



Enforceable Accountability

A Corporate Governance Mirage for South African State-Owned Companies

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ABSTRACT

This research examines the operational and financial shortcomings of South African State-Owned Companies ('SOCs') which is shown to primarily stem from a lack of enforceable accountability.

The resolution of this accountability issue begins with the identification of SOCs. An analysis is undertaken of the predominant statutes with which SOCs are required to comply: the Public Finance Management Act and the Companies Act. An examination of these statutes, together with relevant case law and secondary sources, reveals contradictory, convoluted and confusing provisions relating to the definition and categorization of various State-Owned Enterprises ('SOEs') and SOCs. A complete overhaul of these statutory definitions and categorisations is required through the enactment of an overarching legislation to govern all aspects relating to all SOEs, under which SOCs will be subsumed, as was previously proposed by the Presidential Review Committee on State-Owned Entities in 2012.

The various accountability mechanisms, which should currently be implemented by SOCs, are analysed in terms of primary and secondary sources of law. This analysis divides the mechanisms into two distinct categories: internal and external mechanisms. Internal accountability mechanisms include: the directors, the board and its committees, the role of the company secretary and internal audit and the state, as the sole shareholder of the SOC. The external accountability mechanisms include: the external audit, the role of the Auditor-General and Public Protector, the legislature, the judiciary and the public, as the ultimate stakeholder of the SOC. Notwithstanding the availability of these accountability mechanisms, SOCs still fail to actually account for their continued underperformance.

Research conducted through a direct analysis and interpretation of the annual, integrated reports of South African Airways SOC Limited ('SAA'), from 2012 to 2017, will illustrate the inability of an SOC to effectively account for its performance. It is shown that one of the significant challenges which contributes to the accountability issue facing an SOC stems from the fact that the state is its sole shareholder. Evidence from this case study, together with that garnered from the investigation of the Zondo Commission of Inquiry into State Capture, will conclusively unveil the significant accountability issues experienced by many SOCs in South Africa. There is limited case law on the corporate governance and accountability of SOCs, however, an examination of secondary sources of law illustrates the growing trend for the board of an SOC to implement

corporate governance structures to achieve accountability. However, it is submitted that corporate governance, whilst popular, may not be the best method for achieving the accountability of SOCs.

A structured framework entailing the enforceable accountability of SOCs is proposed as a solution to the accountability issue through the implementation of a reward-based system which incentivizes the board of an SOC, and the state, to achieve real and significant accountability. This system requires the establishment of an independent rating agency which will rate the accountability of an SOC. The rating of the SOC will be linked to the provision of state funding, with maximum thresholds based on specific rating levels. The board of an SOC will retain the discretion of deciding which mechanism is to be instigated to attain actual accountability, of which corporate governance is just one method. The board of an SOC, and the state, will be incentivized to achieve a high rating level in order to secure preferential state funding.

This reward-based enforcement mechanism for the accountability of SOCs will require legislative reform through the enactment of overarching SOE legislation to govern all aspects relating to SOEs. In addition, legislation will be enacted to establish an independent rating agency, akin to the state institutions established under chapter nine of the Constitution. The implementation of an effective enforcement mechanism will result in the achievement of actual and significant accountability for SOCs which will ultimately improve their performance and reduce their reliance on the state's scarce resources.

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CHAPTER ONE: INTRODUCTION

1. Introduction

This research will focus on answering the legal issue of whether the accountability and performance of SOCs may be improved through the implementation of a legal, statutory and corporate governance reform. The definition and categorisation of SOEs and SOCs in South Africa will be fully set out in chapter two of this thesis. The current accountability mechanisms of SOCs, which is outlined in chapter three, may not be fully utilised or properly implemented which leads to an accountability issue. An examination into SAA under chapter four, as a case study, will provide a practical analysis of the possible accountability and financial performance challenges facing an SOC. A solution for the improved performance of SOCs, in the form of enforceable accountability, is then proposed. The concept of enforceable accountability for SOCs proposes a legal reform involving the enactment of certain statutes coupled with a reformed approach to accountability and the current corporate governance structures of SOCs.

1.1 Background

The South African economy has experienced sluggish progress over the last couple of years. The real Gross Domestic Product ('GDP') growth rate was recorded at 0.3 per cent for 2019 and was expected to increase to 0.9 per cent for 2020, however largely due to the impact of the global pandemic caused by the coronavirus, known as COVID19, the GDP growth rate plummeted to negative 7.2 per cent in 2020.¹

South Africa is home to over 700 SOEs, ranging from constitutional organizations to SOEs and SOCS of which the state is the partial or sole shareholder.² South Africa's economy is under enormous pressure to secure state funding and guarantees for numerous SOEs, including SOCs,

¹ National Treasury, Republic of South Africa 'Budget Review 2020' (2020) available at: <http://www.treasury.gov.za/documents/national%20budget/2020/review/FullBR.pdf>, accessed on 12 August 2020 at 7; National Treasury, Republic of South Africa 'Budget Review 2021' (2021) available at: <http://www.treasury.gov.za/documents/national%20budget/2021/review/FullBR.pdf> accessed on 27 February 2021.

² Pamela Mondliwa & Genna Robb 'SOEs and Competition: Reflections on South Africa's Experiences in the Telecommunications and Energy' (2018) *SSRN Electronic Journal* at 2.

which are not capable of financial independence.³ The national budget for 2020 projected the borrowing requirement for SOCs at approximately 1.3% per cent of overall GDP and in 2021 this has been reduced to 1%, however, this seems to be an unrealistic target given the current poor financial performance of SOCs.⁴

SOCs, such as Eskom SOC Limited ('Eskom') and SAA, have dual mandates comprised of both commercial and non-commercial objectives and are capable of being financially self-sustaining.⁵ However, with liabilities far outstripping their assets, resulting in a return on equity for the 2020 financial year of negative 7.9 per cent, SOCs have become more reliant on state funding which causes further strain on our limited resources.⁶

These SOCs have become huge borrowers of state funding, largely in the form of a provision of guarantees over the last decade with a total debt of R692.9 billion and in the next three years R182.2 billion is due to be repaid.⁷ These SOCs shift state funds away from other SOEs which do not have commercial mandates and are unable to be financially self-reliant.⁸ The improvement of the financial performance of SOCs is, therefore, of paramount consideration in order to alleviate the constrained national budget.⁹

It is submitted that a lack of accountability may contribute to the continued underperformance of many SOCs, with a specific focus on their financial performance.¹⁰ Despite many internal and

³Ibid at 2; Presidential Review Committee on State-Owned Entities (PRC) 'Growing the Economy – Bridging the Gap' (PRC) (2013) Available at http://www.gov.za/sites/default/files/gcis_document/201409/presreview.pdf, accessed on 13 August 2020 at 67 & 185.

⁴ National Treasury (2021) op cit note 1 at 38.

⁵ Lynn McGregor 'Can South African State-Owned Companies Succeed?' (2015) available at <http://portal.regenesys.net/course/discussions/editors/kcfinder/upload/files/McGregor%2C%20L.%202015.%20Can%20State%20Owned%20Companies%20succeed.%20USB.pdf>, accessed on 13 August 2020 At 1; PRC Protocol op cit note 3 at 3; National Treasury op cit note 1 at 89; Victoria Bronstein & Morne Olivier 'An Evaluation of the Regulatory Framework Governing State-Owned Enterprises (SOEs) in the Republic of South Africa' (Unpublished research paper, HSRC SOEs Research Project 43, 2011) at 2.

⁶ National Treasury (2021) op cit note 1 at 92.

⁷ Ibid at 92.

⁸ Ibid at 27.

⁹ Adele Thomas 'Governance at South African State-Owned Enterprises: What do Annual Reports and the Print Media Tell Us?' (2012) 8 *Social Responsibility Journal* 448 at 452; Thabane & Snyman Van-Deventer, Elizabeth 'Pathological Corporate Governance Deficiencies in South Africa's State-Owned Companies: A Critical Reflection' (2018) 21 *PER/PELJ* 1-32 at 13.

¹⁰ McGregor op cit note 5 at 1; Modimowabarwa Kanyane & Kombi Sausi 'Reviewing State-Owned Entities' Governance landscape in South Africa' (2015) 9 *African Journal of Business Ethics* 28-41 at 29; Thomas op cit note 9 at 458; Thabane op cit note 9 at 7; Olga Constantatos & Tarryn Sankar 'Futuregrowth Asset Management SOE Governance Unmasked, A Learning Journey' (2018) available at http://www.Futuregrowth.op.cit.note.10.co.za/media/3156/Futuregrowth_soe-governance-unmasked_electronic.pdf, accessed on 13 August 2020.

external measures, with which SOCs are required to comply, accountability remains a significant issue. The internal and external accountability measures available to SOCs will be fully described under chapter three of this thesis. The predominant statutes which govern SOCs are the Public Finance Management Act 1 of 1999 ('PFMA') and the Companies Act 71 of 2008 ('Companies Act'), the Constitution of the Republic of South Africa, 1996 ('Constitution') as well as its own founding legislation.¹¹ The internal accountability measures include: the directors, the board and its committees, the state (as shareholder), the internal audit and the company secretary.¹² External accountability measures include: the external audit and Auditor-General, the Public Protector, the legislature, the judiciary and the public.

This lack of accountability of SOCs has received notable media attention and, following the modern concept of stakeholder inclusivity (which will be more fully defined in Chapter Three), the stakeholders of SOCs, specifically the public as taxpayers and not just the state as the sole shareholder, play an important supervisory role by overseeing the performance of SOCs.¹³ In response to this attention, the state established the judicial commission of enquiry into allegations of state capture, corruption and fraud in the public sector, headed by Deputy Chief Justice Raymond Zondo ('Zondo Commission').¹⁴ The Zondo Commission is mandated to investigate SOCs, with a focus on directors who have allegedly committed breaches of their legislated duties and the state who is meant to supervise the SOC, as its sole shareholder.¹⁵ Together with a report from the Public Protector ('State Capture Report'), the Zondo Commission has uncovered huge accountability failures by numerous SOCs.¹⁶

¹¹ The Public Finance Management Act 1 of 1999; The Companies Act 71 of 2008; The Constitution of the Republic of South Africa Act 8 of 1996.

¹² The Bronstein & Oliver op cit note 5.

¹³ Thomas op cit note 9 at 450; Patricia Makoni 'The Challenges of 'Acting' CEOs in State-Owned Enterprises: the Case of South African Airways' (2015) 11 *Corporate Board: Role, Duties & Composition* 16 at 16.

¹⁴ Terms of Reference of the Judicial Commission of Inquiry to Inquire into Allegations of State Capture, Corruption and Fraud in the Public Sector including Organs of State, Proclamation No. 3 of 2018 by the President of the Republic of South Africa in GG 41403 of 25 January 2018.

¹⁵ Ibid.

¹⁶ Commission of Inquiry into State Capture 'Hearings, recent' available at <http://www.statecapture.org.za/site/hearings>, accessed on 14 August 2020; Thulisile Madonsela 'State of Capture' Public Protector South Africa (2016) report No. 6 of 2016/2017 available at <http://www.saflii.org/images/329756472-State-of-Capture.pdf>, accessed on 12 August 2020.

Under the investigation proceedings, SAA has been highlighted as an SOC with many accountability issues.¹⁷ Notwithstanding numerous legislated measures, with which the directors of SAA are meant to comply, continued and consistent accountability failures, over the last decade, have contributed to airline's voluntary institution of business rescue proceedings in December 2019.¹⁸

In addition to the legislated measures, voluntary corporate governance recommendations have been suggested which SOCs should apply, in order to achieve accountability. In South Africa, the corporate governance of SOCs is dominated through the application of the recommended practices encompassed under the King Reports and Codes on Corporate Governance for South Africa ('King Codes'), the most recent of which code is the King IV Report on Corporate Governance for South Africa ('King IV').¹⁹

However, despite the alleged application of the recommended practices under King IV by SOCs, such as SAA, their accountability remains an issue. From an analysis and interpretation of SAA's annual integrated reports, for the financial year-ends from 2013 to 2017 ('SAA Reports'), it becomes apparent that one of the main issues facing this SOC is the lack of an appropriate enforcement mechanism to ensure its accountability which may have contributed to its poor financial performance.²⁰

¹⁷ Ibid; Ngatane, N 'Zondo Commission hears testimony from PWC auditor on SAA finances' (2020) available at <http://ewn.co.za/2020/07/16/zondo-commission-hears-testimony-from-pwc-auditor-on-saa-finances>, accessed on 14 August 2020.

¹⁸ South African Airways SOC Limited 'SAA to enter into Business Rescue' 5 December 2019 available at <http://www.flysaa.com/about-us/leading-carrier/media-center/media-releases/newsroom>, accessed on 14 August 2020; Thembekile Kimi Makwethu 'PFMA Consolidated General Report on National and Provincial Audit Outcomes 2018-2019' (2019) Auditor-General South Africa available at <http://www.agsa.co.za/Portals/0/Reports/PFMA/201819/GR/2018-19%20PFMA%20Consol%20GR.PDF>, accessed on 12 August 2020; Makoni op cit note 13 at 16.

¹⁹ Institute of Directors Southern Africa (IODSA) *The King Report on Governance for South Africa*. (2016) Johannesburg: IODSA (King IV) at ch 6.

²⁰ South African Airways SOC Limited 'Annual Integrated Report 2013' (2014) available at: <http://www.flysaa.com/documents/51855150/51859528/SAA+Annual+Report+2013.pdf/557e81fd-f531-4596-9853-e079d2d937c4>, accessed on 14 August 2020; South African Airways SOC Limited 'Annual Integrated Report 2014' (2015) available at: <http://www.flysaa.com/documents/51855150/51859528/SAA+Annual+report+2014.pdf/89fba6a8-5fe8-412d-8ee0-f659f92f5471>, accessed on 14 August 2020; South African Airways SOC Limited 'Integrated Annual Report 2015' (2016) available at <http://www.flysaa.com/documents/51855150/51859528/SAA+IAR+2015.pdf/a2f72b91-0dde-4c5f-b3aa-6ed7dc6f4726>, accessed on 14 August 2020; South African Airways SOC Limited 'Annual Integrated Report for year-ended 2016' (2017) available at <http://www.flysaa.com/documents/51855150/51859528/SAA+IAR+2016.pdf/0276a1d0-2848-41bc-a62c-2a5a624605c5>, accessed on 14 August 2020; South African Airways SOC Limited 'Annual Integrated Report for year-ended March 2017' (2018) available at:

Currently, in order to enforce the accountability of SOCs, a combination of retributive and reward-based systems have been implemented but with little success.²¹ Reform of the accountability of SOCs seems inevitable and the focus on enforceability is central to improving their accountability which may lead to better future performance. The legal reform of SOCs through statutory enactments and a different approach to accountability, in comparison to the predominant current approach of corporate governance, is proposed in this research. The premise of this legal reform is that the implementation of a framework for the enforceable accountability of an SOC will serve to improve their future performance.²²

1.2 Primary Research Question and Secondary Research Objectives

As a result of the accountability and performance issues facing SOCs, the following primary research question is addressed in this thesis:

- Whether the accountability and performance of SOCs may be improved through the implementation of a legal statutory and corporate governance reform.

From this primary research question, the following secondary research objectives arise, which are addressed sequentially in the chapters of this thesis:

- To understand how SOCs are defined and categorised through South African legislation;
- To evaluate the current accountability measures which are available for utilisation by SOCs;
- To ascertain the accountability and performance issues facing an SOC where SAA is utilised as the case study;
- To examine how accountability is achieved through the current corporate governance regime in South Africa, with reference to SOCs and to identify any shortcomings in this regime; and

http://www.flysaa.com/documents/51855150/0/SAA_IAR+2017.pdf/22db54be-b1f5-404a-99fd-d12f3fe9e56b, accessed on 14 August 2020 (“SAA Reports”).

²¹ Thabane op cit note 9 at 23.

²² Pricewaterhousecoopers South Africa ‘State-Owned Enterprises: Catalysts for Public Value Creation’ (2015) available at <http://www.pwc.com/gr/en/publications/assets/state-owned-enterprises-catalysts-for-public-value-creation.pdf>, accessed on 13 August 2020; Organisation for Economic Co-operation and Development ‘South Africa Policy Brief: Corporate Governance State-Owned Enterprise Reform’ (2015) Available at <http://www.oecd.org/policy-briefs/south-africa-state-owned-enterprise-reform.pdf>, accessed on 13 August 2020; Thomas op cit note 9 at 449.

- In light of the accountability and performance issues facing SOCs, to propose a legal statutory and corporate governance reform of SOCs to implement enforceable accountability which may serve to improve future performance.

1.3 Methodology

The methodology of this research is comprised mainly of a desktop study involving an interpretation and analysis of primary and secondary sources of law. The following table will identify the methodology adopted in this research using the relevant chapters for reference:

Chapter	Methodology
Chapter One	Introductory chapter which sets out a background to the research issue, the primary and secondary research questions, assumptions made and the justifications for the research.
Chapter Two	An examination of South African statutes to determine the legal definition of SOCs and SOEs in South Africa.
Chapter Three	A description of the accountability mechanisms for SOCs based on an examination of primary and secondary sources of law.
Chapter Four	A case study of SAA to illustrate accountability and performance issues facing an SOC based on an analysis and interpretation of the SAA Reports.
Chapter Five	A description and analysis of the corporate governance regime of SOCs using primarily secondary source of law.
Chapter Six	A proposed legal framework for the enforceable accountability of SOCs by describing a legal and corporate governance reform and using foreign comparatives where necessary.

Chapter Seven	Provides a conclusion to the thesis by describing possible reform and suggesting recommendations.
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1.4 Assumptions

There are various assumptions made in this research in order to answer the primary research question and address the secondary research objectives. First, there is a specific focus on SOCs as opposed to all SOEs in South Africa. The focus on SOCs as opposed to all SOEs is to narrow the scope of the research to identifying the accountability and performance issues facing SOCs which cause a significant drain on state resources due to their increased reliance on state funding as a result of their poor financial performance. Many SOEs are reliant on state funding due to their solely non-commercial mandates and there is little possibility to reform these SOEs to become financially self-reliant and ease the burden on state funds.²³ Such SOEs will always be state funded and therefore the focus of this research is on SOCs which, if reformed, are capable of being financially independent from the state.²⁴

The SOCs which form the focus of this research are ones which discharge dual commercial and non-commercial mandates. The commercial mandates of SOCs will form the specific focus of this research as opposed to a focus on the achievement of their non-commercial mandates. SOCs with commercial mandates are highlighted in this research as an improvement of the financial performance of these SOCs may alleviate their reliance on state funding, which is a scarce resource.²⁵

In order to avoid confusion, any reference in this thesis to an SOE indicates a ‘state-owned entity’ which is a broad definition encompassing all entities which are partially or wholly owned by the state, including enterprises, organisations, departments and companies. Any reference to an SOC indicates only those ‘state-owned companies’ which are defined as such, in accordance with the provisions of the Companies Act and the PFMA.²⁶ Furthermore, although SOCs fall under the

²³ Robb op cit note 2.

²⁴ Bronstein & Oliver op cit note 5 at 11.

²⁵ National Treasury (2020) op cit note 1; Sunita Menon ‘SAA Continues to Stretch the National Purse’ *Business Live* 19 April 2018 available at <http://www.businesslive.co.za/fm/features/2018-04-19-saa-fiasco-continues/>, accessed on 14 August 2020.

²⁶ PFMA op cit note 11; Companies Act op cit note 11.

portfolio of different ministers, the Minister of Public Enterprises will be referred to as the Minister throughout this thesis, to avoid confusion, and the SOCs, in reference such Minister, are the ones falling under the purview of the Department of Public Enterprises and the Minister.

Secondly, SAA will be utilized as the case study to illustrate the accountability failures plaguing SOCs which may be a predominant contributing factor to their poor financial performance. The rationale for the use of SAA is due to its recent initiation of business rescue proceedings and its historic ability to be financially independent from the state. SAA has recently entered into business rescue - as the first South African SOC to have done so, it is important to examine the possible causes for this initiation into business rescue.²⁷

SAA was financially independent from the state until 2012 when it became reliant on state funding to continue its operations.²⁸ Therefore, SAA has the ability to discharge its commercial mandate which may take precedence over its non-commercial mandate and allow the SOC to be financially independent from the state, as was arguably the case prior to 2012.²⁹ Other SOCs, such as Eskom, are required to discharge a burdensome non-commercial mandate, on behalf of the state which may be prioritised over their commercial mandate.³⁰ This would mean that their financial reform will prove a much more difficult and complicated task.

The third assumption of this research relates to the use of accountability throughout this thesis. The definition and concept of accountability will be fully explained in chapter three. This research refers to accountability on a broad spectrum as a principle which may be achieved through various mechanisms. The most popular method of achieving this principle for SOCs in South Africa is the adoption of corporate governance structures. Therefore, accountability is discussed with specific reference to corporate governance in chapter five. However, accountability is referred to in general terms as a principle which may be achieved by an SOC on a standalone basis or under the umbrella of its corporate governance regime, depending on the requirements of the specific SOC. Unless specifically referred to in this research, accountability remains a broadly defined principle and not as specifically referred to in corporate governance.

²⁷ SAA op cit note 18.

²⁸ SAA Reports op cit note 20. Kanyane op cit note 10 at 30; Thabane op cit note 9 at 4; Thomas op cit note 9 at 453.

²⁹ Kanyane op cit note 10 at 30.

³⁰ Department of Minerals and Energy 'Electricity Basic Services Support Tariff (Free Basic Electricity)' in GN 1693 GG 25088 of 4 July 2003.

The fourth assumption relates to the performance of an SOC. In this research the performance of an SOC is referred to on numerous occasions. The performance of an SOC is couched in general terms to refer to a holistic view of performance including: managerial, operational, corporate, financial, and structural performance.³¹ However, due to the case study on SAA where the financial performance of the SOC is examined, there is an emphasis on the financial performance of SOCs in reference to the discharging of their commercial mandates in order to maximize shareholder wealth. Where specifically referred to, financial performance will be stated, otherwise, the performance of an SOC refers to its general performance from a holistic perspective as described in this paragraph.

Lastly, throughout this thesis one of the internal accountability measures of an SOC is differentiated into the directors, the board and its committees. While this differentiation may seem redundant, it is made due to the separate duties which the PFMA and the Companies Act place on the board, as a collective body, and the directors, on an individual basis. Therefore, in order to better analyse the different duties and accountability mechanisms of an SOC, the differentiation is made.

