls for shareholders to act on their rights; most of them would rather depend on regulators such as the JSE and Financial Services Board for enforcement while they take a back seat in the face of flagrant disregard of rules and regulations.

In 2010 the JSE censured Cenmag [Ltd] and imposed a fine of R1million on each of the [company’s] directors for contravening section 3.84 of the listing requirements. Specifically Cenmag’s board of directors had no audit committee, the office of chairman and chief executive were not separate, the company had no full-time finance director, the chief executive served as chairman as well as finance director and company secretary. In addition no independent directors served on the board and the board had no remuneration committee....the listing requirements-particularly the corporate governance requirements safeguard the financial integrity of listed companies.¹⁸³

The directors of Cenmag Ltd appealed the decision of the JSE to impose a fine to the FSB which upheld the fines and added that accepting the approach taken by Cenmag’s directors would amount to lawlessness.¹⁸⁴ The question that one would pose is why the shareholders did not act on such irregular actions and what were they doing while all these wrongs were being committed? This is a clear manifestation of how passive shareholders can be when it comes to enforcement of corporate governance as most of them would rather burry their heads in the sand and only appear when dividends are being declared, which is a major challenge to the growth of corporate governance.

¹⁸² Ibid.

¹⁸³ Ann Crotty ‘JSE Listing Rules are binding, FSB Judges’ *Business Report*, (16th July 2012) 15.

¹⁸⁴ Ibid.

4.8 Complacent nature of shareholders

Shareholders are vested with tremendous amounts of power by virtue of their proprietary interests in the shares that they hold in the company. However, most shareholders seem not to be interested in anything else rather than earning profits at the end of the day which creates a problem for the implementation of corporate governance. Various recommendations were made by the King II report which are still existent in the current version of the King report which are aimed at improving and increasing shareholders involvement in the business embarked upon by the company. However, South Africa has for a long time been classified as a jurisdiction where the typical company AGM is carried out in under an hour which clearly shows the passive nature of shareholders as they do not exercise the powers vested in them by virtue of their position.¹⁸⁵ The complacent nature exhibited by shareholders has a very negative effect on the growth of corporate governance. This position was highlighted as follows:

[P]rimary governance responsibility lies in the board of directors. In formal terms the directors are appointed by and are accountable to the body of shareholders....the role of the shareholders is to exercise the powers that are reposed in them by the corporations Act and constitution of the corporation. The perceived wisdom is I think that shareholders play a passive role as the objects of corporate governance rather than an active role as part of it.¹⁸⁶

Therefore, the lack of interest by the shareholders of a company to take an active role in the affairs of their company is seen as an obstacle to the effective enforcement and implementation of corporate governance.

4.9 Compromised quality of leadership and related matters

In various jurisdictions, the board of directors is responsible for ensuring that the affairs of the company are managed in accordance with corporate governance principles. However, in Asia the role played by the board in

¹⁸⁵ Ramani Naidoo (note 3) 99.

¹⁸⁶ Justice Owen *Report of the HH Royal Commission* (Owen Report) available at https://www.hihroyalcom.gov.au/final_report/index.utmsection6.11. [Accessed on 18th November 2012].

enforcing corporate governance has faced various problems such as the lack of candidates to occupy the positions available on the board.¹⁸⁷

The small pool of candidates not only for the position of independent board members but also for senior managers was attributed to a lack of qualifications, inadequate fee structures and the small number of candidates in some Asian Jurisdictions....¹⁸⁸

This has resulted in compromising the quality of leadership that the board possesses as it will be composed of members who do not have the requisite qualifications to implement the various corporate governance needs of the company.

Asia has also faced challenges in addressing and promoting cumulative voting practices as there still remain some doubts as to the benefits of such practices in that most major players prefer the one share-one vote policy so as to avoid being overruled by majority shareholders who tend to vote systematically.¹⁸⁹

In addition, small companies have reportedly been constrained when it comes to the enforcement and establishment of committees which are aimed at promoting corporate governance. This scenario can be attributed to lack of financial resources and in some instances, a complete lack of knowledge on how to go about setting up the required committees.