1.5 Relevance of the Research

The justifications for this research are from an academic and socio-economic standpoint. From an academic perspective, the implementation of a novel enforceable accountability framework for SOCs provides a knowledge contribution. From a socio-economic standpoint, the implementation of enforceable accountability may improve the accountability and performance of SOCs which will positively impact the economy.

1.5.1 Academic Justifications

A valuable knowledge contribution to the field of commercial law is central to the examination of, and proposed solution to, the poor performance of South African SOCs. The primary knowledge contribution is the proposed concept of enforceable accountability, as a potential solution for the accountability and performance of SOCs. Enforceable accountability is implemented through the creation of an independent rating agency which creates an incentive for SOCs to perform as the provision of state funding is linked to the rating score achieved by the SOC. The rating agency

³¹ Magda Bezuidenhout et al 'The chief executive officer pay-performance relationship within South African state-owned entities' (2018) 16 *South African Journal of Human Resource Management* 1 -13.

rates the SOC based on an accountability scorecard which is more fully detailed and set out in chapter six of this thesis.

While the use of an independent rating agency to assess the performance of SOCs has been attempted in international jurisdictions, the creation of such an agency in the context of South African SOCs is, arguably, a novel concept. Furthermore, linking the outcome of the rating to the provision of state funding is innovative in establishing a reward-based mechanism for South African SOCs.

In an examination of the primary knowledge contribution to the field of commercial law, three secondary academic justifications for this research are also contributed:

Firstly, the statutory duties with which directors of SOCs must comply are complex and contradictory and lack a duty to account. An overarching SOE Legislation will address this issue by amalgamating and codifying the duties, thereby removing unnecessary duplications and contradictions and providing the insertion of an enforceable duty to account. The SOE Legislation will also contain certain mandatory provisions with which SOCs must comply which have been proposed in chapter six.

Secondly, a case study of SAA is used to showcase the possible accountability issues and financial performance of an SOC through an interpretation and analysis of the SAA Reports. This analysis is conducted through a direct examination of the SAA Reports and is not based on any other secondary source of law, such as an article or opinion, which provides a similar summary or analysis.

Thirdly, despite comprehensive corporate governance recommendations, set out in King IV and the Protocol on Corporate Governance in the Public Sector ('Protocol'), SOCs still exhibit a lack of accountability.³² The proposed scorecard to be implemented by the rating agency is largely based on criteria specifically designed to achieve the principle of accountability which may be achieved on a standalone basis or under the popular approach of utilising corporate governance methods.³³ The enforceable accountability of SOCs, through the accountability scorecard, is

³² Kanyane op cit note 10 at 32; Thabane op cit note 9 at 9; Thomas op cit note 9 at 450; PRC *Protocol* op cit note 3 at 139; King IV op cit note 19 at ch 6.

³³ Juergen D Gloeck 'Corporate Governance: light years behind accountability' (2005) University of Pretoria: Department of Auditing.

proposed to transcend the ‘tick box’ approach to the application of the numerous recommended practices suggested in King IV and the Protocol.³⁴

1.5.2 Socio-Economic Justifications

There are primarily three significant socio-economic justifications for implementing the concept of enforceable accountability for SOCs.

The first primary justification focuses on the state’s limited resources in a developing country. With a deteriorating economic outlook, the state can ill afford any unnecessary expenditure.³⁵ In light of the state’s constrained resources, state funding should be provided on an exceptional basis to SOCs and supervision of the expenditure of those funds is essential.³⁶

The implementation of a rating agency, which links the rating score of an SOC to the provision of state funding, will provide an incentive-based enforcement mechanism for the accountability of SOCs. This causal link will focus on the provision of state funding to SOCs exhibiting good accountability and, arguably, assist in decreasing the unnecessary expenditure of the state’s limited resources to financially underperforming SOCs. This implementation will also assist in the state’s supervisory role over any state funding which is provided to SOCs as it will be linked to the accountability scorecard. In addition, the state will have more available resources to assist SOEs which are not capable of being financially self-sufficient.³⁷

The second justification for this research stems from the significant effect which underperforming SOCs have on the economy. The status of the South African economy has deteriorated significantly, with all of the prominent credit rating agencies recently downgrading its creditworthiness to sub-investment status.³⁸ One of the predominant factors leading to the inevitable downgrade was the numerous allegations of corruption coupled with the state of SOCs

³⁴ Jess Schulschenk ‘Interview Summary Report’ *Corporate Governance Research Programme Albert Luthuli Center for Responsible Leadership* (2012) available at <http://citeseerx.ist.psu.edu/viewdoc/download;jsessionid=68F22977B4B9767319AEC519D9869F1E?doi=10.1.1.39.3.5505&rep=rep1&type=pdf>, accessed on 13 August 2020.

³⁵ Futuregrowth op cit note 10 at 3.

³⁶ Thomas op cit note 9 at 451; Kanyane op cit note 10 at 34.

³⁷ McGregor op cit note 5 at 9; Thomas op cit note 9 at 449; Thabane op cit note 9 at 5.

³⁸ Feddersen, M ‘Rating Agencies to Focus on Three Priorities in October’s budget statement’ Pricewaterhousecoopers (2019) available at <http://www.pwc.co.za/en/press-room/rating-agencies.html>, accessed on 14 August 2020; Paul Wallace ‘The price SA will pay for being downgraded to junk’ *BusinessDay* 31 March 2020 available at <http://www.businesslive.co.za/bd/economy/2020-03-31-the-price-sa-will-pay-for-being-downgraded-to-junk/>, accessed on 15 August 2020.

resulting from their underwhelming performance over the last decade.³⁹ Improving the accountability of SOCs may assist in the fight against corruption and circumvent the squandering of limited state resources which may ultimately improve the performance of SOCs and South Africa's creditworthiness rating.

The third justification relates to the detrimental impact which state funding to a financially underperforming SOC may have on competitive neutrality.⁴⁰ State subsidization for SOCs which are capable of performing financially may perpetuate their monopolistic positions which negatively impacts competitive neutrality in the industry in which that SOC operates.⁴¹ Private counterparts, in the same industry sectors as these SOCs, are not afforded the same opportunity when they become financially and commercially insolvent.⁴² Utilizing state funds for SOCs which would otherwise be insolvent, is, arguably, tantamount to an unfair, uncompetitive practice.⁴³ An economy which fosters competitive neutrality is a key concern for foreign investors who may be deterred from making investments in South Africa.⁴⁴

1.6 Chapter Overview and Conclusion

1.6.1 Chapter One: Introduction

Chapter One comprises an introduction for the topic of thesis. The introductory aspects include: a background to the topic, setting out primary and secondary legal questions, assumptions made, the methodology utilized, the justifications and relevance of the research and a chapter overview.

1.6.2 Chapter Two: The Definition of SOCs

Chapter Two provides an examination into the identification and categorization of SOCs in South Africa, in accordance with predominant legislation.⁴⁵ A distinction is drawn between the differing classifications of SOEs and SOCs as a result of compliance with respective legislative instruments. All SOEs, of which SOCs comprise a distinct category, are governed primarily by the PFMA, the

³⁹ Ibid.

⁴⁰ Organisation for Economic Co-operation and Development 'Competitive Neutrality and State-Owned Enterprises Challenges and policy options' (2011) available at <http://pdfs.semanticscholar.org/59db/654b668fc2c8f8e08bd39489af2e4b32b567.pdf> accessed on 15 August 2020 at 4.

⁴¹ Ibid at 4 – 5.

⁴² Ibid.

⁴³ Ibid.

⁴⁴ Ibid.

⁴⁵ Robb op cit note 2 at 2; Thabane op cit note 9 at 4.

Constitution and their own founding legislation.⁴⁶ However, SOCs, as a defined and distinct category of SOEs, are also subject to the Companies Act.⁴⁷

There are numerous discrepancies between the various statutes which results in confusing and contradictory definitions of SOEs and SOCs. The promulgation of an overarching SOE Legislation to govern all aspects relating to SOEs, as previously suggested by the Presidential Review Committee on State-Owned Entities in 2012, is a priority which must now be actioned.⁴⁸ The SOE Legislation will amalgamate provisions of the existing legislation to avoid unnecessary duplications and remove any contradictions.⁴⁹ The identification and categorization of SOEs and SOCs will be updated, clear and simple which will improve compliance costs.

1.6.3 Chapter Three: The Accountability of SOCs

Chapter three will set out an analysis of the current theoretical accountability mechanisms available to SOCs. In this chapter the accountability mechanisms are categorized into various internal and external measures. An overview of the internal accountability measures includes: the directors, the board and its committees, the roles of the internal audit and company secretary and the state, as shareholder. The primary external accountability measures include: the external audit, the offices of the Auditor-General and Public Protector, the roles of the judiciary and legislature and the public.

1.6.4 Chapter Four: A Lack of Accountability for SOCs

Chapter four provides a detailed analysis of the current accountability and performance issues facing SAA, as a case study of an SOC. The conclusions from this chapter, in respect of the accountability failures and poor financial performance of SAA, are drawn from an interpretation and analysis of the SAA Reports.⁵⁰

1.6.5 Chapter Five: Corporate Governance of SOCs.

Chapter five comprises an examination of the corporate governance measures adopted by SOCs as the current, primary method utilised by SOCs to achieve the principle of accountability. An

⁴⁶ PFMA op cit note 11; The Constitution op cit note 11.

⁴⁷ Companies Act op cit note 11.

⁴⁸ Kanyane op cit note 10 at 32, PRC op cit note 3 at 9.

⁴⁹ Ibid.

⁵⁰ SAA Reports op cit note 20.

analysis of the current enforcement mechanisms utilized by SOCs to achieve accountability is undertaken. The effectiveness of the enforcement mechanisms employed by SOCs, encompassing elements of both reward and retribution-based systems, are also examined. The outcome of this examination begets reform based on the implementation of the concept of the enforceable accountability of SOCs.

1.6.6 Chapter Six: Enforceable Accountability

Chapter six proposes a solution to the accountability issues facing SOCs, in the form of legal and corporate governance reform to implement an innovative enforcement mechanism. The enforcement mechanism provides for the annual rating of the accountability of SOCs by an independent institution. The accountability of SOCs will be measured in accordance with uniform categories which are stipulated on a proposed scorecard to be utilized by the rating agency. The provision of state funding to the SOC will be based on its rating and maximum thresholds and terms and conditions will be set.

The statutory reform which is required for SOCs is threefold. First, an amendment to the Constitution to include the rating agency as an independent state institution, akin to the office of the Public Protector or Auditor-General.⁵¹ Secondly, the enactment of a proposed Rating Agency Act ('Rating Agency Act') to govern all aspects relating to the powers and duties of the rating agency. Thirdly, the re-iteration of the proposal made by the Presidential Review Committee on State-Owned Entities in 2012 that an overarching SOE Legislation must be enacted to govern all aspects relating to SOEs, which will include SOCs.⁵² The inclusion of certain proposed statutory provisions of the SOE Legislation are set out in this chapter. The reform to the governance of SOCs is proposed in the form of a specific focus on the achievement of accountability, as a broader, standalone principle and not necessarily defined and implemented through corporate governance structures.⁵³ This SOC reform will address many of the accountability issues facing SOCs, such as SAA, which are highlighted in chapter four of this thesis.

⁵¹ Constitution op cit note 11 at ch 9.

⁵² PRC op cit note 3 at 9.

⁵³ Gloeck op cit note 33.

1.6.7 Chapter Seven: Conclusion

Chapter seven provides possible recommendations to the accountability issues currently faced by SOCs with the implementation of a rating agency as an enforcement mechanism and the inclusion of proposed statutory provisions for the SOE Legislation. SOCs with good ratings will be given preferential funding by the state which incentivizes the board of an SOC to ensure the implementation of effective accountability measures. The improved accountability of SOCs, due to the implementation of enforceable accountability, may lead to their better future financial performance which will alleviate their significant drain on state resources and help improve the economy. Any possible issues with the implementation of these recommendations will also be addressed in this chapter which then ends with concluding remarks.

CHAPTER TWO: THE DEFINITION OF SOCS

2 Introduction

South African SOEs comprise a range of organisations, entities, enterprises, boards, tribunals, companies and commissions which are either partially or wholly owned by the state, on a municipal, provincial or national level.⁵⁴ The scope of this research is focused on the category of SOEs which are defined as SOCs in terms of the Companies Act read together with the PFMA.⁵⁵ These SOCs, such as SAA, discharge commercial mandates and are categorized as ‘major public entities’ under schedule 2 of the PFMA. The predominant pieces of legislation with which these SOCs must comply are the PFMA, the Companies Act and their own founding legislation. Compliance with multiple pieces of legislation makes the identification and categorization of SOEs and SOCs overly complicated. This is remedied by the reiterated proposal of an overarching SOE Legislation which governs all aspects related to SOEs and SOCs.⁵⁶

2.1 The Background Logistics of SOCs

The exact identification of an SOC is important as it will determine the legislation with which its board of directors must comply. All SOCs are subject to the provisions of the Companies Act and the PFMA.⁵⁷ All SOEs, which are not defined as SOCs, are subject to the provisions of the PFMA but not the Companies Act. Both SOEs and SOCs are subject to the provisions contained in their own founding legislation and the Constitution.⁵⁸

Given the legal minefield to which SOEs and SOCs are subject, their definition and classification has never been a settled issue.⁵⁹ At the advent of the constitutional democracy, after the 1994 general elections, it was found that many public policy functions were discharged by SOEs on behalf of the state.⁶⁰ SOEs were not definitively identified in legislation and their direction and control by the government varied on a case by case basis and was also largely determined by the

⁵⁴ Robb op cit note 2.

⁵⁵ Companies Act op cit note at section 1; PFMA op cit note 11 at sections 1 & 3(b) & sch 2.

⁵⁶ PRC op cit note 3 at 9.

⁵⁷ Kanyane op cit note 10 at 32; Pricewaterhousecoopers & Institute of Directors South Africa ‘State-Owned Enterprises: Governance Responsibility and Accountability Public Sector Working Group Position Paper’ (2011) available at http://cdn.ymaws.com/www.iodsa.co.za/resource/collection/879CAE6C-7B90-49F5-A983-28AECBCE196F/PSWG_Position_Paper_3_Governance_in_SOEs.pdf, accessed on 15 August 2020 at 6.

⁵⁸ Kanyane op cit note 10 at 32; PWC op cit note 22 at 6; Bronstein & Oliver op cit note 5 at 11; Constitution op cit note 11 at section 2.

⁵⁹ PRC *Protocol* op cit note 3 at 3.

⁶⁰ *Ibid.*

specific mandates with which they were required to discharge.⁶¹ The need for reform and the specific identification of SOEs was required, as the by-then outdated Companies Act 61 of 1973 ('1973 Companies Act') remained the only mechanism through which to incorporate companies in South Africa.⁶²

Although the 1973 Companies Act made no specific reference to the categorization of a 'State-Owned Company', it did allow for the formation of companies and, therefore, by inference, for the possibility of an SOC.⁶³ Under the 1973 Companies Act, two types of companies could be formed: 'a company having share capital or a company not having a share capital and having the liability of its members limited by the memorandum of association.'⁶⁴ A company having a share capital could be a public or a private company having par value or no par value shares. A public company, whose majority or sole shareholder was the state could be referred to as what is now known as an SOC.⁶⁵ However, no provision for the specific definition of a 'state-owned company' was contained in South African legislation.⁶⁶

The lack of legislative requirements for the identification and formation of SOEs, given their relative importance in the economy, gave way to implementation of the PFMA.⁶⁷ The PFMA was promulgated in 1999 and came into effect on 1 April 2000.⁶⁸ One of the main reasons for the enactment of the PFMA was to give effect to certain provisions encapsulated in the Constitution which came into effect in 1996.⁶⁹ The provisions in the PFMA are intended to complement and support the principles enshrined in the Constitution, with respect to the provincial and national

⁶¹ Ibid.

⁶² The Companies Act 61 of 1973.

⁶³ Ibid; Farouk Cassim et al *Contemporary Company Law* 2ed (2012) at 84; Wiese, Tobie. *Corporate Governance in South Africa with International Comparisons* 2ed (2017) at 88.

⁶⁴ Companies Act op cit note 77 at section 19.

⁶⁵ Bronstein & Oliver op cit note 5 at 8; Airports Company South Africa SOC Ltd 'Legal Structure' Available at: <http://www.airports.co.za/about-us/airports-company/company-profile>, accessed on 13 August 2020; Airports Company Act 44 of 1993.

⁶⁶ PRC *Protocol* op cit note 3 at 3.

⁶⁷ PWC op cit note 22 at 3.

⁶⁸ PFMA op cit note 11; PWC op cit note 22 at 3.

⁶⁹ Constitution op cit note 11.

spheres of government.⁷⁰ All SOEs, regardless of their nature, are subject to the provisions of the Constitution as the overarching and supreme law of the Republic.⁷¹

The PFMA is the overarching piece of legislation which pertains to all provincial and national SOEs and its main object is to provide guidance and enforce compliance, primarily in relation to the financial management of the institutions to which it applies.⁷² Municipal systems are governed by the Local Government: Municipal Systems Act 32 of 2000 and the Local Government Municipal Finance Management Act 56 of 2003 ('MFMA').⁷³ The provisions in the Local Government Municipal Finance Act largely mirror those of the PFMA in respect of the financial management of municipal SOEs.⁷⁴

The Companies Act came into effect in May 2011 and provided a welcomed statutory definition of a 'State-Owned Company'.⁷⁵ The Companies Act was considered a progressive piece of legislation and sought to align South African corporate law with that of international trends.⁷⁶ All companies which are incorporated and registered in South Africa, including SOCs, are subject to the provisions of the Companies Act.⁷⁷ All SOCs are subject to the enhanced accountability and transparency requirements, embedded in chapter three of the Companies Act, unless an exemption has been granted by the Minister of Public Enterprises ('Minister').⁷⁸

2.1.1 The PFMA

Due to their utilization of public funds, the state saw fit to hold SOEs to much higher level of scrutiny, hence the enactment of the PFMA for provincial and national public entities and the MFMA for municipal entities.⁷⁹ The focus of this research is on SOCs which are defined as

⁷⁰ Pricewaterhousecoopers 'State-Owned Companies: The New Companies Act, PFMA and King III in Perspective' (2012) available at <http://www.pwc.co.za/en/assets/pdf/companies-act-steering-point-4.pdf>, accessed on 15 August 2020 at 3; Companies Act op cit note 11; PFMA op cit note 11.

⁷¹ Constitution op cit note 11 at section 2.

⁷² PFMA op cit note 11 at section 2.

⁷³ MSA, Local Government: Municipal Finance Management Act 56 of 2003; Local Government: Municipal Systems Act 32 of 2000 as amended by Municipal System Amendment Act 44 of 2003.

⁷⁴ PWC op cit note 70 at 4.

⁷⁵ Cassim op cit note 63 at 2.

⁷⁶ Cassim op cit note 63 at 4.

⁷⁷ PWC op cit note 70 at 6.

⁷⁸ Companies Act op cit note 11 at ch 3 & section 9 & 84(1)(b).

⁷⁹ Bronstein & Oliver op cit note 5 at 12.

'national public entities' under the PFMA and therefore, further discussion on the MFMA is not germane to this research.

The object of the PFMA has been highlighted as a mechanism *'to secure transparency, accountability and sound management of the revenue, expenditure, assets and liabilities of the institutions to which it [the PFMA] applies'*.⁸⁰ The overarching principles of transparency and accountability are paramount and serve to uplift the values enshrined in the Constitution, specifically with respect to the financial management of national government institutions.⁸¹ Not merely underlying notions, accountability and transparency are the cornerstones to achieving a true constitutional dispensation.⁸² The PFMA enjoys legislative supremacy and in the event of an inconsistency with another piece of legislation, the PFMA prevails.⁸³

The PFMA defines a *'public entity'* as a *'national or provincial public entity'*.⁸⁴ The definition afforded to national public entities and provincial public entities mirror each other in that they are largely similar.⁸⁵ The PFMA specifically categorizes entities in accordance with their borrowing powers and funding capabilities, hence the distinction drawn between national and provincial public entities.⁸⁶ This research focuses on SOCs which are defined as *'national public entities'* and, therefore further discussion of provincial public entities is not relevant to this research.⁸⁷

The PFMA defines a *'national public entity'* as:

- a. *a national government business enterprise; or*
- b. *a board, commission, company, corporation, fund or other entity (other than a national government business enterprise) which is*
 - i. *Established in terms of national legislation;*

⁸⁰ Ibid at section 2.

⁸¹ PWC op cit note 70 at 3; *South African Broadcasting Incorporation Ltd and Another v Mpofu* 2009 (4) ALL SA 169 (GSJ) para 56; Constitution op cit note 11 at section 195, 216 & 217.

⁸² Ibid.

⁸³ PFMA op cit note 11 at section 3(3).

⁸⁴ Ibid at section 1.

⁸⁵ Ibid at section 1.

⁸⁶ Ibid at section 66(1)(c); Bronstein & Oliver op cite note 5 at 7.

⁸⁷ Ibid at section 1.

- ii. *fully or substantially funded either from the National Revenue Fund, or by way of a tax, levy or other money imposed in terms of national legislation; and*
- c. *accountable to Parliament.*⁸⁸

The PFMA defines a ‘*national government business enterprise*’ as an entity which:

- a. *is a juristic person under the ownership control of the national executive;*
- b. *has been assigned financial and operational authority to carry on a business activity;*
- c. *as its principal business, provides goods or services in accordance with ordinary business principles; and*
- d. *is financed fully or substantially from sources other than*
 - i *the National Revenue Fund; or*
 - ii. *by way of tax, levy or other statutory money.*⁸⁹

The definition of a ‘*national public entity*’ necessitates a twofold enquiry. The first leg of the enquiry commences with the differentiation between a ‘*national government business enterprise*’ (“Enterprise”) and a board, commission, company, corporation, fund or any other entity which is not a ‘*national government business enterprise*’ (collectively referred to as an ‘Entity’)⁹⁰ An Entity must be established by national legislation and must be fully or substantially funded by the state.⁹¹

In order to qualify as an Enterprise, four requirements must be satisfied by the ‘*national public entity*’. First, the entity must be a ‘*juristic person under the ownership control of the national executive*’.⁹² The definition of ‘*ownership control*’ relates to the control which the national executive exerts over the entity by holding a majority of the entity’s voting rights and the ability to appoint or remove the entity’s chief executive officer or a majority of its directors.⁹³ The PFMA does not define the ‘*national executive*’ however, it may be reasonably surmised that it is equivalent to the definition of the ‘*executive authority*’ as set out in the Constitution which depicts the President and his Cabinet.⁹⁴ Secondly, the entity must have ‘*been assigned financial and*

⁸⁸ Ibid.

⁸⁹ Ibid.

⁹⁰ Ibid.

⁹¹ Ibid.

⁹² Ibid.

⁹³ Ibid.

⁹⁴ Constitution op cit note 11 at section 85(1) & (2).

operational authority to carry on a business activity'.⁹⁵ Thirdly, as its principle business, the entity must provide goods or services in accordance with ordinary business principles.⁹⁶ Lastly, the entity is financed substantially or fully from sources other than the '*National Revenue Fund*' or '*by way of a tax, levy or other statutory money*'.⁹⁷

The distinction drawn between an Enterprise and an Entity is, arguably, based on their financial sources and borrowing requirements from the state.⁹⁸ An Entity is substantially or fully reliant on funding from the state whereas an Enterprise is substantially or fully financed from sources other than the state.⁹⁹ Therefore, Enterprises are financially self-reliant and are charged with largely commercial mandates whilst Entities are reliant on state funding and discharge mainly non-commercial mandates.¹⁰⁰

The second leg of the enquiry, in the identification of a '*national public entity*', pertains to the principle of accountability. An Enterprise and an Entity are both '*accountable to Parliament*'.¹⁰¹ The PFMA does not define '*Parliament*', however it can be reasonably surmised that it is equivalent to the definition of '*Parliament*' as contained in the Constitution. In the premise, Enterprises and Entities are accountable to Parliament which consists of the National Assembly and the National Council of Provinces ('NCOP').¹⁰²

The PFMA makes no specific reference to the definition of an SOC but applies to all public entities which are listed under its schedule 2 and which may be classified as an Entity or Enterprise.¹⁰³ The entities listed under schedule 2 are categorized as '*major public entities*' and largely consist of Enterprises which are financially self-sufficient, such as SAA or Eskom.¹⁰⁴ SAA is subject to the provisions of the PFMA as it is listed as a major public entity under schedule 2 and is, therefore,

⁹⁵ PFMA op cit note 11 at section 1.

⁹⁶ Ibid.

⁹⁷ Ibid.

⁹⁸ Bronstein & Olivier op cit note 5 at 7.

⁹⁹ Ibid at 8.

¹⁰⁰ Ibid.

¹⁰¹ PFMA op cit note 11 at section 1.

¹⁰² Constitution op cit note 11 at section 41 (1).

¹⁰³ Bronstein & Oliver op cit note 5 at 6; PFMA op cit note 11 at section 3(1)(b).

¹⁰⁴ Ibid at schedule 2.

a ‘*national public entity*’ which is a ‘*national government business enterprise*’.¹⁰⁵ This is a convoluted and counterintuitive way of stating that SAA is subject to the provisions of the PFMA.

2.1.2 The Companies Act

One of the main objects of the Companies Act is to promote compliance with the Bill of Rights, as set out in the Constitution, in the application of company law in South Africa.¹⁰⁶ The Companies Act also streamlines processes, encourages entrepreneurship, improves flexibility and simplifies bureaucratic red tape, thereby fostering innovation and providing a uniform regulatory framework which is applicable to all incorporated companies.¹⁰⁷ The implementation of the Companies Act represented a fundamental shift to align South African corporate law with international trends, replacing the outdated 1973 Companies Act.¹⁰⁸

The advent of the Companies Act, gave rise for the first time to the definition of an SOC.¹⁰⁹ The specific identification of an SOC provides a valuable contribution to South African corporate law jurisprudence. Neither its predecessor, the 1973 Companies Act, nor the PFMA, provided for the definition of an SOC.¹¹⁰ All SOCs, along with the other types of companies, can now specifically register with the Companies and Intellectual Property Commission (‘CIPC’). An SOC is now a separately defined type of company and much of the uncertainty surrounding the identification of an SOC should have been alleviated. However, this is not always the case, as will be illustrated below.

A distinction has been drawn between SOEs and SOCs in that not all SOEs are SOCs, unless they comply with the definition of an SOC under the Companies Act, read in conjunction with the relevant provisions of the PFMA.¹¹¹

A ‘*state-owned company*’ is defined in the Companies Act as:

‘... an enterprise that is registered in terms of this Act as a company, and either,

¹⁰⁵ Ibid at schedule 2, sections 1 & 3(1)(b).

¹⁰⁶ Companies Act op cit note 11 at section 7; Walker, David & Mokoena, Stimela ‘South Africa’ in Willem JL Calkoen *The Corporate Governance Review* (2011) at 276.

¹⁰⁷ Ibid.

¹⁰⁸ Ibid at 285.

¹⁰⁹ Companies Act op cit note 11 at section 1; PWC op cit note 70 at 6.

¹¹⁰ Companies Act, 1973 op cit note 77.

¹¹¹ Bronstein & Oliver op cit note 5 at 8.

- a. *is listed as a public entity in Schedule 2 or 3 of the Public Management Finance Act, 1999 (Act No. 1 of 1999); or*
- b. *is owned by a municipality, as contemplated in the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000) and is otherwise similar to an enterprise referred to in paragraph (a).*¹¹²

The definition of an SOC under the Companies Act comprises a twofold analysis. First, the entity must be registered as a company, in accordance with the provisions of the Companies Act. Secondly, the registered company must be listed as a public entity under schedule 2 or 3 of the PFMA.

Under the first leg of the analysis the enterprise must be a registered company, as defined under the Companies Act:

“company” means a juristic person incorporated in terms of this Act, a domesticated company, or a juristic person that, immediately before the effective date –

- (a) *was registered in terms of the –*
 - (i) *Companies Act, 1973 (Act 61 of 1973), other than as an external company as defined in the Act; or*
 - (ii) *Close Corporations Act, 1984 (Act 69 of 1984), if it has subsequently been converted in terms of Schedule 2;*
- (b) *was, in existence and recognized as an ‘existing company’ in terms of the Companies Act, 1973 (Act 61 of 1973); or*
- (c) *was deregistered in terms of the Companies Act, 1973 (Act 61 of 1973) and has subsequently been re-registered in terms of this Act;*¹¹³

This expansive definition of a company allows for the inclusion of juristic persons which are registered under the Companies Act and for juristic persons which, under the 1973 Companies Act, were designated as a registered company, recognized as an ‘existing company’ and a deregistered company (which has subsequently been re-registered in terms of the Companies Act).¹¹⁴ Legislators predicted the upheaval which the implementation of the Companies Act would have on existing companies and thus the definition allows for the most seamless transition possible.

¹¹² Companies Act op cit note 11 at section 1.

¹¹³ Ibid at section 1.

¹¹⁴ Ibid.

There are two types of companies which can be formed and incorporated under the Companies Act: a profit company and a non-profit company.¹¹⁵ A profit company is an SOC if it is not registered as a private company, personal liability company or public company.¹¹⁶ This ‘default type’ definition of an SOC is confusing as it is determinant on a company not being registered as any other company. Therefore, if a company is registered as a private, personal liability or public company, it is not an SOC. Viewed from a positive perspective, an SOC is a company which is registered in terms of the Companies Act, but which is not registered as a private company, personal liability company or a public company.

Under the second leg of the definition of an SOC, a company, as defined, must then also be a public entity listed under schedule 2 or 3 of the PFMA.¹¹⁷ The focus of this research is on SOCs which are listed under schedule 2 of the PFMA, such as SAA.

An entity such as SAA is defined as an SOC as it is a registered public company, in terms of the 1973 Companies Act and a public entity listed under schedule 2 of the PFMA.¹¹⁸ Any provision of the Companies Act which is applicable to a public company automatically applies to an SOC, unless specifically exempted.¹¹⁹ Under the Companies Act, an SOC may be deemed to have amended its constitution and changed the suffix of its name to ‘SOC Limited’, as at the general effective date of 1 May 2011.¹²⁰

2.2 Classification Issues for SOCs

An example of the classification of an SOC which will be utilized throughout this research is SAA. SAA may be categorized as an Enterprise due to its satisfaction of the four requirements for a ‘*national government business enterprise*’ in accordance with the PFMA.¹²¹

First, SAA is under the ownership control of the national executive in that the state, as its sole shareholder: holds all of the voting rights at the annual general meeting, casts the majority of voting rights at a board meeting and has the ability to appoint and remove the chief executive officer as well as a majority of the directors on the board.¹²² Secondly, SAA has been assigned the financial

¹¹⁵ Ibid at section 8 (1).

¹¹⁶ Ibid at section 8 (2).

¹¹⁷ Ibid at section 1.

¹¹⁸ South African Airways Act 5 of 2007 at section 2 & 4.

¹¹⁹ Companies Act op cit note 11 at Section 9 (1).

¹²⁰ Ibid at sch 5 item 4 (1)(c).

¹²¹ Ibid at section 1; PFMA op cit note 11 at section 1 & 3(1)(b).

¹²² SAA Act op cit note 118 at section 3 (3)(b).

and operational authority to carry on a business activity to engage in passenger airline and cargo transport services.¹²³ Thirdly, as its principal business, SAA provides passenger airline and cargo transport services in accordance with ordinary business principles.¹²⁴ Whilst SAA is charged with a non-commercial mandate, which entails the establishment of trade routes with potential allies and trade partners, its principal business is the provision of passenger airline and cargo transportation services for a profit.¹²⁵

Lastly, SAA is meant to be substantially or fully financed from sources other than the '*National Revenue Fund or by way of a tax, levy or other statutory money*'. SAA is charged with performing a dual mandate: a non-commercial one, on behalf of the state and a commercial mandate for the generation of its own profit.¹²⁶ The profits borne out of the discharging of its commercial mandate, should arguably be utilized in order to perform its non-commercial mandate. However, SAA has been substantially or fully reliant on state funding in order to continue its operations, over the last decade.¹²⁷ Therefore, as a result of a change in its financial sources, SAA may arguably be categorized as an Entity, as opposed to an Enterprise.

According to the Department of Public Enterprises, these public entities are considered SOCs: Transnet SOC Limited ('Transnet'), SAA, South African Express SOC Limited, Eskom, Denel SOC Limited ('Denel'), SAFCOL SOC Limited and Alexkor SOC Limited.¹²⁸ All of these SOCs are listed as major public entities under schedule 2 of the PFMA.¹²⁹ These SOCs account for seven of the total 21 major public entities, listed under schedule 2 of the PFMA.¹³⁰ Arguably, the remaining fourteen entities are SOEs which are only subject to the PFMA and not the Companies Act.

However, the reasoning for the differentiation between the seven SOCs and the fourteen SOEs under schedule 2 of the PFMA is not provided and, therefore, remains unclear. It would appear as

¹²³ Ibid at section 6.

¹²⁴ Ibid.

¹²⁵ Ibid.

¹²⁶ Kanyane op cit note 10 at 33.

¹²⁷ National Treasury op cit note 1 at 4.

¹²⁸ Department of Public Enterprises (DPE) 'State-Owned Companies' available at <http://dpe.gov.za/state-owned-companies/> accessed on 14 August 2020.

¹²⁹ PFMA op cit note 11 at sch 2.

¹³⁰ Ibid.

if there is no uniform method of categorizing the various SOCs and SOEs which are listed under schedule 2 of the PFMA. None of the seven SOCs include the suffix ‘SOC Limited’ in their names, which is required for their identification in accordance with the Companies Act. The PFMA should have been amended so that SOEs which fulfil the criteria of the definition for SOCs are identified as SOCs and follow the appropriate naming convention set out in the Companies Act.

Without such an amendment, the distinction and classification between SOEs and SOCs, under schedule 2, is inferred based on announcements made by the Department of Public Enterprises and appears to have been determined on an arbitrary basis. Evidence of this arbitrary determination between SOEs and SOCs will be shown with reference to the Airports Company South Africa (‘ACSA’) and Denel, both of which are listed as major public entities under schedule 2 of the PFMA.¹³¹

The ACSA is a registered company, in terms of the Companies Act and is listed as a public entity under schedule 2 of the PFMA.¹³² Denel is a registered company under the Companies Act and listed as a public entity under schedule 2 of the PFMA.¹³³ Therefore, both Denel and the ACSA meet the requirements for the definition of an SOC in accordance with the Companies Act and the PFMA.¹³⁴ However, according to the Department of Public Enterprises, Denel is an SOC whereas the ACSA is not.¹³⁵ There is no reasoning provided for this differentiation and the categorization of Denel as an SOC and the ACSA as an SOE appears to be made on an arbitrary basis.

Even more startling is the fact that the ACSA states that it is ‘*legally and financially autonomous and operates under commercial law*’.¹³⁶ Without any further explanation as to its exclusion from the provisions of the Companies Act or the PFMA, the ACSA seems to be defined as an entity which is a law unto itself, operating under the very broad dimensions of the ‘commercial law’ of South Africa.

Notwithstanding the clearly defined statutory requirements for an SOC, there is no uniformity or clarity on the identification and categorization of SOEs and SOCs, especially with reference to the

¹³¹ Ibid.

¹³² Ibid; Airports Company Act 44 of 1993 at section 2.

¹³³ Ibid; Denel SOC Limited ‘About Us: Corporate Governance’ available at <http://www.denel.co.za/about-us/corporate-governance>, accessed on 14 August 2020.

¹³⁴ Ibid; Companies Act op cit note 11 at section 1.

¹³⁵ DPE op cit note 128.

¹³⁶ ACSA op cit note 80.

public entities listed under schedule 2 of the PFMA. Any SOE which meets the statutory requirements for an SOC should be defined as such and will be required to comply with the provisions of the Companies Act.

2.3 Circumvention of the Companies Act by SOEs

All SOCs are required to comply with the Companies Act, the PFMA and their own founding legislation.¹³⁷ All SOEs, which are not defined as SOCS, are only subject to the provisions of the PFMA and not those of the Companies Act. The primary differentiation between the purpose of the PFMA and the Companies Act is that the PFMA focuses on the financial management of an entity while the Companies Act regulates matters on a much wider scale than just financial management.¹³⁸ Given the numerous statutory provisions with which SOCs must comply, conflicts between the Companies Act and the PFMA were bound to arise.

In the event of a conflict between the provisions of the two pieces of legislation, the intention and purpose of the provisions bear closer examination. It is imperative that the conflicting provisions of the statutes be applied concurrently, to the extent that it is possible to apply one of the provisions without contravening the other.¹³⁹ However, to the extent that concurrent application of the two statutory provisions is not possible, the provisions of the PFMA prevail.¹⁴⁰

Furthermore, section 9 of the Companies Act allows for an exemption from the provisions of the Companies Act for an SOC in the event of a conflict between the PFMA and the Companies Act.¹⁴¹ The wide discretionary nature of section 9 is limited by the narrow scope of the requirements under which the Minister may grant an exemption.¹⁴² The Minister may only grant an exemption on the grounds of an overlap or duplication between the applicable provisions of the Companies Act and the provisions of an applicable regulatory scheme established in terms of any other national legislation.¹⁴³

It is submitted that, as a result of its narrowed application, the provisions of section 9 will not be abused by SOCs and the Minister in order to circumvent the provisions of the Companies Act.¹⁴⁴

¹³⁷ Bronstein & Oliver op cit note 5 at 8.

¹³⁸ Ibid at 20; Cassim op cit note 63 at 4; PWC op cit note 22 at 6.

¹³⁹ Companies Act op cit note 11 at section 5 (4)(a).

¹⁴⁰ Ibid at section 5 (4)(b) (i)(ee); PFMA op cit note 11 at section 3 (3).

¹⁴¹ Ibid Companies Act at section 9.

¹⁴² Ibid at section 9 (2) & (3); Bronstein & Oliver op cit note 5 at 13.

¹⁴³ Ibid at section 9 (2).

¹⁴⁴ Bronstein & Oliver op cit note 5 at 13.

However, given the legislative supremacy of the PFMA and the possibility of exempting an SOC from provisions of the Companies Act, the binding nature of the Companies Act on SOCs is somewhat diluted.¹⁴⁵

The Companies Act may still be circumvented by SOEs. All SOEs, which are not defined as SOCs for whatever reason, are not subject to the provisions of the Companies Act as the Companies Act is only applicable to SOCs and not to SOEs.¹⁴⁶ It is submitted that there are three primary justifications for holding all SOEs and SOCs to the provisions of the Companies Act, in addition to the PFMA and their own founding legislation.

First, the Companies Act is a much more recent statute coming into effect in 2011 whereas the PFMA came into effect 1999 which is two decades earlier. The Companies Act is, therefore, more aligned to the socio-economic and political changes in South Africa and to international trends.¹⁴⁷

Secondly, the directors' duties which are partially codified in the Companies Act are more contemporary than those provided under the PFMA.¹⁴⁸ The PFMA only requires its statutory duties to be discharged by the board of an SOC, jointly, while the Companies Act requires that the board and its directors, individually, fulfil its statutory duties.¹⁴⁹ The directors of an SOE may be sheltered from the harsh imposition of individual criminal or personal liability, for a breach of their statutory duties, under the protection of the board, as a collective body of all of the directors, in their joint decision taking.¹⁵⁰ Therefore, the individual directors of SOCs are held to a much higher standard of duties, the same as for private companies, than the board of SOEs under the PFMA.

Thirdly, and most notably, the Companies Act contains enhanced standards of transparency and accountability which are applicable to SOCs whilst SOEs are only subject to the governance requirements set out in the PFMA.¹⁵¹ Directors of SOCs, who are required to comply with both the Companies Act and the PFMA, are therefore required to comply with many more requirements than SOE directors.¹⁵² Although this might come with higher compliance costs, SOCs are held to

¹⁴⁵ Ibid.

¹⁴⁶ Ibid at 8; Companies Act op cit note at section 8(2)(a).

¹⁴⁷ Cassim op cit note 63 at 4.

¹⁴⁸ Companies Act op cit note 11 at section 76; PFMA op cit note 11 at section 50 & 51; Bronstein & Oliver op cit note 5 at 10.

¹⁴⁹ Companies Act op cit note 11 at section 76; PFMA op cit note 11 at section 50 & 51.

¹⁵⁰ Ibid at section 77 (2); Ibid at section 86 (2).

¹⁵¹ Companies Act op cit note 11 at section 9 and ch 3; Bronstein & Oliver op cit note 5 at 11; PFMA op cit note 11 at Section 46 and ch 6.

¹⁵² Ibid at 11.

a much higher level of scrutiny in their attempts to achieve the constitutional principles of accountability and transparency.¹⁵³

An examination of all of the SOEs and SOCs under schedule 2 of the PFMA should be undertaken by the Minister and attempts should be made to define all SOEs, which satisfy the legislated requirements, as SOCs. Many more of the SOEs under schedule 2 of the PFMA will then be defined as SOCs and be subject to the provisions of the Companies Act, in addition to the PFMA. Furthermore, as custodians of national assets and utilisers of taxpayer monies, arguably all SOEs, regardless of their identification as SOCs, should be held to the utmost scrutiny and be bound by the provisions of the Companies Act.

2.4 Conclusion

Two primary issues are evident from the preceding paragraphs surrounding the identification and classification of SOEs and SOCs. The first issue relates to the complex and contradictory definitions of SOEs under the PFMA, with specific reference to the major public entities listed under schedule 2, which may be categorized as Entities or Enterprises, based on their borrowing requirements from the state.¹⁵⁴ The second issue relates to the arbitrary differentiation between SOCs and SOEs, listed under schedule 2 of the PFMA, despite clear statutory requirements pertaining to the definition of an SOC contained in the Companies Act.¹⁵⁵

The enactment of an overarching SOE Legislation is re-iterated as the proposed solution to resolve the two primary issues, as was concluded by the Presidential Review Committee on State-Owned Enterprises in 2012.¹⁵⁶ The proposed SOE Legislation will be the overarching statute which will govern all aspects relating to SOEs and SOCs, including their identification and classification.¹⁵⁷ Under chapter six of this thesis, there are proposed recommendations for certain provisions to be contained in the SOE Legislation.

Provisions contained in the Companies Act (especially those pertaining to the enhanced accountability and transparency requirements) and the PFMA should be amalgamated into clear and uniform provisions for insertion into the SOE Legislation. The amalgamation of the statutory

¹⁵³ Ibid at 12.

¹⁵⁴ PFMA op cit note 11 at section 1 & sch 2.

¹⁵⁵ Ibid; Companies Act op cit note 11 at section 1.

¹⁵⁶ PRC op cit note 3 at 9.

¹⁵⁷ Kanyane op cit note 10 at 30.

provisions should serve to remove duplications and contradictions surrounding the definition given to SOCs and SOEs and eliminate the subsequent confusion regarding the possibility of having to comply with the PFMA or the Companies Act or both statutes. SOCs and SOEs should be given a transitional period, following enactment of the SOE Legislation, in order to amend their founding legislation to remove any inconsistencies with the SOE Legislation which would prevail in the event of any contradicting provisions.

Unless it can be shown to be meaningfully required, there should only be one overarching and uniform definition for all SOEs and the distinction between SOCs and SOEs should be removed. The SOE Legislation may define various categories of SOEs, based on their mandates and borrowing requirements from the state.¹⁵⁸ Those SOEs which are fulfilling non-commercial mandates on behalf of the state, such as service delivery and public policy functions, are likely to be reliant on the state as the sole source of their financing.¹⁵⁹ Those SOEs which discharge dual mandates, comprising commercial and non-commercial objectives, are likely to be less reliant on the state as a financial source and may be financially self-sufficient.¹⁶⁰ The mandates and borrowing requirements are interlinked and should be considered in a holistic manner when determining the criteria and for the categorization of SOEs.

Furthermore, the SOE Legislation should incorporate provisions which allow for the reclassification of an SOE into a different category should the need arise. The Minister should be able to reclassify an SOE in the event of a change in the requirements of its mandate or its financial circumstances which may affect its borrowing requirements from the state.¹⁶¹ The ability to reclassify SOEs will allow for their categorisation to be aligned with their current mandates as well as their economic, operational and financial circumstances.