The boards of State Owned Enterprises¹⁹⁰ have also continued to face major challenges when it comes to the implementation of corporate governance. The nomination process of the board members has recorded a lack of transparency in that appointments are perceived to be politically inclined and thus the managers become indebted to the politicians who tend to derive some form of benefit and power from these SOE's.¹⁹¹ Therefore, managers of most SOE's are answerable to the politicians in power who seek

¹⁸⁷ OECD (note 95) 12.

¹⁸⁸ Ibid.

¹⁸⁹ Ibid.

¹⁹⁰ Herein after referred to as SOE.

¹⁹¹ 'Reforming the Ceylon Electricity Board', *The Sunday times* 19th October 2008 available at <https://www.Sundaytimes.lk/081019/financialtimes/ft316.html> [Accessed on 26th November 2012].

to champion their own interests at the expense of various corporate governance stakeholders.

4.10 Disclosure Issues

Transparency is one of the fundamental principles in ensuring that good corporate governance structures are established and therefore should be strictly adhered to by all entities. The advantages of being transparent outweigh the disadvantages of acting in such a way. It enables the various stakeholders to gain clear information that is not manipulated or tainted with fiction with a view to distract the public from the real issues. However, many companies tend to prefer to disclose only positive matters about the company while the negative issues are swept under the carpet in an effort to keep them out of the public eye.¹⁹² This problem goes to the core of corporate governance because of the adverse effects it tends to have on public perception.

The convergence of local accounting principles (GAAP) with the internationally accepted accounting standards (IFRS) has brought about a different set of challenges to the implementation of corporate governance in that the new accounting regime are not cheap to execute which may be difficult for most small companies. Most of the costs that flow from the execution of IFRS are associated with enacting the accounting packages that are in line with the said standards. In addition, most jurisdictions do not have adequate numbers of skilled personnel to oversee the smooth implementation of these international accounting standards.¹⁹³

¹⁹² Naidoo (note 3) 213 refers to a situation that involved Tiger brands which opted to refute the negative issue regarding bread price fixing scandal in March 2007.

¹⁹³ OECD (note 95) 13.

4.11 Entrenched Management

Corporate governance has registered disappointing progress when it comes to penetrating management that has been firmly established over time and is old school in nature. This is mostly common for companies that are family owned and are motivated to maintain the “family tree” at the helm of the company at whatever cost.¹⁹⁴ In such companies, corporate governance is usually received with resistance and hostility in that it is perceived as a mechanism that is aimed at destabilizing and usurping their controlling power over the company. In essence, the corporate governance structures that exist in such companies are only effective on paper but will usually have no practical application when it comes to the real issues that affect corporate governance. This poses a real challenge to implementation and enforcement.

4.12 Conclusion

Having explored all of the possible demanding circumstances that could affect the implementation and enforcement of corporate governance, one can conclude that it is normal for any system to be faced with obstacles before it can start to operate smoothly. However from this chapter the question that still begs an answer is why do these challenges keep recurring 18 years down the line? It seems as if the turn of each year presents a new challenge that has evolved from the previous year’s stock of unresolved issues. Furthermore, one would ask if it is living up to the various expectations of the various proponents and stakeholders who depend upon its efficient running in order to sustain their businesses.

Therefore, there is need to rethink the true objectives of corporate governance in order to find a lasting solution. It is noteworthy that corporate governance has faced various challenges in all sectors of a company starting from the legal and regulatory frameworks, enforcement and disclosure.

¹⁹⁴ Ibid 5.

Shareholders rights have not been spared by the challenges together with the board which is the custodian of corporate governance. Looking on the bright side it can be said that all of these challenges faced are the residual effects of a functioning corporate governance structure and act as sign posts of the areas which require further attention.