This should have been the case with SAA which has been classified as an Enterprise under the PFMA, since its inception in 1999 but which should now be reclassified as an Entity due to its sole reliance on state funding over the last decade.¹⁶² The inability to reclassify SAA has meant that for many years its directors have been complying with the requirements under the PFMA pertaining

¹⁵⁸ Ibid.

¹⁵⁹ Ibid at 31; Bronstein & Olivier op cit note 5 at 20.

¹⁶⁰ Ibid.

¹⁶¹ PFMA op cit note 11 at section 48 & sch 3.

¹⁶² SAA Reports op cit note 20; National Treasury op cit note 1 at 5.

to Enterprises when they should have been complying with the requirements pertaining to Entities.¹⁶³ This reclassification may have assisted in preventing the downfall of SAA which, in late December 2019, voluntarily initiated business rescue proceedings.¹⁶⁴

All SOEs (and SOCs subsumed under the definition of an SOE) will be subject to the SOE Legislation and the specific proposed provisions which will be discussed in chapter six of this thesis. It is re-iterated that the definition and categorization of all SOEs should be included in the SOE Legislation.¹⁶⁵ Uniform, simple and clear provisions in the SOE Legislation will provide certainty and clarity and serve to reduce compliance costs for directors who only have to comply with one statute as opposed to multiple. A clear and uniform approach to the definition of SOEs will assist as a precursor to an analysis of their accountability mechanisms in an attempt to provide recommendations to improve their future corporate performance.

¹⁶³ PFMA op cit note 11.

¹⁶⁴ SAA op cit note 18.

¹⁶⁵ PRC op cit note 3 at 9.

CHAPTER THREE: THE ACCOUNTABILITY MECHANISMS FOR SOCS

3 Introduction

South African SOCs have the ability to drive and accelerate national growth and development for our budding economy.¹⁶⁶ However, the underperformance of SOCs, which has largely been attributed to a chronic lack of accountability, has resulted in their reliance on state funding thereby depleting scarce state resources.¹⁶⁷ Notwithstanding a plethora of legislation, comprising internal and external mechanisms attempting to ensure accountability, the enforcement of these mechanisms on deteriorating SOCs is virtually non-existent and in dire need of reform.¹⁶⁸ The concept of enforceable accountability for SOCs, through the implementation of a novel reward-based mechanism, is proposed for such reform which may serve to improve their future performance.

3.1 The Concept of Accountability

King IV defines the principle of accountability as:

*'the obligation to answer for the execution of responsibilities. Accountability cannot be delegated, whereas responsibility can be delegated without abdicating accountability for that delegated responsibility'.*¹⁶⁹

Responsibility is then defined as:

*'taking ownership of a duty, obligation or liability'.*¹⁷⁰

Accountability is a principle which attempts to ensure the effective fulfilment of directors' duties, in the execution of their responsibilities, to act in the best interests of the company, at all times.¹⁷¹ Accountability is a principle which stems from the age old 'agency issue'.¹⁷² Shareholders rely on directors to take decisions in the best interest of the company which will serve to protect

¹⁶⁶ Kanyane op cit note 10 at 30; PRC Protocol op cit note 3 at 4; PWC op cit note 22 at 4.

¹⁶⁷ Ibid at 30; Thomas op cit note 9 at 450; Bronstein & Oliver op cit note 5 at 5; David J Fourie 'The Role of Public Sector Enterprises in the South African Economy' (2014) 7 *African Journal of Public Affairs* 30 at 32; Futuregrowth op cit note 10 at 4; Thabane op cit note 9 at 5; McGregor op cit note 5 at 6; *South African Broadcasting Corporation SOC Ltd and Others v Democratic Alliance and Others* 2016 (2) SA 522 (SCA) para 44.

¹⁶⁸ Makwethu (AGSA) op cit note 18 at 10.

¹⁶⁹ King IV op cit note 19 at 9.

¹⁷⁰ Ibid.

¹⁷¹ Ibid at 12.

¹⁷² Thabane op cit note 9 at 6; Futuregrowth op cit note 10 at 3.

and grow their investments.¹⁷³ In other words, the directors of a company are accountable to the shareholders for their decisions which are to be taken, at all times, in the best interests of the company.¹⁷⁴

When a director is tempted with personal gains, attained by virtue of her position as director, a conflict may arise between the interests of the director and the interests of the company.¹⁷⁵ In such an instance, the director is meant to act in the best interests of the company and not in pursuit of her own personal interests.¹⁷⁶ The principle of accountability is meant to ensure that the conflicted director places the interests of the company ahead of her own in order to protect the investment of the shareholder, to whom she must account for any decisions taken in her capacity as director.¹⁷⁷

Accountability is a principle which may be used to subvert detrimental conflicts of interest which could negatively impact the company if left unchecked.¹⁷⁸ If directors are required to account for every decision taken, they will be forced to provide sound judgement and reasoning for their decisions, thereby deterring unscrupulous and selfish behaviour.¹⁷⁹ It is submitted that directors who are not held to account for their decisions may take decisions, on a continual basis, which are not in the best interests of the company and may negatively impact the performance of the company. The principle of accountability is, therefore, utilised not to promote the ethical behaviour of directors but rather as a measure to constrain the unethical.¹⁸⁰ Accountability also fosters other important principles which promote the interests of a company, including: transparency, responsibility and fairness.¹⁸¹

3.2 The Accountability Mechanisms for SOCs

Section 195 of the Constitution places a pre-emptory, accountability requirement on all public administration in South Africa, which includes public enterprises such as SOEs and SOCs.¹⁸² This section states that:

¹⁷³ Ibid.

¹⁷⁴ Ibid.

¹⁷⁵ Futuregrowth op cit note 10 at 3.

¹⁷⁶ Thabane op cit note 9 at 5.

¹⁷⁷ Ibid.

¹⁷⁸ Ibid.

¹⁷⁹ Futuregrowth op cit note 10 at 6.

¹⁸⁰ Ibid.

¹⁸¹ King IV op cit note 19 at 20; Thabane op cit note 9 at 10; Bronstein & Oliver op cit note 5 at 32.

¹⁸² Constitution op cit note 11 at section 195(1)(f) & (2)(c).

'1. Public administration must be governed by the democratic values and principles enshrined in the Constitution, including the following principles:

...

f. public administration must be accountable.

...

2. The above principles apply to

...

*c. Public enterprises.*¹⁸³

This inclusion in our supreme law further emphasizes the importance of the principle of accountability for all SOCs.¹⁸⁴ The current accountability structures which should be implemented by all SOCs involve a delicate system of internal and external checks and balances.¹⁸⁵ All internal and external checks and balances should be continually enforced and monitored by SOC stakeholders to ensure their effectiveness as enforceable accountability mechanisms.

3.3 Internal Accountability Mechanisms

The internal accountability framework for SOCs comprise three predominant pillars. First, the directors, the board and its various committees.¹⁸⁶ Secondly, the supervisory role of the state as sole shareholder.¹⁸⁷ Thirdly, the role of the internal auditors and the company secretary.¹⁸⁸ As the first hurdle to ensuring enforceable accountability, an SOC needs to fulfil the internal accountability mechanisms as a matter of absolute priority. Only once the internal mechanisms are completely satisfied, will the external mechanisms be put to the test to establish their true potential in achieving the actual and proper accountability of an SOC.

¹⁸³ Ibid.

¹⁸⁴ Mandla M Masuku 'Effective Governance in South Africa: reality or myth?' (2019) 6 *African Journal of Democracy and Governance* 118 at 118.

¹⁸⁵ Kanyane op cit note 10 at 39.

¹⁸⁶ Bronstein & Oliver op cit note 5 at 10.

¹⁸⁷ SABC case supra note 167 para 44; Wiese op cit note 63 ; King IV op cit note 19 at 117.

¹⁸⁸ Ibid Wiese op cit note 63 at 36; King IV op cit note 19 at 59.

3.4 Directors Duties and Liabilities

The point of departure with regard to a discussion of the accountability of an SOC, must, as a matter of course, commence with its directors.¹⁸⁹ Directors are required to fulfil their common law duties as well as their partially codified statutory duties, contained in the PFMA, the Companies Act and its own founding legislation, to act in the best interests of the SOC at all times.¹⁹⁰ Directors are able to delegate a duty, of which they have taken ownership, however, they remain accountable for the execution of such duty.¹⁹¹ The board of an SOC and its directors, individually and collectively, are always held accountable to the state, as its sole shareholder, for the execution of their responsibilities which includes the performance of their duties.¹⁹²

There is no specific statutory duty to account, which the directors of an SOC are required to fulfil. However, fulfilment by the directors of their common law duties and the partially codified fiduciary duties together with the duty of care and skill in every decision taken, in the best interests of the SOC, should result in their accountability to the state and various other stakeholders. Therefore, the effective fulfilment of directors' duties and the principle of accountability are inextricably linked. A director who fails to discharge his or her duties will compromise his or her own ability to account for decisions taken, which may not have been in the best interests of the SOC and which may ultimately hinder its performance.¹⁹³

3.4.1 Definition of Directors: Who Owes the Duty?

The board of an SOC, jointly and its directors, individually, are required to discharge their common law and partially codified statutory duties in accordance with the Companies Act and the PFMA, as the predominant pieces of legislation, as well as their own founding legislation.¹⁹⁴

¹⁸⁹ Ibid; Emily Makuta 'Towards Good Corporate Governance in State-Owned Industries: the Accountability of Directors' (2009) 3 *Malawi Law Journal* 1.

¹⁹⁰ Companies Act op cit note 11 at section 76; PFMA op cit note 11 at section 50 & 51; Dullah Omar Institute for Constitutional Law, Governance and Human Rights (University of the Western Cape) 'Legal Framework of SOE Boards' (2018) available at: http://dullahomarinate.org.za/women-and-democracy/board-members-of-state-owned-enterprises-towards-transparent-appointments/reports/wandrag_legal_framework_paper_2_revision_4_04_07_2019.pdf accessed on 5 June 2019 at 30.

¹⁹¹ King IV op cit note 19 at 9; *Mthimunya-Bakoro v Petroleum Gas and Oil Corporation of South Africa (SOC) Limited and Another* 2015 (6) SA 338 (WCC) para 25; Madonsela op cit note 16 at 255.

¹⁹² King IV op cit note 19 at 21; *Mpofu* case supra note 96 para 30.

¹⁹³ *PetroSA* case supra note 207 para 20.

¹⁹⁴ Bronstein & Oliver op cit note 5 at 30; PFMA op cit note 11 at section 50 & 51; Companies Act op cit note 11 at section 76; Cassim op cit note 63 at 509.

The Companies Act provides for the wide definition of a director as ‘*a member of the board of a company, as contemplated in section 66 or an alternate director of a company and includes any person occupying the position of a director or alternate director by whatever name designated.*’¹⁹⁵

The board of an SOC has the authority, unless restricted in its founding legislation or by the provisions of the PFMA, to exercise all of the powers and perform any of the functions of the SOC.¹⁹⁶ This extensive definition indicates that all of the members of the board of an SOC, regardless of their designation, will be regarded as directors who have the authority to exercise all of the powers and perform all of the functions of the SOC.

In addition, section 76 of the Companies Act, pertaining to directors’ duties, complements the extensive definition of a director.¹⁹⁷ Section 76 (1) stipulates that ‘*an alternate director, a prescribed officer or a person who is a member of a committee of a board of a company or of the audit committee of the company, irrespective of whether or not the person is also a member of the company’s board*’, will be included in the definition of a director for the purposes of the section.¹⁹⁸

This wide definition affords extensive protection for an SOC by requiring such persons to err on the side of caution and take every decision in the best interests of the SOC, even if they are not specifically designated as a director of the SOC.¹⁹⁹

As a result of the extensive definition of a director, persons cannot escape liability for a breach of their statutory duties on the basis that they are not formally designated as a director of the SOC.²⁰⁰ Therefore, any executive, non-executive, independent, de facto, nominee, de jure, shadow, ex-officio director, prescribed officer, alternate director or member of a board or audit committee of the SOC is required to perform the statutory duties.²⁰¹ The all-encompassing definition of a director contained in the statutory duties in section 76, coupled with the extensive definition of a director in section 1, make it increasingly difficult for persons to escape liability for a breach of their statutory duties.²⁰²

¹⁹⁵ Companies Act op cit note 11 at section 1; Cassim op cit note 63 at 403.

¹⁹⁶ Ibid at section 66; Ibid at 404.

¹⁹⁷ Ibid at section 1 & 76 (1).

¹⁹⁸ Ibid at section 76 (1).

¹⁹⁹ *Kaimowitz v Delahunt and Others* 2017 (3) SA 201 (WCC).

²⁰⁰ *Howard v Herringel* 1991 (2) SA 660 (A) at 678.

²⁰¹ Cassim op cit note 63 at 404 - 10; *Mpofu* case supra note 96 para 30; *PetroSA* case supra note 207 para 56.

²⁰² Ibid at 510; Wiese op cit note 63 at 68; *Howard* case supra note 216 at 678.

The PFMA also prescribes statutory duties which the board of an SOC must fulfil.²⁰³ The PFMA defines the board of directors of an SOC as its ‘*accounting authority*’.²⁰⁴ The PFMA also contains a duty which may be described as a duty to account by the board of an SOC: ‘*Every public entity must have an authority which must be accountable for the purposes of this Act*’.²⁰⁵ The board owes statutory duties to the SOC and must be held accountable for its compliance with the provisions of the PFMA.²⁰⁶ However, in contrast to the Companies Act, the board, and not the individual directors, are specifically referred to in the PFMA with regard to the statutory duties and the statutory accountability requirement.²⁰⁷

It is submitted that a conflict between the PFMA and the Companies Act may arise as the PFMA only makes reference to the board of an SOC being required to discharge statutory duties and not the individual directors as required by the Companies Act. Where there is a conflict between the provisions of the PFMA and the Companies Act, which cannot be reconciled by reading them concurrently, the PFMA prevails.²⁰⁸ Therefore, it is submitted that an individual director of an SOC may defend a claim based on a breach of his or her statutory duty in the Companies Act, on the basis that the board, and not the individual directors, owe a duty to the SOC as required by the prevailing provisions of the PFMA.

Recent case law also suggests a judicial preference to hold the board accountable, as opposed to the individual directors, in terms of the overall management and supervision of a company.²⁰⁹ However, there is nothing prohibiting the directors, individually, as well as the board, collectively, owing the statutory duties to the SOC. In fact, SOCs should be held to a higher level of accountability, given their status as custodians of national assets and therefore, it seems likely that this discrepancy between the Companies Act and the PFMA is merely due to a legislative oversight. The board of an SOC and its individual directors should be required to discharge the statutory duties contained in the PFMA and the Companies Act which can be applied concurrently to ensure that the utmost level of accountability is achieved.²¹⁰

²⁰³ PFMA op cit note 11 at section 50 & 51.

²⁰⁴ Ibid at section 1 and section 49 (2)(a); King IV op cit note 19 at 112.

²⁰⁵ Ibid at section 49.

²⁰⁶ Ibid.

²⁰⁷ Ibid at section 50, 51 & 49; Companies Act op cit note 11 at section 76;

²⁰⁸ Companies Act at section 5 (4)(b)(i)(ee).

²⁰⁹ *Kaimowitz* case supra note 215 para 27.

²¹⁰ Futuregrowth op cit note 10 at 6; King IV op cit note 19 at 112.

In this research, for the sake of clarity when PFMA is referred to, it will be stated that the board, collectively, owe their duties to the SOC and when the Companies Act is referred to, it will be stated that the directors, individually, owe their duties to the SOC. The board will be described as a collective body which comprises the directors jointly but only severally where it is possible to make a distinction between the directors and where allowed under the relevant statutes. Unless specifically mentioned under the relevant statute, reference to the board indicates the directors making decisions jointly and as a collective body.

3.4.2 Definition of ‘the Company’: To Whom do Directors owe their Duties?

The next issue pertains to the identification of the entity to whom the directors owe their duties. The Companies Act requires that directors discharge their duties in ‘*the best interests of the company*’.²¹¹ The PFMA stipulates that the board owes its duties to the ‘*public entity*’.²¹² The Companies Act does not provide for the definition of a ‘*company*’ whilst the PFMA, as previously discussed defines a ‘*public entity*’, as an Entity or Enterprise. It is submitted that the directors owe statutory duties to the SOC, in accordance with the provisions of the Companies Act, read together with the PFMA.

However, the issue which now arises is to whom exactly the directors owe their statutory duties, in terms of the ownership structure of the SOC and its various stakeholders. The Companies Act and the PFMA do not provide for the description of what constitutes the ‘*company*’ or ‘*public entity*’ under the provisions encompassing the statutory duties.²¹³ The provision of such a description which sets out the ownership structure of an SOC would greatly assist in identifying to whom exactly the board and its directors owe their duties.

It is trite from the common law that directors owe their statutory duties to the ‘*company*’ which depicts the collective interests of its existing and future shareholders.²¹⁴ This is a traditional approach which requires directors to balance the short-term profit maximization with the long-term future sustainability of the company, to the absolute benefit of the shareholders, as a collective body.²¹⁵ This approach was further expanded with the ‘*pluralist*’ and ‘*enlightened shareholder*

²¹¹ Companies Act opt cit note 11 at section 76 (3)(b).

²¹² PFMA op cit note 11 at section 50 & 51.

²¹³ Ibid; Cassim op cit note 63 at 515.

²¹⁴ Ibid at 515; *Cohen v Segal* 1970 (3) SA 702 (W) 706; *Brady v Brady* [1988] BCLC 20 (CA); *Miller v Bain Sub Nom Pantone 485 Ltd* [2002] BCLC 266 (ChD).

²¹⁵ Ibid at 516 – 517.

value’ approaches which allow for the consideration of other stakeholders interests, in addition to the shareholders, in the decision taking by the directors of the company.²¹⁶

The most progressively altruistic approach to the duties owed by the directors to a company is that of the ‘*stakeholder-inclusive*’ approach which is advocated by the King Codes.²¹⁷ Under this approach, the directors are required to take into account the legitimate interests and expectations of the stakeholders in the execution of their duties, in the best interests of the company.²¹⁸ The shareholders’ interests are not prioritized over that of the other stakeholders, whose interests are balanced and taken into account to best serve the interests of the company.²¹⁹ Aligning with international corporate governance trends, the company is to be a responsible corporate citizen within the community in which it operates, from an economic, social and environmental perspective.²²⁰

However, this ‘*stakeholder-inclusive*’ approach is not mandated by the Companies Act or the PFMA and therefore, the directors of an SOC are not required to consider the interests of all stakeholders in order to fulfil their statutory duties.²²¹ The directors are therefore primarily concerned with serving the interests and expectations of the state, as the sole shareholder of the SOC, in discharging their statutory duties. The directors of an SOC would only voluntarily determine whether to take the interests of various stakeholders into account, on a case by case basis, to serve the best interests of the SOC.²²²

The ‘*stakeholder-inclusive*’ approach presents a unique and challenging hurdle for the directors of SOCs in terms of the competing dual mandates, comprising both commercial and non-commercial objectives, which have to be performed.²²³ Directors of SOCs may, therefore, be faced with the complicated task of having to balance the legitimate interests and expectations of the state, in its multiple capacities as: public policy maker, service delivery provider and profit-orientated sole shareholder. This may present a daunting challenge as the interests of the state, in these various

²¹⁶ Ibid at 518.

²¹⁷ Institute of Directors Southern Africa (IODSA) *The King Report of Governance for South Africa* (2009) Johannesburg: IODSA (King III) at 100 para 4; King IV op cit note 19 at 25.

²¹⁸ Ibid.

²¹⁹ Ibid at 13.

²²⁰ Ibid at 22.

²²¹ Companies Act op cit note 11 at section 76(3)(b); Cassim op cit note 63 at 517.

²²² King IV op cit note 19 at 117.

²²³ Ibid.

capacities, may not always be aligned. In addition, the directors of the SOC may also take into account the interests of other stakeholders including: employees, trade unions, creditors, suppliers and the public.²²⁴

In order to balance the competing interests of the state, in its various capacities, a shareholder compact agreement is entered into between the state and the SOC.²²⁵ This compact is meant to be executed annually and updated on a continual basis to ensure the achievement of key performance indicators by the SOC. This is an important document to maintain an open line of communication between the state and the directors of the SOC and to promote the efficient transparency and disclosure of the performance of mandates. The directors of the SOC should also set up methods to engage with the other stakeholders on a continual basis and not only through the publication of the annual, integrated report.

3.4.3 Specific Duties: What Duties are the Directors Required to Discharge?

There are two overarching statutory duties which directors of SOC's are obliged to perform: the fiduciary duty and the duty of care and skill.²²⁶ Both overarching duties have one supreme commonality: to act in the best interests of the SOC at all times.²²⁷ The board of an SOC is also required to discharge the numerous, additional statutory duties codified in the PFMA.²²⁸ An ever-evolving and flexible concept, directors' duties are often unclear, which makes their fulfilment a question of interpretation and application on a case by case basis.²²⁹

(a) Fiduciary Duties

The overarching obligation underpinning the core of the fiduciary duties is that directors are required to act with the utmost loyalty to the company, as its fiduciary.²³⁰ With this core obligation in mind, the fiduciary duties of directors contain four primary duties.²³¹ First, the duty to act in good faith, in the best interests of the SOC and for a proper purpose.²³² Secondly, the duty to

²²⁴ Ibid.

²²⁵ King IV op cit note 19 at 117.

²²⁶ Wiese op cit note 63 at 67; PFMA op cit note 11 at sections 50 & 51; Companies Act op cit note 11 at section 76.

²²⁷ Cassim op cit note 63 at 524; *Re Smith v Fawcett Ltd* (1942) Ch 304 at 306.

²²⁸ PFMA op cit note 11 at section 51.

²²⁹ Wiese op cit note 63 at 67.

²³⁰ Ibid at 68; *Building Society v Mothew* [1996] 4 ALL ER 698 (CA).

²³¹ Cassim op cit note 63 at 524.

²³² Ibid at 523 – 28.

exercise independent judgment.²³³ Thirdly, the duty to act within their powers.²³⁴ Fourthly, the duty to avoid a conflict of interest.²³⁵

The Companies Act and the PFMA have partially codified these four common law fiduciary duties, to various extents and with slight variations.²³⁶ In terms of section 76 of the Companies Act, directors are required to exercise their powers and perform their functions ‘*in good faith and for a proper purpose, in the best interests of the company*’.²³⁷ The duty to avoid a conflict of interest is also partially codified in section 50 (3) of the PFMA and under section 76 (2) read with section 75 of the Companies Act.²³⁸

The fiduciary duties encompassed under the PFMA are more robust than those contained in the Companies Act.²³⁹ The PFMA specifies four different and distinct fiduciary duties which include: exercising the utmost of care; acting with fidelity, honesty and integrity, the duty to disclose material and reasonably discoverable facts and to seek to prevent any prejudice to the state’s financial interests.²⁴⁰ The PFMA also contains provisions relating to general duties, in addition to the fiduciary statutory duties, with which the board of the SOC is required to comply.²⁴¹

The duties, encompassed in the PFMA, the Companies Act and the common law, should be applied concurrently to ensure the utmost accountability of the board and its directors for decisions which are to be taken in the best interests of the SOC.²⁴² The duty to avoid a conflict of interest has been one of the most, if not the most, adjudicated upon duties under the common law.²⁴³ A director is under a fiduciary duty to avoid placing himself or herself in a scenario where his or her personal interests conflict with his or her duties as a director.²⁴⁴ This is a stringent obligation which our

²³³ Ibid at 528 – 530; *Fisheries Development Corporation of SA Ltd v Jorgensen; Fisheries Development Corporation of SA Ltd v AWJ Investments (Pty) Ltd* 1980 (4) SA 156 (W).

²³⁴ Ibid at 532 – 34.

²³⁵ Ibid at 523 – 536; *Imageview Management Ltd v Jack* [2009] BCLC 725 at 739 (CA); *Parker v Mckenna* (1874) LR 10 Ch App 96 at 124.

²³⁶ Ibid at 523.

²³⁷ Companies Act op cit note 11 at section 76 (3)(a).

²³⁸ Ibid at section 76 (2) & 75 (4) & (5); PFMA op cit note 11 at section 50 (3).

²³⁹ PFMA op cit note 11 at section 50 (1).

²⁴⁰ Ibid.

²⁴¹ Ibid at section 51.

²⁴² Cassim op cit note 63 at 523; Companies Act op cit note 11 at section 4 (a).

²⁴³ Wiese op cit note 63 at 60; Cassim op cit note 63 at 523; *Keech v Sandford* (1726) Sel Cas Ch 61; *Regal (Hastings) v Gulliver*. Op Cit (note 7); *Imageview* case supra note 250, *Parker* case supra note 250 at 124; *Canadian Aero Service Ltd v O’Malley* (1973) 40 DLR (3d) 371 (SCC).

²⁴⁴ Wiese op cit note 63 at 70; *Robinson v Randfontein Estates Gold Mining Co Ltd* 1921 AD 168; *Dorbyl Ltd v Vorster* 2011 (5) SA 575 (GSI); *Da Silva v CH Chemicals (Pty) Ltd* 2008 (6) SA 620 (SCA).

courts have emphasized on many occasions.²⁴⁵ The partial codification of this duty in the Companies Act and the PFMA is evidence of its status as a core fiduciary duty.²⁴⁶

Under the umbrella of the statutory fiduciary duties, the Companies Act also specifically depicts a duty to avoid a personal financial interest for directors in the course and scope of discharging their duties.²⁴⁷ The introduction of this duty into the Companies Act is due to the numerous instances where directors' personal financial interests have taken precedence over their duties as a director.²⁴⁸ The requirements of this duty are that the conflicted director must disclose his or her conflict to the board, prior to the decision being taken, and then recuse himself or herself while the matter is under discussion for resolution.²⁴⁹ The statutory duty has a wide ambit in its inclusion of the expansive definition afforded to the 'directors' which is akin to the definition under section 76 and also encompasses the personal financial interests of any related party to the director.²⁵⁰

The difference between this duty and the general duty to avoid a conflict of interest, is the emphasis on the presence of a financial gain for the director.²⁵¹ The outcome of a director's failure to discharge this duty will be that the resultant board decision is regarded as invalid, unless the shareholders have subsequently ratified the decision following a disclosure of the interest.²⁵² An interested person may also approach the court to declare the board decision valid.²⁵³

In the event of an SOC director taking a decision to benefit his or her own personal interests, to the possible detriment of the SOC, he or she cannot be said to be acting in the best interests of the SOC.²⁵⁴ Where the personal interests of the director and the SOC diverge, one interest must be subverted in order for a decision to be taken. This divergence of interests results in a conflict, in which case the requirements of the Companies Act and the PFMA must be followed, failing which,

²⁴⁵ *Phillips v Fieldstone Africa (Pty) Ltd* 2004 (3) SA 465 (SCA); *Sibex Construction (SA) (Pty) Ltd v Injectaseal CC* 1988 (2) SA 54 (T) at 66D; *PetroSA* case supra note 207 para 56; Cassim op cit note 63 at 514.

²⁴⁶ Companies Act op cit note 11 at section 76 (2)(a); PFMA op cit note 11 at section 50 (2) & (3).

²⁴⁷ Ibid at section 75.

²⁴⁸ Cassim op cit note 63 at 568.

²⁴⁹ Companies Act op cit note 11 at section 75 (4) & (5).

²⁵⁰ Ibid at section 75 (1) & (6) & 76 (1).

²⁵¹ Ibid at section 75 & 76 (2); Cassim op cit note 63 at 550.

²⁵² Ibid at section 75 (7).

²⁵³ Ibid at section 75 (8).

²⁵⁴ Wiese op cit note 63 at 73; Cassim op cit note 63 at 569.

the board and/or director may be in breach of his or her statutory duty and subject to possible liability.²⁵⁵

The statutory fiduciary duties in the PFMA and the Companies Act do not specifically refer to a duty of accountability for SOC directors. It is conceivable that the principle of accountability is achieved through the directors effective fulfilment of all of their statutory duties.²⁵⁶ The PFMA does, however, mention accountability under the statutory fiduciary duties by prescribing a requirement for the disclosure of any material facts, including reasonably discoverable ones, by the board of an SOC to the legislature, to which the SOC is accountable which may influence the actions or decisions of the legislature.²⁵⁷ However, this is a duty to disclose rather than to account for the board and a similar duty is also encompassed under the Companies Act for the individual directors.²⁵⁸

There is a requirement stipulating that the board of an SOC must be held accountable for the purposes of the PFMA.²⁵⁹ This accountability requirement is not included under the statutory fiduciary duties of the PFMA but rather encompassed under section 49 forming a separate and distinct obligation on the board of an SOC.²⁶⁰

One of the fiduciary duties under the PFMA is unique to the position in which the board of an SOC finds itself as the manager of an entity where the state is its sole shareholder. This duty prescribes that the board of an SOC ‘*seek, within the sphere of influence of that accounting authority, to prevent any prejudice to the financial interests of the state*’.²⁶¹ This statutory fiduciary duty is unlike any other duty which is required of directors of private and public companies in South Africa under the common law or the Companies Act.²⁶²

²⁵⁵ Companies Act op cit note 11 at section 75 & 76 (2); PFMA op cit note 11 at section 50 (3).

²⁵⁶ Thulisile Madonsela ‘When Governance and Ethics Fail’ (2014) Public Protector South Africa report No. 23 of 2013/2014 available at http://static.pmg.org.za/1/161115WHEN_GOVERNANCE_FAILS_REPORT_EXEC_SUMMARY_17Feb2014.pdf, accessed on 12 August 2020 at 120.

²⁵⁷ PFMA op cit note 11 at section 50 (1)(c).

²⁵⁸ Companies Act op cit note 11 at section 76 (2)(b) & 75 (4), (5) & (6); Cassim op cit note 63 at 553.

²⁵⁹ Ibid at section 49 (2)(a).

²⁶⁰ Ibid.

²⁶¹ Ibid at section 50 (1)(d).

²⁶² Companies Act op cit note 11 at section 76.

The imputation of this onerous duty is that the board of an SOC owes this particular fiduciary duty specifically to the state, as shareholder.²⁶³ The application of this duty is narrowed in its scope due to the qualification that the board is only required to act within its own sphere of influence. As a result of this qualification, the duty may be subject to circumvention as the board of an SOC may argue that the financial prejudice suffered by the state was not within the realm of the board's influence and the prevention thereof was impossible. It may be difficult to prove that the financial prejudice suffered by the state ensued as a result of the decisions taken by the board of an SOC.²⁶⁴ The difficulty in proving a causal link between the financial prejudice suffered by the state and the decision taken by the board of the SOC may, therefore, dilute the enforceability of this important duty.²⁶⁵

However, the inclusion of this fiduciary duty under the PFMA clearly depicts the intention of the legislature to hold the board of an SOC to the highest level of accountability in taking decisions to actively prevent any financial prejudice being suffered by the state.²⁶⁶ It is clear that because SOCs may utilise state funding and perform mandates on behalf of the state, the decisions of the board may have a significant impact on the state and its limited resources.²⁶⁷ Therefore, the board of an SOC is required to act with the utmost vigilance to ensure the fulfilment of this additional statutory fiduciary duty which is burdensome and would not be required of the directors of private or public companies.

(b) The Duty of Care and Skill

In addition to the statutory fiduciary duties, the Companies Act and the PFMA have also partially codified the duty to act with a degree of care and skill in taking decisions in the best interests of the company.²⁶⁸ However, the Companies Act and the PFMA diverge in respect of the parameters of this duty. The duty of care and skill under the Companies Act comprises an objective and subjective element whilst the PFMA contains a duty which is solely subjective.²⁶⁹

²⁶³ Futuregrowth op cit note 10 at 11.

²⁶⁴ Madonsela op cit note 16 at 20.

²⁶⁵ Ibid at 20.

²⁶⁶ Madonsela op cit note 256 at 21; Madonsela op cit note 16 at 310.

²⁶⁷ Ibid at 125.

²⁶⁸ Companies at op cit note 11 at section 76 (3)(c); PFMA op cit note 11 at section 50 (1)(a).

²⁶⁹ Wiese op cit note 88 at 76; Cassim op cit note 63 at 559.

The PFMA requires that the board act with the ‘*utmost care to ensure the reasonable protection of the assets and records of the public entity*’.²⁷⁰ Despite the inclusion of an element of reasonableness, which is objective but only in relation to the amount of protection to be given, the test of ‘*utmost care*’ is subjective and refers to what the board considers to be in its utmost care.²⁷¹ There is no prescribed minimum standard of care and the test is solely determined in reference to those directors’ states of mind which is proven with evidence gained from those directors. The complete subjectivity of this duty under the PFMA, stemming from common law precedent, may leave it open to abuse by the board and therefore undermine its enforceability.²⁷²

The Companies Act requires a degree of care, skill and diligence that may reasonably be expected of a person carrying out those same functions and having the same knowledge, skill and experience of that director.²⁷³ This duty sets out a test for the director’s actions or decision taking which comprises both an objective and subjective element.²⁷⁴ The first leg of the test is objective in that it tests the director’s care, skill and diligence against that of a reasonable person carrying out the same functions as those carried out by that director.²⁷⁵ The second leg of the test is subjective in that the knowledge, skill and experience of that particular director must be taken into consideration.²⁷⁶

For inexperienced directors, there is a minimum standard of care and skill which must be displayed whereas experienced directors will be held to a much higher standard, given their breadth of knowledge, experience and skillset.²⁷⁷ The dual objective and subjective nature of the duty of care and skill under the Companies Act is implemented to increase the accuracy of the test in order to establish whether a specific director has fulfilled his or her duty.²⁷⁸ The addition of the element of reasonableness and objectivity to the duty of care and skill in the Companies Act serves to upgrade

²⁷⁰ PFMA op cit note 11 at section 50 (1)(a).

²⁷¹ Ibid.

²⁷² Wiese op cit note 63 at 76; *Re Brazilian Rubber Plantations & Estates Ltd* [1911] Ch 425 (CA) 437; *Re City Equitable Fire Insurance Co* [1925] ch 407; *Fisheries* case supra note 248.

²⁷³ Companies Act op cit note 11 at section 76 (3)(c)(ii) & (iii).

²⁷⁴ Cassim op cit note 63 at 523.

²⁷⁵ Ibid at 599; Companies Act op cit note 11 at section 76 (3)(c)(i).

²⁷⁶ Ibid at 559; Wiese op cit note 63 at 76; Companies Act op cit note 11 at section 76 (3)(c).

²⁷⁷ Ibid.

²⁷⁸ Ibid

the traditional duty, which was completely subjective and to align it with modern international trends and foreign law jurisprudence.²⁷⁹

The duty of care and skill, as set out in the common law, PFMA and Companies Act, should be applied concurrently by the board of an SOC and its directors to the extent that it is reasonably possible to do so.²⁸⁰ The concurrent application of this duty will assist in attempting to ensure the utmost protection of the stakeholders' interests, primarily focusing on the state as the sole shareholder and promote the accountability of decisions taken by the directors of an SOC.

(c) *Other Duties*

The board of an SOC must also comply with the general statutory duties under section 51 of the PFMA.²⁸¹ These general duties focus on the financial governance of the SOC and include duties relating to: compliance with tax regulations, safeguarding assets, management of revenue, expenditure and liabilities, internal and external audit controls, an appropriate and fair procurement and provisioning system, managing working capital, collecting revenue and preventing irregular, fruitless and wasteful expenditure.²⁸²

In addition, the board is required to effectively discharge a human relations role in respect of the disciplinary measures against employees of the SOC.²⁸³ The board is also responsible for the submission of all reports, notices, returns and other information to Parliament, the Minister (as the relevant executive authority for SOCs under his portfolio) or the National Treasury, as required.²⁸⁴ The board must inform the National Treasury of any new entity which the SOC intends to establish.²⁸⁵ The board must also ensure compliance with the provisions of the PFMA and any other legislation to which the SOC is subject.²⁸⁶ In the event of an inability of the board to comply with its responsibilities in terms of the PFMA, it must promptly report such inability to the Minister and the National Treasury.²⁸⁷

²⁷⁹ Cassim op cit note 63 at 558.

²⁸⁰ Companies Act op cit note 11 at section 5 (4)(a).

²⁸¹ PFMA op cit note 11 at section 51.

²⁸² Ibid at section 51 (1).

²⁸³ Ibid at section 51 (1)(e).

²⁸⁴ Ibid at section 51 (1)(f).

²⁸⁵ Ibid at section 51 (1)(g).

²⁸⁶ Ibid at section 51 (1)(h).

²⁸⁷ Ibid at section 51 (2).

The PFMA also contains requirements with which board of an SOC must comply in respect of information to be submitted to the Minister, National Treasury or Auditor-General.²⁸⁸ The board must compile annual budgets, financial reports and corporate plans which are to be submitted to the Minister and National Treasury or Auditor-General.²⁸⁹ The board of an SOC, as a national government business enterprise, is required to submit annual budgets and corporate plans, in the prescribed form, to the Minister and National Treasury.²⁹⁰ The annual budget comprises a projection of the revenue, expenditure and borrowings for that financial year whilst the corporate plan sets out the strategic plans and affairs of the SOC for the following three financial years.²⁹¹

In addition to the annual budget and corporate plans, the Minister must conclude an annual shareholders compact with the SOCs under his or her portfolio.²⁹² The shareholders compact provides an agreement between the Minister and board of the SOC in respect of the key performance indicators that the SOC is required to fulfil.²⁹³ The shareholders compact is a key document for illustrating the relationship between the Minister and the board of the SOC and is essential for goal orientation and the effective implementation of strategies and plans. The shareholders compact is meant to provide a governance framework from which the board of an SOC can derive a performance guidebook.²⁹⁴

The PFMA also places particular emphasis on the financial affairs of an SOC, over which the board must exercise particular care in the fulfilment of their duties.²⁹⁵ The financial management and oversight of an SOC is emphasized under the PFMA as a result of the widespread financial implications which SOCs may have on the national budget and economy.²⁹⁶ The PFMA stipulates stringent borrowing requirements for SOCs which must be complied with, in order to avoid the implications of liability due to financial misconduct.²⁹⁷

²⁸⁸ Ibid at section 54.

²⁸⁹ Ibid at section 52, 54 & 55.

²⁹⁰ Ibid at section 52.

²⁹¹ Ibid at section 52; Thomas op cit note 9 at 463; Public Finance Management Act Treasury Regulations in GN R225 GG 27388 of 15 March 2005 at reg 29.1.

²⁹² Ibid at reg 29.2.2.

²⁹³ Thomas op cit note 9 at 463.

²⁹⁴ Ibid.

²⁹⁵ PFMA op cit note 11 at section 50.

²⁹⁶ Madonsela, op cit note 16; National Treasury op cit note 38 at 90.

²⁹⁷ PFMA op cit note 11 at ch 10.

In comparison to the PFMA, the Companies Act affords directors a wide discretion in light of their responsibility to manage the business and affairs of the SOC, by allowing them to exercise all powers and perform any functions required, unless their founding legislation or Memorandum of Incorporation ('MOI') provides otherwise.²⁹⁸ The MOI of an SOC may limit the powers of the board by requiring the passing of a shareholders special resolution opposed to the board's ordinary resolution.²⁹⁹ In this way, the state as sole shareholder of an SOC maintains a degree of control over the business and affairs of the SOC in protection of its assets, and the board's control is diluted.³⁰⁰

The MOI can also include additional duties for directors, as long as there is not a conflict with the provisions of the Companies Act, in which case the Companies Act prevails.³⁰¹ The shareholders compact can also be used to specify additional duties for the board of an SOC and should set out as much detail as is reasonably possible for the role and responsibilities of the board.³⁰²

The PFMA makes it clear that the board of an SOC is to be held accountable for ensuring compliance with its provisions.³⁰³ Similarly, there is a reciprocal duty on the Minister to ensure that the board of an SOC complies with its statutory duties to take decisions in the best interests of the SOC at all times. The Minister of Finance also has a duty under the PFMA to hold the board of an SOC accountable for its statutory compliance.³⁰⁴ However, the PFMA does not specify how the board of an SOC is to be held accountable to the state and its various stakeholders.³⁰⁵

The accountability of the board of an SOC is a matter of interpretation in ascertaining whether or not the directors have complied with their statutory and common law duties. The omission of a specific statutory duty to account, while promoting innovation and flexibility, may result in uncertainty and lead to a lack of communication between the board of the SOC and its various stakeholders. A lack of clarity and certainty of the manner in which the board of an SOC is held to account may undermine the board's authority to control and manage the SOC and may diminish

²⁹⁸ Companies Act op cit note 11 at section 66 (1); Bronstein & Oliver op cit note 5 at 29.

²⁹⁹ Ibid at section 65 (11).

³⁰⁰ Bronstein & Oliver op cit note 5 at 29.

³⁰¹ Companies Act op cit note 11 at section 6 (1).

³⁰² PRC *Protocol* op cit note 3 para 5.1.12.1; Bronstein & Oliver op cit note 5 at 29.

³⁰³ PFMA op cit note 11 at section 49.

³⁰⁴ Ibid at section 63 (2).

³⁰⁵ Bronstein & Oliver op cit note 5 at 29.

the effective oversight role which is to be provided by the state, as the sole shareholder.³⁰⁶ Legislation may have to be amended to include a duty to account in the statutory duties with which the board and the directors of SOCs are required to comply. The parameters of this duty to account have not been proposed in this research as they will dependent on the proposed amalgamation of all of the statutory duties, and how these are worded, in the overarching SOE Legislation.

3.4.4 Liability of Directors

The PFMA, Companies Act and common law place numerous duties on the directors of SOCs in an attempt to ensure accountability for their decisions. Actual and significant accountability is only achieved through the implementation of an enforcement mechanism which attempts to ensure that directors effectively discharge their duties. The imposition of statutory liability on the board and the directors of SOCs, in the event of a breach of a statutory or common law duty, under the Companies Act and the PFMA is currently one of the main enforcement mechanisms.³⁰⁷ Fear of the imposition of criminal or personal liability acts as a deterrent for directors of SOCs who are contemplating a breach of their statutory and common law duties.³⁰⁸ In the event of such a breach, the SOC must bring an action against its board, jointly, or its directors, individually, for a breach of the statutory or common law duties under the Companies Act or the PFMA, as set out in the case of *Hlumisa Investment Holdings (RF) Limited and Another v Kirkinis and Others*.³⁰⁹

The board of an SOC, meaning the directors jointly, may be held criminally liable for a grossly negligent breach of certain statutory duties contained in the PFMA, and the directors of the SOC, individually, for certain fraudulent activities in terms of the Companies Act.³¹⁰ Under the Companies Act, the director of an SOC may be held criminally liable in the event of an act of fraud, perpetrated in relation to the SOC, its employees or creditors.³¹¹ Furthermore, the Companies Act allows for directors to be held criminally liable in the event of participation by the directors in the reckless carrying on of the business of the SOC with the intent to defraud.³¹²

³⁰⁶ PWC op cit note 70 at 8.

³⁰⁷ Companies Act op cit note 11 at section 77 (1) – (10); PFMA op cit note 11 at ch 10.

³⁰⁸ Cassim op cit note 63 at 582 – 86.

³⁰⁹ *Hlumisa Investment Holdings (RF) Limited and Another v Kirkinis and Others* [2020] ZASCA 83 para 1.

³¹⁰ Ibid; Companies Act op cit note 11 at section 214; PFMA op cit note 11 at section at 86 (2).

³¹¹ Ibid Companies Act at section 214.

³¹² Ibid at section 22 (1) read with section 214(1)(c).

The board of an SOC may be held criminally liable in the event of a breach of a statutory fiduciary duty, general duty or any other duty, as dictated by the PFMA.³¹³ Section 86 (2) of the PFMA states that the board may be guilty of an offence and liable, on conviction, to a fine or imprisonment, for a maximum of five years if there is a wilful or grossly negligent breach of the fiduciary, general or financial duties.³¹⁴ The inclusion of the condition of wilful or gross negligence conceivably eases the burden on the board as it increases the burden of proof which is required before criminal liability may be imposed. This is due to the severity of imposing criminal liability against directors who are jointly, as the board, guilty of a breach of their statutory duties.