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CHAPTER 5

5. CONCLUSION AND RECOMMENDATIONS

5.1 Conclusion

This paper has made an earnest attempt to take stock of the corporate governance progress and challenges in South Africa and the following conclusions can thus be drawn. The collapse of major multinational corporations in the early 1990's can be said to have been a blessing in disguise in that it provided the much needed impetus for the growth and development of corporate governance. As a result of the international trends that were moving towards adopting corporate governance principles and practices, South Africa was encouraged to take a critical look at its own corporate legislation and this resulted in a landmark revision of the law in order to be on par with the various corporate governance principles that existed around the world whilst at the same time implementing the recommendations made by the King II report.

After conducting a critical analysis of how the King II report has evolved into the King III report this paper has brought to the fore that major improvements have been achieved in corporate governance which makes South Africa's corporate governance system uniquely stand out from the rest of the world's corporate governance structures. This has been attributed to South Africa's sophisticated yet emerging market that promises new innovations every day. Unlike other corporate governance structures and systems that exist around the world, South Africa's corporate governance system has departed from the normal text book corporate governance as it possesses the qualities of a hybrid system which is the first of its kind in many respects. The hybrid nature of South Africa's corporate governance system can be attributed to the existence of a unique blend of a highly refined economic infrastructure and growing economic market that has nurtured an environment which is suitable for entrepreneurship and investment opportunities.

Since the publication of the King II report in 2002, South Africa has registered tremendous gains and changes which have come out in the form of the King III report and the enactment of the companies Act number 71 Of 2008. South Africa's steady growth and changes have been attributed to the consistent nature in which corporate governance issues have been handled by the King committee. The country has become the front runner and an authority in corporate governance matters because it has not change its winning formula even though at times it seemed as if the formula is not working. It is a delight to observe that South Africa has built on the various recommendations that were initially made by King I report through the publication of the King II and King III reports which have all seen the consistent use of the same working committee that seems to pick up from where they left off with each successive report and through the years have gained experience in dealing with the specific needs of the South African economy. In comparison, other corporate governance structures such as the UK have exhibited lack of consistency in handling corporate governance issues through the use of different committees with different ideologies and goals with respect to achieving an effective corporate governance structure. All in all, South Africa's corporate governance structure requires a standing ovation due to the consistent nature in which it has developed in such a short period of time. Furthermore, the compromise to encompass the needs of the various stakeholders through the triple bottom line concept can be seen as a remarkable achievement.

Ever since its conception in 1994, corporate governance in South Africa has continued to register steady growth and progress. The market has been cited as one of the most important agents of change that has necessitated its growth. Corporate governance operates in a market economy that is regulated by laws and regulations. In essence, corporate governance, the market and the law are the three aspects that cannot be unhinged from each other as they are interdependent in order to operate efficiently. Therefore, any change that occurs in any one of the three areas will have a domino effect on the other aspects due to the link that exists

between them. This paper has thus shown that corporate governance in South Africa does not operate in a vacuum and this is an aspect that was built on by the King committee which saw the integration of all of the stakeholders of corporate governance. Furthermore, any change in corporate governance principles will act as a stimulant for changing the corporate laws either through amendments or by way of regulations which play a pivotal role in the development of corporate governance.

Various areas of corporate governance have achieved prominence in the King I through to the King III reports. It is noteworthy that as a result of the King III report, companies are no longer incorporated with the short view of making profits for their shareholders but look beyond to include other stake holders and ensure the longevity of the company by ensuring that companies are sustainable in terms of profits and the way resources in the environment are utilised. An issue that emerges clearly during the course of this paper is that the progress that has been recorded cannot be measured empirically in that there is no set formula that can be used to measure the overall progress of corporate governance. Progress can thus only be looked at on a case by case basis, as what may be considered as progress in one jurisdiction may not necessarily be progress in another jurisdiction due to the difference in the pace at which it grows and also the difference in laws that exist in these jurisdictions.