Furthermore, in respect of the Prevention and Combating of Corrupt Activities Act 12 of 2004, SOC directors have a further statutory duty to report any knowledge or reasonable suspicion of fraudulent conduct, by another person, to any police official.³¹⁵ A failure to do so would result in the director possibly being held criminally liable.³¹⁶ Criminal liability, may also be imposed on the SOC, under the Criminal Procedure Act 51 of 1997, for any offence committed as a result of an act or omission of a director in the exercise of his powers or performance of his duties.³¹⁷ The said director will be guilty of the offence as well, unless it can be proven that he did not take part in the commission of the offence or could not have prevented its occurrence.³¹⁸ Therefore, a director can be held criminally liable for any criminal offence committed by the SOC unless he can prove his innocence. This is a serious burden on directors as it shifts the onus of proof onto the director and may result in conviction for a crime for which the director is not responsible.³¹⁹

In addition to the imposition of criminal liability, fear of suspension or dismissal for certain activities may deter SOC directors from breaching their duties under the PFMA.³²⁰ The board of an SOC may be found guilty of committing an act of financial misconduct in the event of a wilful or negligent breach of a fiduciary, general or any other duty under the PFMA, or the making or permitting of an irregular expenditure or fruitless and wasteful expenditure.³²¹ If the board of the SOC is found guilty of financial misconduct then every director is held liable, individually and

³¹³ PFMA op cit note 11 at section 86 (2).

³¹⁴ Ibid at section 86 (2).

³¹⁵ Prevention and Combating of Corrupt Activities Act 12 of 2004 at section 34.

³¹⁶ Ibid.

³¹⁷ Criminal Procedure Act 51 of 1997 at section 332 (2).

³¹⁸ Ibid at section 332 (5).

³¹⁹ Wiese op cit note 63 at 84.

³²⁰ PFMA op cit note 11 at section 83 (1).

³²¹ Ibid.

severally, for the financial misconduct perpetrated by the board.³²² Financial misconduct by the board of an SOC is a ground for the dismissal or suspension of, or sanction against, every director serving on the board regardless of any other legislation.³²³

Unlike its predecessor, the Companies Act does not hold directors criminally liable in the event of a breach of their statutory duties and only in the event of fraudulent conduct.³²⁴ The Companies Act holds directors personally liable in the event of a breach of a statutory or common law duty.³²⁵ The liability of directors is categorized in accordance to the specific breach of duty, whether it be a breach of a fiduciary duty, the duty of care and skill or other statutory or common law duties.³²⁶

Under the Companies Act, the individual directors of an SOC may be held liable for a breach of their duties.³²⁷ The statutory personal liability imposed on directors in the event of a breach of their statutory duties, under the Companies Act, is separated into two distinct categories.³²⁸ First, a director may be held liable, in accordance with the principles of the common law, for a breach of a fiduciary duty, as a result of which the company sustains any loss, damages or costs.³²⁹ This liability specifically refers to a breach of the statutory fiduciary duties relating to a disclosure of a personal financial interest, the duty to avoid a conflict of interest, the duty to act in good faith and for a proper purpose and the duty to act in the best interests of the company.³³⁰

Secondly, a director may also be held liable, in accordance with the principles of the common law relating to delict, for any loss, damages or costs sustained by the company due to a breach of the statutory duty of care and skill, any duty contained in the Companies Act or any provision contained in the company's MOI.³³¹ The statutory delictual liability imposed on directors arises in instances where fiduciary or contractual liability does not arise.³³²

³²² Ibid at section 83 (2).

³²³ Ibid at section 83 (4).

³²⁴ Wiese op cit note 63 at 80; Companies Act op cit note 77; Companies Act op cit note 11 at section 214 & 22 (1).

³²⁵ Companies Act op cit note 11 at section 77 (2).

³²⁶ Ibid at section 77 (2) & (3); Wiese at op cit note 78 at 80.

³²⁷ Ibid.

³²⁸ Cassim op cit note 63 at 584 – 86.

³²⁹ Companies Act op cit note 11 at section 77 (2)(a); Cassim op cit note 63 at 584 – 86.

³³⁰ Ibid.

³³¹ Companies Act op cit note 11 at section 77 (2)(b); Cassim op cit note 63 at 585.

³³² Ibid; Wiese op cit note 63 at 81.

In order for personal liability to be imposed on the director, a causal link needs to be established between the breach and the loss, damage or costs sustained by the SOC.³³³ The director is held personally liable for the loss, damage or cost sustained by the company as a result of his or her breach. All directors may be held liable, jointly and severally, for the same breach which caused the SOC to sustain a loss, damage or cost.³³⁴

The Companies Act places a time limitation on the liability which may be imposed on directors in that proceedings to recover any loss, damage or costs sustained by the SOC must have commenced within three years from the date on which the act or omission, which gave rise to the liability, took place.³³⁵ The director may also be held liable for court costs for all parties involved in the proceedings contemplated in imposing the liability.³³⁶ Furthermore, the director may be required to restore to the SOC any amount improperly paid by the SOC as a result of the breach and which amount is not recoverable in terms of the Companies Act.³³⁷

Directors of SOCs may also, in certain instances, be held personally liable for losses or damages sustained by the shareholders and creditors of the SOC.³³⁸ Shareholders may institute a claim for damages suffered by them as a result of a director acting intentionally fraudulently or with gross negligence which causes the SOC to contravene the Companies Act.³³⁹ In this instance, the directors will be liable to the state as the sole shareholder of the SOC and not to the SOC itself, as a separate legal entity distinct from its shareholder.³⁴⁰

Aggrieved creditors may establish a cause of action holding directors personally liable under the requirements of section 77 (3) and the ‘catch-all’ section 218 of the Companies Act, read with section 22 (1) which restricts a company from carrying on its business recklessly, with gross negligence or the intent to defraud any person.³⁴¹ Our courts have also extended the meaning of ‘sustained by the company’ under section 77 (2) and (3) to allow for any third party to hold a

³³³ Ibid at 81; Companies Act at section 77 (2).

³³⁴ Ibid at section 77 (6).

³³⁵ Ibid at section 77 (7).

³³⁶ Ibid at section 77 8(a).

³³⁷ Ibid at section 77 (8)(b).

³³⁸ Ibid at section 20 (6) (a) & (b); Cassim op cit note 63 at 586.

³³⁹ Ibid.

³⁴⁰ Wiese op cit note 63 at 83.

³⁴¹ Companies Act op cit note 11 at section 218, 77 & 22 (1); *Sanlam Capital Markets (Pty) Ltd v Mettle Manco (Pty) Ltd and Others* (2014) 3 ALL SA 454 (GJ) para 40; *Blue Farm Fashion Limited v Rapitrade 6 (Pty) Ltd and Others* [2016] ZAWCHC 35(WCC); Emile Myburgh ‘Holding Delinquent Directors Personally Liable’ (2017) *De Rebus DR* 29 available at <http://www.derebus.org.za/holding-delinquent-directors-personally-liable/>, accessed on 28 May 2019.

director personally liable for acquiescing to or knowing about conduct that falls within the ambit of the reckless trading provisions under section 22 (1) of the Companies Act.³⁴² The ‘*catch-all*’ cause of action contemplated under section 218 of the Companies Act is discussed in detail under the next heading of this chapter.

The liability imposed on directors, under the Companies Act, is extensive and should act as an effective deterrent for unscrupulous behaviour. However, in the event that liability is not an effective deterrent, the order of a mandatory delinquency declaration by the court may serve as an additional enforcement mechanism for directors’ duties.³⁴³ In the event of a person being found to be personally liable under section 77(3) (a)(b) or (c) of the Companies Act, a court must make an order declaring that person delinquent.³⁴⁴ The result of such an order is that the person will not be allowed to act as a director of any company for a period of seven years, from the date on which the court order was granted.³⁴⁵ This mandatory delinquency provision acts as a safeguard, protecting other companies from falling victim to the disastrous effects of an unscrupulous director.³⁴⁶

There are various discrepancies between the liability provisions contained in the Companies Act and the PFMA. One of the most predominant and confusing is reference in the PFMA to the board of an SOC being guilty of an offence and being held criminally liable, in terms of a fine or imprisonment.³⁴⁷ Unlike personal liability, it seems improbable to hold directors on the board of an SOC jointly and severally liable in the imposition of criminal liability. A possible interpretation of this provision is that the entire board of the SOC is held criminally liable and the onus is on each and every director to prove their innocence, thereby exempting himself or herself from liability.

The board of an SOC, jointly, as well as the directors, individually, may be subject to the imposition of personal or criminal liability, in the event of a breach of the statutory duties under

³⁴² *Rabinowitz v Van Graan and Others* 2013 (5) SA 315 (GSI).

³⁴³ Companies Act op cit note 11 at section 162 (5)(c)(iv) read with section 22 (1), 77(3)(b) and 218 (2); *Rabinowitz* case supra note 357; *Gihwala and Others v Grancy Property Ltd and Others* 2017 (2) SA 337 (SCA).

³⁴⁴ *Ibid.*

³⁴⁵ Myburgh op cit note 356 at 5.

³⁴⁶ *Organisation Undoing Tax Abuse & Others v Duduzile Cynthia Myeni & Others* [ZAGPPHC] unreported case no. 15996/2017 on 27 May 2020.

³⁴⁷ PFMA op cit note 11 at section 86 (2).

the PFMA and the Companies Act.³⁴⁸ Therefore, as SOCs are subject to the concurrent application of the PFMA and the Companies Act, it is submitted that the legislature sought to ensure that the strong enforcement mechanisms are utilized against the board of an SOC and its directors through the possible imposition of criminal and personal liability.

(a) *New Remedy for the Public*

The Companies Act introduced the possibility of an innovative remedy for the stakeholders of an SOC against its directors.³⁴⁹ Section 218 (2) reads that ‘*Any person who contravenes any provision of this Act is liable to any other person for any loss or damage suffered by that person as a result of that contravention*’.³⁵⁰ This provision expands the statutory liability of directors to be held personally liable, not only to the SOC, but to other persons who have suffered any loss or damages as a result of a contravention of the Companies Act.³⁵¹ This remedy has been referred to as a ‘*catch-all*’ provision as it is couched in very broad terms in that any person can institute proceedings against any other person for a contravention of the Companies Act.³⁵²

Our courts have debated whether the broad ambit of section 218 (2) allows for dissatisfied investors to institute proceedings against the director of a company, alleging that the director’s breach of the Companies Act has resulted in the investor suffering a loss or damage, mainly resulting from a diminution in the value of the shares of the company.³⁵³ The predominant requirements under section 218 (2) are twofold. First, there would have to be a causal link between the loss or damage suffered by the person and the director’s contravention of the Companies Act.³⁵⁴ Secondly, the person must prove to have actually suffered a loss or damage, which is differentiated from the loss or damage suffered by the company, as a result of the director’s breach of the Companies Act.³⁵⁵

³⁴⁸ PFMA op cit note 11 at section 83 & 86 (2); Companies Act op cit note 11 at section 77 (2) & (3).

³⁴⁹ Companies Act op cit note 11 at section 218 (2); *Rabinowitz v case supra* note 357.

³⁵⁰ *Ibid.*

³⁵¹ Wiese op cit note 63 at 83.

³⁵² Cassim op cit note 63 at 821.

³⁵³ *De Bruyn v Steinhoff International Holdings N.V and Others* [ZAGPJHC] unreported case no 29290/2018 of 26 June 2020 para 180; *Hlumisa case supra* note 309 para 1.

³⁵⁴ Companies Act op cit note 11 at section 218 (2).

³⁵⁵ *Hlumisa case supra* note 309 para 38.

Recent case law indicates that satisfying these two requirements has proved a challenging task for those wanting to institute claims under section 218 (2).³⁵⁶ Shareholders of African Bank Investments Limited ('ABI') launched an unsuccessful damages claim under section 218 (2) against the directors of ABI for the loss they allegedly suffered as a result of a diminution in the value of their shares.³⁵⁷ The shareholders claimed that the directors of ABI breached section 22 (1) and section 76 (2) and (3) of the Companies Act which resulted in a drop in the share price causing the shareholders to suffer a loss of their investments.³⁵⁸

The Supreme Court of Appeal upheld the precedent set by previous courts in terms of the 'reflective loss principle' which states that the shareholders cannot claim for a loss suffered by them which is merely a reflection of the loss suffered by the company.³⁵⁹ The claim of the shareholders needs to be distinct from that of the company to avoid both the company and the shareholder making claims against the directors of a company based on the same set of facts.³⁶⁰ Following case precedent, the court held that a drop in the share price did not constitute a loss that was suffered by the shareholders that was distinct from the loss suffered by ABI itself.³⁶¹

Under the 'reflective loss principle', the shareholders may not even institute a claim if the company decides not to pursue action against the directors.³⁶² The only exception to the principle is that a shareholder, who has a separate cause of action, may institute a claim against a director where the company is unable to proceed due to the wrongful act of the director.³⁶³ In this instance, the 'loss or damage' requirement would be fulfilled regardless of whether it is reflective of the company's loss.³⁶⁴

Furthermore, the corresponding provision for a remedy in the event of a breach by directors of section 76 (3) is 77 (2) and section 218 (2) cannot be used as a general remedy when a specific remedy under the Companies Act is already available.³⁶⁵ The shareholders of Steinhoff

³⁵⁶ Ibid.

³⁵⁷ Ibid.

³⁵⁸ Ibid para 40.

³⁵⁹ Ibid para 41; *Johnson v Gore, Wood & Co* [2002] 2 AC 1 (HL) 62; *Izikowitz v ABSA Bank Limited* 2016 (4) SA 432 (SCA); Cassim op cit note 63 at 822.

³⁶⁰ Ibid.

³⁶¹ *Hlumisa* case supra note 309 para 52.

³⁶² Ibid; *Johnson* case supra not 375; *Izikowitz* case supra note 375.

³⁶³ *Giles v Rhind* [2003] Ch 618 (CA); *Perry v Day* [2005] BCLC 405; Cassim op cit note 63 at 823.

³⁶⁴ Ibid.

³⁶⁵ *Hlumisa* case supra note 309 para 12; *De Bruyn* case supra note 353 at 189.

International Holdings N.V (‘Steinhoff’) also unsuccessfully attempted to bring a claim under section 218 (2) against the directors for a breach of their statutory duties which resulted in the diminution of the value of their shares.³⁶⁶ Following the precedent set by the High Court in the *Hlumisa* judgement, the court held that the shareholders of a company do not have a cause of action under section 218 (2) against the directors a company for a diminution of the value in their shares which is simply a reflection of the loss suffered by the company.³⁶⁷

As a result of the precedent set by the Supreme Court of Appeal in the *Hlumisa* case, it would be difficult for stakeholders to satisfy the requirements under section 218 (2) to institute proceedings against directors of SOCs for a contravention of the Companies Act.³⁶⁸ It should be left to the board of the SOC to the institute a claim against its directors for a breach of their statutory duties under the Companies Act, as may be the case for the directors of Eskom.³⁶⁹

For SOCs, the implications of a successful claim under the catch-all remedy may be drastic in that any member of the public, as a stakeholder, may institute proceedings against a director of an SOC for loss which they suffered as a result of a contravention of the Companies Act. SOCs cannot even seek refuge under the specific requirements for the organs of state under the provisions of the Institution of Legal Proceedings Against Certain Organs of State Act 40 of 2002.³⁷⁰ In accordance with relevant case law, SOCs which are not specifically mentioned under section one of the aforesaid statute cannot be classified as organs of state and, therefore, the said statute does not apply to them.³⁷¹

However, due to the strict decision laid down in the *Hlumisa* judgment, it is arguable that substantiating a causal link between the loss suffered to the public and a contravention by the

³⁶⁶ *De Bryun* at 186; *Hlumisa Investment Holdings (RF) Limited and Another v Kirkinis and Others* 2019 (4) SA 569 (GP).

³⁶⁷ *Ibid.*

³⁶⁸ *Hlumisa* case supra note 309.

³⁶⁹ Mayibongwe Maqhina ‘Eskom goes to court to recover billions from former executives, Guptas’ *IOL* 3 August 2020 available at <http://www.iol.co.za/news/politics/eskom-goes-to-court-to-recover-billions-from-former-executives-guptas-9fa5da35-057d-4d11-8e3e-1e250dfd50e8> accessed on 26 August 2020; Owen Skae ‘The fault does not lie with King IV’ *Moneyweb* 25 August 2020 available at <http://www.moneyweb.co.za/moneyweb-opinion/soapbox/the-fault-does-not-lie-with-king-iv/> accessed on 26 August 2020.

³⁷⁰ Institution of Legal Proceedings Against Certain Organs of State Act 40 of 2002.

³⁷¹ *Haigh v Transnet Ltd (ZANCHC)* unreported case no 2115/2010 of 2 December 2011.

directors of the Companies Act may prove the undoing in the public's attempt to hold directors of an SOC liable in terms of a section 218 (2) claim.³⁷²

(b) *Business Judgement Rule, Relief, Condonation, Insurance and Indemnities*

The possible imposition of criminal and personal liability, in the event of a breach of a statutory duty, may result in persons being reluctant to serve as directors on the board of an SOC. However, there are a number of statutory safeguards available to directors which may, in certain instances, serve to negate the punishment levied against them. These safeguards include: codification of the 'business judgement rule', relief from the court, condonation from shareholders and director's indemnification and insurance.³⁷³

In an attempt to counter the higher governance standards placed on directors by the Companies Act, the common law business judgment rule was partially codified.³⁷⁴ The rule is aimed at providing protection for directors against potential liability claims, subject to compliance with certain requirements.³⁷⁵ In order to comply with the rule and be exempt from liability, the director must have taken reasonable steps to be informed, should not have a financial interest and should have a rational basis for believing, and did believe, that the decision taken was in the best interests of the company.³⁷⁶

Rationality is based on the connection between the purpose for which the power was given to the director and the decision taken by the director.³⁷⁷ There must be a rational connection between the decision taken and the purpose of the power, in order for the requirement to be fulfilled.³⁷⁸ Directors are also allowed to rely on the performance of, or information provided by, designated persons, in taking their decisions.³⁷⁹ However, there is a minimum standard of reasonableness in terms of the information provided and the performance of the person which is required to make the reliance acceptable.³⁸⁰ If the requirements of the business judgement rule are satisfied, the

³⁷² *Hlumisa* case supra note 309.

³⁷³ Wiese op cit note 63 at 85; Cassim op cit note 63 at 563.

³⁷⁴ Companies Act op cit note 11 at section 76 (4).

³⁷⁵ Wiese op cit note 63 at 77.

³⁷⁶ Companies Act op cit note 11 at section 76 (4); Wiese op cit note 63 at 79; Cassim op cit note 63 at 564.

³⁷⁷ Wiese op cit note 63 at 78.

³⁷⁸ *Visser Citrus (Pty) Ltd v Goede Hoop Citrus (Pty) Ltd and Others* 2014 (5) SA 179 (WCC).

³⁷⁹ *Ibid*; Companies Act op cit note 11 at section 76 (4)(b) & (5).

³⁸⁰ *Ibid*; Wiese op cit note 63 at 79.

director will have discharged his statutory fiduciary duty and the duty of care and skill, acting in the best interests of the company.³⁸¹

In addition to the business judgement rule, the Companies Act allows for a court, on any terms it considers just, to partially or wholly relieve a director from any liability, if the director is or may be liable but has acted honestly and reasonably or having regard to all of the circumstances of the case, it would be fair to excuse the director.³⁸² The exemption by the court does not extend to instances where the director is liable due to wilful misconduct or wilful breach of trust.³⁸³

Furthermore, the shareholders of the company may also condone, through ratification by way of a special resolution, any act of the director which contravenes a restriction in the company's MOI, pertaining to powers of the company or the authority of the director.³⁸⁴ The condonation of a director's contravention by the shareholders may still expose the director to being held liable, in terms of third party claims initiated against him or her under section 218 of the Companies Act.³⁸⁵ Shareholders are not able to condone, through ratification, a director's contravention of a provision in the Companies Act.³⁸⁶

A company may also provide an indemnity to a director, in terms of any liability which may arise, unless such indemnification is restricted by the company's MOI.³⁸⁷ There are certain instances for which the indemnification of directors by the company is limited. Directors will not be indemnified by the company in the following instances: in the event of gross negligence or fraudulent conduct in the reckless carrying on of business, intentional defrauding of a creditor, shareholder or employee of the company, liability due to wilful misconduct or wilful breach of trust or a fine imposed on the director as a result of being convicted of an offence.³⁸⁸

Moreover, a company is allowed to purchase insurance to protect a director against any liability or expense for which the company is permitted to indemnify the director, unless otherwise restricted in the company's MOI.³⁸⁹ Companies tend to, therefore, take out director and officer insurance

³⁸¹ Companies Act op cit note 11 at section 76 3(b) & (c) & (4)(a)(i), (ii) & (iii).

³⁸² Ibid at section 77 (9).

³⁸³ Ibid; Wiese op cit note 63 at 85.

³⁸⁴ Ibid at section 20 (2).

³⁸⁵ Ibid at section 20 (3); Ibid at 86.

³⁸⁶ Ibid.

³⁸⁷ Ibid at section 78 (5).

³⁸⁸ Ibid at section 78 (6).

³⁸⁹ Ibid at section 78 (7).

with reputable insurance companies, in order to cover any losses incurred by the company or any third party as a result of a director executing his duties in good faith but still being held liable under the Companies Act.³⁹⁰

The potential imposition of criminal and personal liability, together with an order of delinquency, serve as retribution-based enforcement mechanisms to ensure that directors discharge their duties in order to avoid punishment. However, the numerous statutory safeguards available to directors in the event the possible imposition of liability tend to dilute these enforcement mechanisms. Directors may rely too heavily on the safeguards thereby negating the effectiveness of utilizing liability to deter breaches of duties. The duties for SOC directors must be enforceable otherwise their effectiveness in holding directors to account for their decisions is largely nullified.

An alternative to current retribution-based enforcement mechanism is the implementation of a reward-based enforcement mechanism which incentivizes directors to effectively fulfil their duties. Such incentive methods may include the granting of share options to the directors or linking corporate performance to directors' remuneration and bonus payment structures.³⁹¹ Although the granting of share options to directors may create a conflict of interest between the ability of the director to discharge his duties to the company and his own personal interest by virtue of his or her shareholding in the company. This reward-based mechanism may be more suited for executive as opposed to non-executive directors and the granting of share options may not be suitable for SOCs where the state is the sole shareholder.

3.5 The Board

The board is required to manage and direct the affairs of the SOC unless restricted by its MOI or founding legislation.³⁹² The board of any company has two primary functions: to determine the strategic direction of the SOC and to exercise control over it.³⁹³

As discussed, the PFMA requires that the board of an SOC must be held accountable for the purposes of compliance with the PFMA.³⁹⁴ King IV also emphasizes the principle of accountability as a fundamental concept of the board's primary governance roles and

³⁹⁰ Wiese op cit note 63 at 86.

³⁹¹ Ibid at 88.

³⁹² Companies Act op cit note 11 at section 66 (1).

³⁹³ King III op cit note 217 at ch 1 & 7.

³⁹⁴ PFMA op cit note 11 at section 49(2)(a).

responsibilities.³⁹⁵ The board of an SOC must be accountable for the SOC's performance through, *inter alia*, effective and efficient reporting and disclosure mechanisms.³⁹⁶ The board also oversees and monitors the implementation and execution of strategic plans and policies by management which will serve to enhance the accountability and performance of an SOC.³⁹⁷

Therefore, the importance of the role of the board in accounting for the governance, performance, strategic planning and control of the SOC cannot be understated.³⁹⁸ There are three primary aspects pertaining to the accountability of the board of an SOC: its composition, the role of the independent non-executive directors and the governance of board meetings.

Under the first aspect, the composition of the board of an SOC is addressed. The Companies Act only specifies requirements pertaining to the composition of the audit committee and the social and ethics committee of an SOC.³⁹⁹ However, it provides no requirements for the general composition of the board of an SOC, in respect of the independence, diversity, skills, knowledge, experience and qualifications of the directors, unless otherwise stated in the SOC's founding legislation or its MOI.⁴⁰⁰ The Companies Act sets a requirement for the minimum number of directors to serve on the board of an SOC which is three, subject to the MOI and founding legislation.⁴⁰¹ Recommended practices for the board composition of an SOC, specifically the skills, knowledge, experience, independence and diversity of the directors, is suggested in King IV but is not a mandatory requirement.⁴⁰²

SOCs in South Africa comprise a unitary board composition where all of the directors, executive and non-executive, sit together for board meetings.⁴⁰³ This unitary board structure is advocated as the most appropriate board structure for South African companies by the King III Report on Corporate Governance for South Africa ('King III').⁴⁰⁴ The King IV report does not mention the recommendation of a unitary board structure for SOC's but focuses on providing recommendations

³⁹⁵ King IV op cit note 19 at 21.

³⁹⁶ Ibid.

³⁹⁷ Ibid; Thabane op cit note 9 at 6; Futuregrowth op cit note 10 at 4.

³⁹⁸ Ibid; *Mpofu* case supra note 96 para 60.

³⁹⁹ Companies Act op cit note 11 at section 94 & 72 (4)(c); John Olson 'South Africa moves to a Global Model of Corporate Governance but with Important National Variations' 2010 *Acta Juridica* 219-247 at 227; Masuku op cit note 184 at 119.

⁴⁰⁰ Bronstein & Oliver op cit note 5 at 22.

⁴⁰¹ Companies Act op cit note 11 at section 66 (2)(a).

⁴⁰² King IV op cit note 19 at 50 – 52 & 115; Wiese op cit note 63 at 30.

⁴⁰³ King III op cit note 217 para 62 at 38; Cassim op cit note 63 at 482.

⁴⁰⁴ Ibid.

in terms of the appropriate mix of the skills, knowledge, independence and experience of the directors serving on the board.⁴⁰⁵

Under the second aspect, the role played by the independent non-executive directors of an SOC is examined. There is no statutory differentiation between executive and non-executive directors and all directors, regardless of their categorization, are required to take decisions in the best interests of the SOC.⁴⁰⁶ However, the specific roles which executive and non-executive directors, especially the independent ones, are required to fulfil whilst serving on the board of the SOC are very different.⁴⁰⁷

The common law, together with the King Codes and Reports, provide the primary sources of law in distinguishing between and interpreting the roles which executive and non-executive directors are required to perform.⁴⁰⁸ King IV recommends a transparent disclosure of the categorization of each director as an executive director, non-executive director or an independent non-executive director as well as the reasons for such distinction.⁴⁰⁹ Transparency in director selection and the categorization of directors is imperative to ensuring satisfactory board composition, in relation to a diverse range of skills, knowledge and experience.⁴¹⁰

In terms of their roles, non-executive directors are not involved in the day-to-day management of the SOC and they provide a supervisory role in the execution of their duties in the best interests of the SOC which role is performed on an intermittent basis at board meetings.⁴¹¹ Executive directors provide a management role to strategically steer and control the SOC.⁴¹² Executive directors are involved in the daily operations of the SOC and discharge their duties on a continual basis.⁴¹³ Executive directors are under an employment relationship with the SOC, whereas, non-executive directors are independently contracted to the SOC for certain periods.⁴¹⁴

⁴⁰⁵ King IV op cit note 19 at 50.

⁴⁰⁶ Companies Act, op cit note 11 at section 1; Stevens, Richard Stevens 'The Legal Nature of the Duty of Care and Skill: Contract or Delict' (2017) 20 *PER/PERJ* at 3.

⁴⁰⁷ *Ibid.*

⁴⁰⁸ *Ibid* at 2; King III op cit note 217 at annex 2.2; Cassim op cit note 63 at 477.

⁴⁰⁹ King IV op cit note 19 at 52.

⁴¹⁰ Stevens op cit note 422 at 8; Fisheries case supra note 248 at 165H – 166B.

⁴¹¹ *Ibid.*

⁴¹² *Ibid*; Fisheries case supra note 248.

⁴¹³ *Ibid.*

⁴¹⁴ Stevens op cit note 422 at 12; Cassim op cit note 63 at 477.

The board of an SOC and its directors are bound, in performing their differing roles, to fulfil their duties in respect of the common law, the PFMA, the Companies Act, the MOI and founding legislation.⁴¹⁵ Labour law legislation may also be applicable to the employment relationship between the SOC and the executive director.⁴¹⁶ All directors, regardless of their categorization, owe fiduciary duties as well as the duty of care and skill to the SOC. In the event of a breach of a duty, the board or director of an SOC may be held liable under the provisions of the PFMA or the Companies Act.⁴¹⁷

The Companies Act suggests a distinction between the duties of executive and non-executive directors under the statutory duty of care and skill.⁴¹⁸ The test under this statutory duty compares the care, skill and diligence of the director in question with the care, skill and diligence which can be reasonably expected of a person ‘*carrying out the same functions in relation to the company as those carried out by the director*’.⁴¹⁹ The function or role to be provided by the director, as an executive or non-executive director, will have an impact on the outcome of the test for the statutory duty of care and skill.

A non-executive director will have breached his duty if he fails to perform his role to act independently and supervise the decisions taken by the executive directors, in the best interests of the SOC.⁴²⁰ An executive director will have breached his duty if he fails to perform his management role in taking decisions to strategically control, steer and manage the SOC, in its best interests.⁴²¹ In this respect, the liability imposed on directors, in respect of a breach of their duty of care and skill, is determined based on the facts of each case, with reference to the functions carried out by that director, as an executive or non-executor director, together with his or her skill, knowledge and experience.⁴²²

The most contested issue around board composition remains the hotly debated topic surrounding the number of executive and independent, non-executive directors, that should serve on the

⁴¹⁵ Ibid; PFMA op cit note 11 at section 1, 50 & 51; Companies Act op cit note 11 at section 1 & 76.

⁴¹⁶ Stevens op cit note 422 at 13.

⁴¹⁷ Ibid; PFMA op cit note 11 at section 83 (2) & 86 (2); Companies Act op cit note 11 at section 77 (2).

⁴¹⁸ Ibid at section 76 (3).(c)(i).

⁴¹⁹ Ibid.

⁴²⁰ Stevens op cit note 422 at 23.

⁴²¹ Ibid.

⁴²² Ibid.

board.⁴²³ There are differing legal perspectives as to whether a board composition comprising a majority of independent, non-executive directors contributes to the achievement of accountability, improves the performance of the company and prevents conflicts of interest.⁴²⁴

The King Codes advocate a board composition for all companies, including SOCs, which consists of a majority of non-executive directors, most of whom should be independent and a minority of executive directors.⁴²⁵ King IV suggests the presence of at least two executive directors, usually the chief executive officer ('CEO') and chief finance officer ('CFO'), in order to ensure more than one point of direct interaction with management at board meetings.⁴²⁶ The independent, non-executive directors comprise the chairperson together with a number of independent, non-executive directors.⁴²⁷ All of the directors are appointed by the state, as the sole shareholder of the SOC.⁴²⁸

Independent, non-executive directors are appointed for the purpose of providing objectivity and ensuring the avoidance of conflicts of interests by bringing an external, independent perspective to the management of the company.⁴²⁹ King IV emphasizes the importance of independency as a critical element of board decision taking by providing a very detailed definition of 'independence':

*Independence generally means the exercise of objective, unfettered judgement. When used as the measure by which to judge the appearance of independence or to categorise a non-executive member of the governing body or its committee as independent, it means the absence of an interest, position or association or relationship which, when judged from the perspective of a reasonable and informed third party, is likely to influence unduly or cause bias in decision-making.*⁴³⁰

The independence of directors is twofold. First, all directors who take decisions in the best interests of the SOC, should bring an independent mind to bear on the issues at hand and should not be influenced by other directors but should deliberate each decision taken based on their own

⁴²³ Cassim op cit note 63 at 411 & 477; Sanjai Bhagat & Bernard Black 'The Non-Correlation Between Board Independence and Long-Term Economic Performance' (2001) 27 *Journal of Corporate Law* 231 at 235; Olson op cit note 399 at 235; King IV op cit note 19 at 50; Stevens op cit note 422 at 8; Michael Blackman et al *Commentary on the Companies Act* (2002) at 8.

⁴²⁴ Wiese op cit note 63 at 32.

⁴²⁵ King IV op cit note 19 at principle 7 at 50 & 115.

⁴²⁶ Ibid.

⁴²⁷ Ibid at 53 & 115.

⁴²⁸ Ibid.

⁴²⁹ Cassim op cit note 63 at 478; Wiese op cit note 63 at 32.

⁴³⁰ King IV op cit note 19 at 13.

reasoning.⁴³¹ Secondly, in order to be classified as an independent, non-executive director, the director's independence must be continuously analysed to ensure its authenticity.⁴³² King IV provides recommendations to retain the independence of directors, including: effective rotation and succession planning of the board members, maximum time periods for serving on the board and the continuous assessment of the independence and identification of any conflicts of interest, real or perceived.⁴³³

There are many critics of the recommendation of a majority of independent, non-executive directors on the board. Opponents of the recommendation argue that there is not enough empirical evidence to support the claim that a majority of independent, non-executive directors results in better governance or corporate performance.⁴³⁴ Furthermore, an emphasis on the majority rule to the extent of only appointing two executive directors on a board, of a total of say twelve directors, may actually be counterproductive. An overemphasis of supervisory and compliance roles over the strategic management of the company may actually hinder corporate performance.⁴³⁵

The intermittent nature of the role of the independent, non-executive directors, in relation to their attendance at board meetings together with their huge reliance on the information provided by the executive directors is, arguably, disadvantageous to their supervisory roles.⁴³⁶ Independent, non-executive directors may also have other interests and other directorships which require their focus and attention which may detract from their capacity to effectively fulfil their duties.⁴³⁷ King III advocates for a reasonable number of directorships so as not to impede the effectiveness of the role which the director brings to each board meeting.⁴³⁸ King IV requires that the number of other directorships be taken into consideration when appointing independent, non-executive directors.⁴³⁹

A more balanced approach in respect of the number of independent, non-executive and executive directors, would serve to better the accountability of the board. Arguably, a balanced board composition would constitute a 60 to 40 per cent ratio, in favour of the independent, non-executive

⁴³¹ Ibid; Cassim op cit note 63 at 478.

⁴³² Ibid; Stevens op cit note 422 at 8.

⁴³³ Ibid; King IV op cit note 19 at 51 & 52.

⁴³⁴ Wiese op cit note 63 at 32; Bhagat op cit note 440 at 235; Olson op cit note 399 at 237.

⁴³⁵ Ibid; Bhagat op cit note 440 at 240.

⁴³⁶ Ibid at 241; Cassim op cit note 63 at 478.

⁴³⁷ Ibid.

⁴³⁸ King III op cit note 217 para 84 at 41.

⁴³⁹ King IV op cit note 19 at principle 35 at 53.

directors. An over reliance on the number of independent, non-executive directors may detract from the importance of the role which executive directors play, in terms of the strategic planning, control and management of the SOC. Furthermore, more than two points of contact would be beneficial for the independent, non-executive directors, as the recommendation of only the CEO and CFO, serving on the board, will only provide for a minimum amount of information from the SOC's executive perspective.

Whilst a majority of independent, non-executive directors cannot guarantee the effective supervision of the board, they are still an indispensable accountability cornerstone for all companies, including SOCs.⁴⁴⁰ The foundation for the success of the role played by the independent non-executive directors lies in the complete comprehension of the exact duties and roles required of directors in their appointment to the board.⁴⁴¹ An independent, non-executive director who does not understand the supervisory and compliance roles expected of him or her, cannot effectively, if at all, discharge his or her fiduciary duties or the duty of care and skill, in acting in the best interests of the SOC.

In addition to its composition, the board of an SOC must always adhere to the minimum statutory requirements regarding its meetings. The right to requisition a meeting, the number of meetings per annum, notice of meetings, quorums, voting rights and processes, minutes, records and resolutions are all board governance requirements mandated by the Companies Act and PFMA.⁴⁴² The SOC's MOI or its founding legislation may adjust the alterable statutory governance standards to make them more, and not less, stringent on the board.⁴⁴³ Fulfilment of these minimum governance standards for board meetings is another mechanism used by the legislature in attempting to ensure the utmost accountability of an SOC.⁴⁴⁴

3.6 The Committees

The board of an SOC may appoint any number of committees and delegate to any committee any authority of the board, unless the founding legislation or MOI provide otherwise.⁴⁴⁵ However, for

⁴⁴⁰ Ibid at 51.

⁴⁴¹ Cassim op cit note 63 at 478.

⁴⁴² Ibid at 462 – 7; Wiese op cit note 63 at 38 – 9; PFMA op cit note 11 at ch 6; Companies Act at ch 2 part F & section 73.

⁴⁴³ Ibid Companies Act at section 73.

⁴⁴⁴ *Mpofu* case supra note 96 para 39.

⁴⁴⁵ Cassim op cit note 63 at 457; Companies Act op cit note 11 at section 72 (1).

SOCs the appointment of an audit committee and a social and ethics committee is compulsory.⁴⁴⁶ Other committees which are recommended, but not compulsory include: a risk committee, a remuneration committee and a nominations committee.⁴⁴⁷ The committees established by the board may be standing committees which perform a continuous function or ad hoc committees, which are required to perform only a specific or once-off task.⁴⁴⁸

The members of the committees, unless otherwise stated in the MOI or founding legislation of the SOC, may be directors or other persons who are not directors, subject to certain qualifications prescribed by the Companies Act.⁴⁴⁹ It is generally not common or advisable to appoint persons who are not directors to the committees due to the fact that such persons would be subject to the same duties and liabilities as directors which may dissuade their participation.⁴⁵⁰ The board and its directors remain accountable for the execution of their responsibilities and duties, despite delegation of any of the board's authority to a committee.⁴⁵¹

Board committees are established for the delegation of selected responsibilities from the board to the committee.⁴⁵² King IV recommends the formal establishment and approval of terms of reference for each committee.⁴⁵³ The terms of reference should include the composition and rotation of the committee members, details of the committee's role as well as the specific details of the delegated responsibilities, available resources, access to information and meeting procedures.⁴⁵⁴ The composition, functions and meetings of the audit committee are legislated by the PFMA and Companies Act due to its importance in the financial regulation of the SOC.⁴⁵⁵ The same is true of the composition, functions and meetings of the social and ethics committee, although the prescribed requirements are not as stringent or numerous as those pertaining to the audit committee.⁴⁵⁶

⁴⁴⁶ Ibid at section 94 (2), 84 (4)(c), 72 (4)' Companies Act Regulations in GN R351 GG34239 of 26 April 2011 at reg 43 (1).

⁴⁴⁷ Wiese op cit note 63 at 45 -6; King IV op cit note 19 principle 8 at 54 - 7.

⁴⁴⁸ Ibid at 40.

⁴⁴⁹ Companies Act op cit note 11 at section 72 (2).

⁴⁵⁰ Wiese op cit note 63 at 41.

⁴⁵¹ Cassim op cit note 63 at 457; King IV op cit note 19 at 9; *Barlows Manufacturing Co Ltd v RN Barrie (Pty) Ltd* 1990 (4) SA 608 (C) at 610 -11; Companies Act op cit note 11 at section 94 (10).

⁴⁵² King IV op cit note 19 principle 8 at 54.

⁴⁵³ Ibid.

⁴⁵⁴ Ibid.

⁴⁵⁵ Companies Act op cit note 11 at section 94, 72 (4) & reg 43 (1); PFMA op cit note 11 at section 77; Wiese op cit note 63 at 42.

⁴⁵⁶ Wiese op cit note 63 at 43.

Board committees play an important role in the internal accountability structure of SOCs. Effectively functioning committees are accountable to the board for the performance of their responsibilities through efficient disclosure mechanisms.⁴⁵⁷ The board is ultimately accountable for the execution of the responsibility which has been effectively fulfilled by the committee.⁴⁵⁸ Arguably, the board may improve its own performance through delegation by structuring an efficient committee system to execute its numerous responsibilities. The delegation of responsibilities to various committees is meant to act as a mechanism to improve and not deter the accountability of the board

3.7 Shareholder Supervision

The shareholders of a company can perform an important internal accountability check on the directors. The performance of the company is the focal point for shareholders whose investment is directly affected by the financial performance of the company.⁴⁵⁹ There are a number of statutory mechanisms which attempt to ensure that the shareholders of a company maintain a measure of control over the affairs of the board, thereby attempting to protect their investment.⁴⁶⁰ In this way, the shareholders ensure that the board is held accountable for its decision taking, in the best interests of the company. However, in the case of an SOC the effect of shareholder supervision, in holding the board accountable, is significantly diluted due to the state being its sole shareholder.

3.7.1 Forms of Shareholder Supervision

There are various forms of shareholder supervision which promote activism and are legislated through the Companies Act.⁴⁶¹ The most predominant of which include: the passing of shareholder resolutions, shareholder meetings and mandatory annual general meetings of shareholders, remedial action for minority shareholders, the election and removal of directors, voting blocs and the right of access to information.⁴⁶²

The Companies Act requires the passing of a special resolution of the shareholders in order to implement certain transactions.⁴⁶³ In these circumstances, a board resolution will not suffice. The

⁴⁵⁷ King IV op cit note 19 at 54.

⁴⁵⁸ Ibid at 9; Cassim op cit note 63 at 457.

⁴⁵⁹ Wiese op cit note 63 at 88; Cassim op cit not 63 at 497.

⁴⁶⁰ Ibid.

⁴⁶¹ Cassim op cit note 63 at ch 16; Companies Act op cit note 11 at section 163, 165, 164, 161, 20 & 218.

⁴⁶² Ibid.

⁴⁶³ Companies Act op cit note 11 at section 65 (11).

company's MOI may prescribe additional transactions which require the passing of a special resolution, as an added measure of control for shareholders.⁴⁶⁴

The Companies Act facilitates the cost effective and efficient passing of shareholder resolutions. A lower percentage of shareholders is required in order to call for a meeting, with institutional shareholders holding majority shares in most publicly listed companies.⁴⁶⁵ Shareholder meetings can be held entirely by electronic communication which reduces the attendance costs.⁴⁶⁶ The electronic submission of proxies also reduces attendance costs, thereby promoting shareholder activism.⁴⁶⁷ Quorum requirements for shareholder meetings may be altered in the company's MOI, however, higher requirements may force more shareholders to be present at meetings which may improve shareholder activism.⁴⁶⁸

The statutory requirement for the holding of an annual general meeting of the shareholders is also an internal accountability check for shareholders.⁴⁶⁹ Shareholders are able to request items to be considered at the meetings without advance notice which advocates a forum for the discussion of business affairs.⁴⁷⁰ An opportunity is also provided for the questioning of directors on the contents of financial statements and reports as well as for addressing other areas of concern.⁴⁷¹

Minority shareholders are afforded statutory protection for the enforcement of their rights in the form of remedies set out in the Companies Act.⁴⁷² These include: derivate actions, relief for prejudicial conduct, appraisal rights, the use of an alternative dispute resolution mechanism, an application for protection of the rights of securities holders and filing a complaint with the CIPC.⁴⁷³

The election and removal of directors through a shareholder's ordinary resolution, unless otherwise stated in the company's MOI, is also an internal accountability check for shareholders.⁴⁷⁴ Shareholders can elect directors who they deem sufficiently qualified to protect their investment

⁴⁶⁴ Ibid at section 65 (12)

⁴⁶⁵ Ibid at section at 1, 61 (4); Cassim op cit note 63 at 369.

⁴⁶⁶ Ibid at section 63 (2).

⁴⁶⁷ Ibid at section 58 read with section 6 (11).

⁴⁶⁸ Ibid at section 64 (1) (2) & (3).

⁴⁶⁹ Ibid at section 61 (7); Cassim op cit note 63 at 369.

⁴⁷⁰ Ibid at 370; Wiese op cit note 63 at 89;

⁴⁷¹ Ibid.

⁴⁷² Ibid at 755.

⁴⁷³ Ibid, Companies Act op cit note 11 at section 165, 163, 164, 156, 161 and 168 (1).

⁴⁷⁴ Ibid at section 68 (2).

and to manage the affairs of the business.⁴⁷⁵ If the company performs poorly, a shareholder can remove a director, subject to certain statutory requirements.⁴⁷⁶ Shareholders can exercise a degree of control over the performance of directors as well as the management of business affairs by virtue of their ability to elect and remove directors to and from the board. However, the Companies Act does prescribe specific ineligibility and disqualification requirements which restricts certain persons from serving as a director on the board of a company.⁴⁷⁷

Shareholders may also supervise the decisions of the board by exercising their voting rights. Shareholders do not owe fiduciary duties to act in the best interests of the company when exercising their voting rights, and may vote as selfishly as they wish in order to protect their own interests.⁴⁷⁸ Major shareholders of companies may vote together, in the creation of voting blocs, in order to adopt their own selfishly motivated resolutions.⁴⁷⁹ However, the board of a company or its minority shareholders can always seek the intervention of the court, under section 163 of the Companies Act, in preventing shareholder voting blocs which may act to the serious detriment of the company.⁴⁸⁰

The rights granted to shareholders to inspect the records and to access the information of the company may assist in promoting shareholder supervision.⁴⁸¹ Every person who has a beneficial interest in the securities issued by a profit company has the right to inspect and copy certain information which is contained in the records of a company.⁴⁸² This inspection of information may illuminate any inconsistencies in terms of the company's performance and decisions taken by the directors, thereby prompting pertinent enquiries by shareholders. The enforcement of this right lies in the fact that the company will commit an offence in the event that it fails to accommodate any reasonable request, in respect of the access to information.⁴⁸³

⁴⁷⁵ Ibid at section 68 (1).