The approach taken by this paper in assessing the overall progress has been more theoretical in nature and sometimes, where the need has arisen, the practical aspects have been examined in order to come up with a concrete position. The major areas that have been identified by this paper relate to the legal framework which has received a face lift. Areas of enforcement and implementation have also seen the introduction of new regulatory bodies. Moreover, some of the major players in corporate governance such as the shareholders have been given rights whilst at the same time enhancing the board's ability to handle corporate governance matters. Furthermore, the need for the board to be accountable to the shareholders has also taken the limelight with enhanced disclosure issues.

To sum up, one can conclude that South Africa has done quite well in scoring major successes which can be built upon from one year to the next in an effort to remain consistently at the forefront of the corporate governance pack.

Inasmuch as progress can be attributed to corporate governance in South Africa, its implementation and enforcement has not been all rosy and free from problems. This paper has approached the challenges and obstacles to corporate governance in the same vein as the progress in that it is difficult to confine the obstacles and challenges to an established empirical formula. However, these challenges have been looked at from a case by case basis and comparative aspects with other jurisdictions have been made in order to find the common threads that affect corporate governance from one jurisdiction to the next despite of the different systems that exist. Corporate governance has faced enormous challenges in the implementation and enforcement process whilst at the same time the shareholders have also contributed to the problems being faced due to their passive and inactive nature when it comes to dealing with corporate governance issues. Constraints in resources, skilled manpower and court systems have been seen as areas that pose challenges to the growth of corporate governance. In some jurisdictions the independence of boards (especially those of SOE's) and disclosure issues have been identified as obstacles to the growth of corporate governance.

Overall the progress that has been achieved outweighs the challenges being faced by corporate governance. The challenges should be viewed in a positive light in that they signify the areas of the existing corporate governance structures that need to be revisited and require more attention. They can thus be said to be a residual effect of a framework that is running and operating at full capacity. Any system that does not present challenges in its operations in the initial stages of implementation is at a great risk of grinding to a halt. Therefore, the challenges faced are healthy for any growing framework as they tend to act as signals as to the parts that require to be revisited in order to have a system that operates smoothly.

5.2 Recommendations

At the moment, South Africa's corporate governance framework seems to be operating smoothly despite the numerous glaring challenges that have been highlighted by this paper. In its current state, if it is left unchecked, the challenges which are being experienced could potentially escalate and become even more serious and destructive. Therefore, it is against this background that this dissertation makes the following recommendations to be considered by the policy makers for implementation:

- There should be an intensified campaign aimed at raising the awareness and activism of shareholders. There should be some sort of incentive for the shareholders to take an active role in the performance and operations of the company.
- Judicial reforms that are aimed at creating specialised courts that deal with corporate governance issues are long overdue. In addition, these should be presided over by judges who are well versed and experienced in corporate governance matters, for instance some of the members of King committee can make good candidates in this realm.
- The current cohort of judges should undergo intensive training coupled with vigorous programmes that are aimed at educating them on how best to deal with corporate governance matters.
- The importance of corporate governance to the life of any entity should be inculcated into the minds of 'lawyers in the making' at an early stage through expansion of commercial law programmes, both at undergraduate and postgraduate levels, thereby making it a priority and at the same time sufficiently equipping them to handle corporate governance issues in future.
- The corporate governance codes such as King III should be legally enforceable for all companies as opposed to restricting enforceability only to those companies that are listed on the JSE.

- There should be a reduction in government's involvement when it comes to SOE's whose focus should shift from serving the needs of politicians and encompass the various interests of other stakeholders as is required by the King report. In addition the various regulators of corporate governance should not be over-dependent on government as there should be some level of detachment from the government's invisible control.
- Providing intensive training for company secretaries who are the gate keepers of corporate governance and ensuring that these officers take a hands-on practical approach of ensuring that corporate governance principles are being adhered to instead of dealing with corporate governance as a paper based concept that lacks practicality. This will ensure vigilance and avoid companies from falling into bankruptcy.

Lastly, it is noteworthy that the above recommendations constitute just a fraction of the amount of work that remains outstanding as there are various areas that need attention in order to achieve a corporate governance framework that is formidable enough to withstand the test of time and any shockwaves that maybe experienced in future.

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