⁴⁷⁶ Ibid at section 64 (4)(a)(i).

⁴⁷⁷ Ibid at section 69.

⁴⁷⁸ Wiese op cit note 63 at 89.

⁴⁷⁹ Ibid.

⁴⁸⁰ Ibid; Companies Act op cit note 11 at section 163.

⁴⁸¹ Wiese op cit note 63 at 89.

⁴⁸² Companies Act op cit note 11 at section 26 (1).

⁴⁸³ Ibid at section 26 (9).

3.7.2 Shareholder Apathy and Activism

Even with the implementation of the statutory measures to bolster activism, shareholder apathy still presents a significant hurdle to the effective oversight of the board.⁴⁸⁴ Active and informed shareholders may assist, although possibly in limited ways, in holding the board to account for their decisions.⁴⁸⁵ The costs of activism for shareholders and a lack of knowledge, in terms of their respective rights, often results in shareholders selling their shares as opposed to their becoming vocal when the company underperforms.⁴⁸⁶ Some companies even deter shareholder activism as it is thought to disrupt efficient operational workings and subvert long-term managerial goals to the detriment of other stakeholders.⁴⁸⁷

However, impact of globalization on the corporate platform has resulted in an unexpected opposition to shareholder apathy in the form of an increase in institutional investors as the majority shareholders of publicly listed companies.⁴⁸⁸ The presence of institutional investors may result in majority voting blocs over which the company or minority shareholders have no control.⁴⁸⁹ As a result, institutional investors have a greater influence over the way in which companies are governed. Institutional codes and guidelines establish principles which provide recommendations to institutional investors to act as responsible shareholders.⁴⁹⁰ Institutional investors are required to account to their clients for their investment decisions and are, therefore, more likely to be active shareholders and hold directors to account for company performance.⁴⁹¹

In South Africa, the Code for Responsible Investing in South Africa ('CRISA') was published in response to a recommendation proposed by King III.⁴⁹² CRISA sets out the best recommended practices to be initiated by institutional investors in exercising their rights as shareholders, through investment analysis and activities, which serve to promote sound governance practices in the companies in which they have invested their client's monies.⁴⁹³ In the premise, CRISA aids in

⁴⁸⁴ Cassim op cit note 63 at 498; Wiese op cit note 63 at 104.

⁴⁸⁵ Ibid.

⁴⁸⁶ Ibid.

⁴⁸⁷ Wiese op cit note 63 at 107.

⁴⁸⁸ Ibid.

⁴⁸⁹ Cassim op cit note 63 at 499; King IV op cit note 19 at 32.

⁴⁹⁰ Wiese op cit note 63 at 107.

⁴⁹¹ Cassim op cit note 63 at 499.

⁴⁹² Institute of Directors Southern Africa (IODSA) *Code for Responsible Investing in South Africa* (2011) Johannesburg: IODSA (CRISA).

⁴⁹³ Wiese op cit note 63 at 109.

holding the board to account to the institutional investors, who in turn, have to account to their clients. Although CRISA is a voluntary set of principles and recommendations, it has gained traction through exposure and implementation by reputable institutional investors such as Old Mutual Limited and Liberty Holdings Limited.⁴⁹⁴

3.7.3 The State as Shareholder

The fact of the state being the sole shareholder may compromise its ability to effectively supervise the actions of the board of the SOC.⁴⁹⁵ Due to the state being the sole shareholder, the abovementioned forms of shareholder supervision in holding the board accountable become largely ineffectual for SOCs. As the sole shareholder of the SOC, the effect which numerous shareholders have over the supervision of the board of an SOC is diluted.⁴⁹⁶ The passing of a special resolution for certain transactions, holding an annual general meeting and the special remedies for the protection of minority shareholders will not be effective as supervisory measures in holding the board of an SOC to account where the state is the sole shareholder.

The essential feature of the aforesaid supervisory measures lies in the fact that numerous shareholders of the company are able to form voting blocs, pass resolutions and question directors at annual general meetings. However, with the state as sole shareholder the effect of active interaction debate and discussion amongst various shareholders and their engagement with the board of directors is negated. The state, in its sole direction exercises its own judgement and there are, arguably, no other counteracting views or healthy debates or differing perspectives in shareholder decision taking.⁴⁹⁷ Remedies for minority shareholders, such as derivative actions, prejudicial conduct and appraisal rights, are also not an option with the state as the sole shareholder.

In an attempt to conceivably counteract these issues, the PFMA stipulates certain statutory requirements which the state, through its representative (such as the Minister as the *'executive*

⁴⁹⁴ Old Mutual Limited 'CRISA Disclosure' (2016) available at <http://ww2.oldmutual.co.za/docs/default-source/old-mutual-south-africa/omig/omig-about-us/responsible-investments/crisa-disclosure-february-2016.pdf> accessed on 22 August 2020; Liberty Holdings 'Responsible Investment' available at <http://www.libertyholdings.co.za/sustainability/provide-responsible-financial-services/Pages/responsible-investment.aspx> accessed on 22 August 2020.

⁴⁹⁵ Thabane op cit note 9 at 28.

⁴⁹⁶ Ibid.

⁴⁹⁷ Futuregrowth op cit note 10 at 8.

authority of certain SOCs) must fulfil.⁴⁹⁸ Even though shareholders do not owe fiduciary duties and are not accountable to companies for their actions, SOCs are different in that the state is their sole shareholder and the state is held accountable for its public administration in terms of the Constitution.⁴⁹⁹

Under the PFMA, the Minister has two primary responsibilities. First, to ensure that the board of an SOC complies with the provisions of the PFMA and the financial policies of the executive.⁵⁰⁰ Secondly, to table in the National Assembly the annual financial statements and auditors report of an SOC within one month after receiving the report and the findings of any outcome or sanctions imposed in any case of financial misconduct against the board of an SOC.⁵⁰¹

In the event that the Minister fails to table the financial statements and auditors report in the National Assembly, within six months after the SOC's financial year-end, the Minister must provide a written explanation as to the reasons for the failure and the Auditor-General may issue a special report on the delay.⁵⁰² There is a draft bill in progress to amend section 65 (2) (a) of the PFMA to include a requirement that the Minister has 60 days after providing the written reasons for the failure to table the annual financial statements and auditors report in the National Assembly.⁵⁰³

The issue with these statutory requirements on the executive authority of an SOC is that they lack an element of enforceability. The broad nature of the duty on the Minister to ensure that the SOC complies with the provisions of the PFMA means that it does not specify how the Minister is to fulfil the duty. The other requirement that any outcome or sanction of a case for financial misconduct must be tabled in the National Assembly by the Minister also does not assist in the execution of his or her responsibilities to ensure compliance with the PFMA.

All that the PFMA requires is for the Minister to ensure compliance with its provisions, which seemingly implies that the Minister is authorised to ensure that the board complies with the PFMA by holding itself liable, jointly and severally, if it commits an act of financial misconduct.⁵⁰⁴

⁴⁹⁸ PFMA op cit note 11 at ch 7.

⁴⁹⁹ Constitution op cit note 11 at section 195 (1)(e).

⁵⁰⁰ PFMA op cit note 11 at section 63 (2).

⁵⁰¹ Ibid at section 65 (1)(a) & (b).

⁵⁰² Ibid at section 65 (2).

⁵⁰³ Public Finance Management Amendment Bill in GN 660 GG 43418 of 12 June 2020

⁵⁰⁴ PFMA op cit note 11 at section 83 (2) & 86 (2).

However, where the board fails to hold itself liable there is no provision which allows the Minister to hold the board liable for an act of financial misconduct.⁵⁰⁵ Unlike the shareholder remedies provided in the Companies Act, there is no mechanism for the state, as the sole shareholder of an SOC, to hold its board liable in the event of a breach of its statutory duties in a case for financial misconduct.⁵⁰⁶

Therefore, the ability of the Minister to enforce compliance by the board of an SOC with its statutory duties is hindered by the toothless provisions under the PFMA. It is paramount for the accountability of an SOC that the executive be able to enforce the accountability of the directors of an SOC.⁵⁰⁷

The internal accountability check which is meant to be provided by the supervisory role of the shareholder for an SOC is further compounded if the state is complacent and corrupt.⁵⁰⁸ Corruption festers in an environment where accountability, transparency and disclosure are lacking.⁵⁰⁹ Corruption begets political interference in board decisions and the appointment and removal of directors to and from the board of an SOC, with the sole aim of furthering corrupt practices for the personal gain of the minority who are in control.⁵¹⁰ Left unchecked, without probing questions and disclosure, the state's control over the board of an SOC, with nefarious goals which are not in the best interests of the SOC, will erode the constitutional principles of accountability, responsiveness and openness.⁵¹¹ Such principles are meant to be enshrined by government through its institutions which are meant to utilise state resources in an effective manner.⁵¹²

In addition, the state, as sole shareholder, is arguably not incentivized to look after its investment in comparison to the shareholders of a private company.⁵¹³ Shareholders of a private company are driven to ensure good performance and board accountability to promote the maximum growth in their investments.⁵¹⁴ For the state, the protection and growth of its investment, as an incentive to properly supervise and monitor an SOC and board performance may not be a paramount

⁵⁰⁵ Ibid.

⁵⁰⁶ Companies Act op cit note 11 at section 165, 163, 164, 156, 161 and 168 (1).

⁵⁰⁷ *OUTA v Myeni* case supra note 346 para 267

⁵⁰⁸ Thabane op cit note 9 at 28; Kanyane op cit note 10 at 38.

⁵⁰⁹ Futuregrowth op cit note 10 at 19.

⁵¹⁰ Ibid.

⁵¹¹ *Glenister v President of the Republic of South Africa and Others* 2011 (3) SA 347 (CC) para 176 and 177.

⁵¹² Ibid.

⁵¹³ Ibid.

⁵¹⁴ Kanyane op cit note 10 at 38.

consideration.⁵¹⁵ However, the creeping appeal of corruption and personal gain, to the detriment of the SOC, may act as a strong incentive for the state in taking decisions as the sole shareholder.⁵¹⁶

3.8 The Company Secretary and Internal Audit Function

Every SOC is subject to compliance with the enhanced accountability and transparency requirements encompassed under chapter three of the Companies Act.⁵¹⁷ Although an SOC may be exempted from the provisions contained in chapter three by the Minister.⁵¹⁸ The enhanced requirements pertain to the mandatory appointment of a company secretary, an auditor and an audit committee.⁵¹⁹ The requirements under chapter three are indicative of the higher governance standards incorporated under the Companies Act, with specific emphasis on the principles of accountability and transparency.⁵²⁰ The focus on accountability and transparency in the Companies Act aligns with the fundamental global shift towards good governance and the utmost accountability of the board of directors.⁵²¹

3.8.1 The Company Secretary

In compliance with the Companies Act, an SOC must appoint a company secretary either initially through its incorporators or, subsequently, by the board or shareholders through an ordinary resolution.⁵²² The SOC must maintain a record of the identity of all appointed company secretaries, unless specifically exempted by the Minister.⁵²³ A company secretary is required to be knowledgeable or experienced in the relevant laws and must be a permanent resident of South Africa for duration of the appointment.⁵²⁴ A company secretary may be a juristic person, subject to certain statutory requirements.⁵²⁵ A person who has been disqualified from serving as a director, in terms of the Companies Act, may not be appointed as a company secretary.⁵²⁶ If the SOC fails

⁵¹⁵ Kanyane op cit note 10 at 38.

⁵¹⁶ Thabane op cit note 9 at 25; McGregor op cit note 5 at 9.

⁵¹⁷ Companies Act op cit note 11 at section 84(1)(b).

⁵¹⁸ Ibid section 84 (1)(b)(i).

⁵¹⁹ Ibid at section 84 (4).

⁵²⁰ Ibid at section 7 (b)(iii), Wiese op cit note 63 at 34.

⁵²¹ Ibid; Cassim op cit note 63 at 14; Olson op cit note 399 at 221

⁵²² Ibid at section 86(1) and (3).

⁵²³ Ibid at section 85 (1).

⁵²⁴ Ibid at section 86 (1) and (2).

⁵²⁵ Ibid at section 87.

⁵²⁶ Ibid at section 84 (5).

to appoint a company secretary, the CIPC may, by notice to the SOC, require the convening of a shareholders meeting to make the appointment.⁵²⁷

The company secretary is accountable to the board of the SOC and his or her duties relate predominantly to ensuring fulfilment by the board of its governance and compliance mandate.⁵²⁸ From an accountability perspective, the company secretary fulfils an important internal check for the SOC.⁵²⁹ The duties of the company secretary include providing directors with guidance on corporate governance structures, their duties, powers and responsibilities and making them aware of any relevant laws which may affect the SOC.⁵³⁰ The company secretary is required to report to the board any failure by the board or the SOC of any provision in the Companies Act, its own founding legislation or MOI.⁵³¹

The SOC must accurately record all board, shareholder and committee meetings and the company secretary is required to ensure that all records are made in accordance with the Companies Act.⁵³² The company secretary must certify, in the annual financial statements of the SOC, that all notices and returns have been properly filed and are true, correct and up to date.⁵³³ The company secretary is to ensure that a copy of the SOC's annual financial statements is sent to every person who is entitled to receive them, in terms of the Companies Act.⁵³⁴ The company secretary is also required to ensure that the SOC complies with all of the requirements under chapter three of the Companies Act.⁵³⁵

The company secretary may resign, on one month's notice or be removed by the board of the SOC.⁵³⁶ In the event that the board removes the company secretary, it may, by notice to the SOC, require inclusion in the annual financial statements of the circumstances which, in its opinion, resulted in such removal.⁵³⁷ The inclusion of these provisions is an attempt to increase transparency in the event that the board decides to remove a secretary who is considered to be

⁵²⁷ Ibid at section 84 (6).

⁵²⁸ Ibid at section 88(1) and (2); Wiese op cit note 63 at 34.

⁵²⁹ Cassim op cit note 63 at 418.

⁵³⁰ Companies Act op cit note 11 at section 88(2)(a) & (b); Cassim op cit note 63 at 419; King IV op cit note 19 at 59.

⁵³¹ Ibid at section 88 (2)(c).

⁵³² Ibid at section 88(2)(d).

⁵³³ Ibid at section 88 (2)(e).

⁵³⁴ Ibid at section 88(2)(f).

⁵³⁵ Ibid at section 88(2)(g) & section 33 (3).

⁵³⁶ Ibid at section 89 (1) & (2).

⁵³⁷ Ibid at section 89 (2) & (3).

meddlesome.⁵³⁸ It should, for instance, be made transparent that the removal may be due to nefarious reasons by the board if the company secretary has, on numerous occasions, pointed out contraventions by the directors or the board of various statutory requirements.⁵³⁹

The PFMA does not make mention of the appointment of a company secretary for an SOC.⁵⁴⁰ The Companies Act stipulates the statutory requirements for SOCs, pertaining to the appointment, removal and duties of the company secretary.⁵⁴¹ However, the Companies Act is silent as to the independence of the company secretary in relation to the SOC.⁵⁴² King IV recommends that the company secretary maintain an arms-length relationship with the company to ensure independent, objective and unfettered decision making by the board.⁵⁴³

The independence of the company secretary is to ensure the effective fulfilment of his or her duties, without interference or influence from the board.⁵⁴⁴ The company secretary may, and is encouraged, to attend shareholder and board meetings but, to maintain independence, should not be a member of the board of the SOC or related to any member.⁵⁴⁵ The position of the company secretary should be reviewed annually by the board, in relation to his or her independence, knowledge and experience.⁵⁴⁶ The rotation of the company secretary is also recommended in order to ensure independence.⁵⁴⁷

The recommended practices contained in the King IV are only voluntary, however, in order to ensure the utmost accountability of SOCs, it would be advisable for all SOCs to appoint an independent company secretary.⁵⁴⁸ A company secretary who is not independent may hinder his or her ability to ensure the accountability and transparency of the SOC. Political interference, conflicts of interest and undue board influence may negatively impact the ability of the company secretary in fulfilling duties which are the best interests of the SOC. Given the importance of the role played by the company secretary in promoting the accountability and transparency of an SOC,

⁵³⁸ Wiese op cit note 63 at 35.

⁵³⁹ Ibid; Companies Act op cit note 11; PFMA op cit note 11.

⁵⁴⁰ PFMA op cit note 11; Treasury Regulations op cit note 291.

⁵⁴¹ Companies Act op cit note 11 at section 86 – 89.

⁵⁴² Ibid; Companies Act Regulations op cit note 463.

⁵⁴³ King IV op cit note 19 at principle 10.94 at 60 & 116.

⁵⁴⁴ Ibid.

⁵⁴⁵ Ibid at principle 10.96.

⁵⁴⁶ Ibid at principle 10.98.

⁵⁴⁷ Wolpert, Joel 'The role of the company secretary: corporate governance' (2010) 4 *Enterprise Risk* 4 available at: <http://www.chartsec.co.za/documents/latestNews/EnterpriseRiskArticleMay2010.pdf>, accessed on 13 August 2020.

⁵⁴⁸ Ibid.

the board should ensure that the position is filled only by persons with the sufficient capacity, independence, qualifications and experience to effectively perform the requisite duties.⁵⁴⁹

3.8.2 Internal Audit Function

The auditing processes for an SOC depict an intricate system of internal and external checks and balances. The PFMA is the predominant statute governing the internal audit function for SOCs and the National Treasury may make regulations pertaining to the financial management, internal control and internal audit components to which SOCs must adhere.⁵⁵⁰ All SOCs must have an internal audit function, the effectiveness of which is monitored by the mandatory audit committee.⁵⁵¹ The internal audit function and the audit committee are the two most predominant pillars of the internal, financial accountability mechanisms for SOCs. The two pillars work interactively and simultaneously with an aim to ensure the effective financial management and internal control of the SOC.⁵⁵²

The internal audit function may be outsourced to an external institution with specialist audit expertise, however, the external auditors of the SOC may not provide the internal audit function.⁵⁵³ An internal auditor must be a member of the Institute of Internal Auditors South Africa ('IIASA') and must comply with the rules and regulations set by the IIASA at all times.⁵⁵⁴ An internal audit charter must be established, in consultation with the board of the SOC, which sets out the purpose, authority and responsibility of the internal audit function.⁵⁵⁵ The internal audit must be conducted in accordance with the provisions of the IIASA.⁵⁵⁶

The IIASA defines an '*internal audit*' as the following:

Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.

⁵⁴⁹ Blackman op cit note 440 at ch 9A at 3.

⁵⁵⁰ PFMA op cit note 11 at section 76 (4).

⁵⁵¹ Treasury Regulations op cit note 291 reg 27.2.2. & 27.1.10.

⁵⁵² Makwethu (AGSA) op cit note 18 at 5.

⁵⁵³ Treasury Regulations op cit note 291 reg at 27.2.4.

⁵⁵⁴ Institute of Internal Auditors South Africa (IIASA) 'About Internal Audit' available at http://www.iiasa.org.za/page/About_IA, accessed on 23 August 2020.

⁵⁵⁵ Treasury Regulations op cit note 291 reg 27.2.5.

⁵⁵⁶ Ibid.

*Although accounting is an important skill for an internal auditor, the focus for internal auditors is the evaluation of operational risk management, internal control and the governance processes of the organisation.*⁵⁵⁷

The role of the internal audit function differs from that of the external audit, both of which are mandatory for an SOC.⁵⁵⁸ The internal audit function, whilst having a focus on financial management, is not a financial discipline, like the external audit.⁵⁵⁹ The role of the internal audit encompasses evaluating key risk areas and the effectiveness of operations, safeguarding assets, monitoring and examining financial controls and relaying such controls to all managers and employees as well as analysing and confirming information and reviewing compliance.⁵⁶⁰

The internal audit function is a continual analysis of the financial controls and operations within the SOC, whereas, an external audit occurs only once a year.⁵⁶¹ The internal audit function must also prepare, in consultation with the audit committee, a rolling three-year strategic internal audit plan for the SOC.⁵⁶² King IV recommends that the integrity of the internal audit function be maintained by the board of the SOC which ensures a review by the external auditors once every five years.⁵⁶³

The internal auditor must have unlimited access to any information required in order to effectively perform his or her duties and must report to the board of the SOC.⁵⁶⁴ The internal audit function must assist the board of the SOC by providing recommendations and improvements through which accountability is ensured.⁵⁶⁵ King IV recommends the appointment of a Chief Audit Executive to facilitate the internal audit function and report to the board of the SOC.⁵⁶⁶

Under the PFMA, the board of the SOC also has specific functions and duties to ensure that effective risk management and internal controls are in place to prevent irregular expenditure and to ensure the continued financial health and operations of the SOC.⁵⁶⁷ The board is required to

⁵⁵⁷ IIASA 'Definition of Internal Audit' available at http://www.iiasa.org.za/page/Technical_IADef., accessed on 23 August 2020.

⁵⁵⁸ Ibid.

⁵⁵⁹ IIASA op cit note 574.

⁵⁶⁰ Ibid; Treasury op cit note 306 at reg 27.2.10.

⁵⁶¹ Wiese op cit note 63 at 158.

⁵⁶² Treasury op cit note 306 at reg 27.2.7.

⁵⁶³ King IV op cit note 19 at 70.

⁵⁶⁴ Treasury op cit note 306 at reg 27.2.8.

⁵⁶⁵ Ibid at reg 27.2.11.

⁵⁶⁶ King IV op cit note 19 at 69.

⁵⁶⁷ PFMA op cit note 11 at section 51.

fulfil its statutory duties failing which the directors may be guilty of financial misconduct and criminal or civil liability may be levied against them, individually and severally.⁵⁶⁸

The board of an SOC must also comply with requirements under the PFMA pertaining to the financial management and strategy of the SOC.⁵⁶⁹ Without compliance with these prescribed functions by the board, the internal audit function of the SOC may be severely compromised. The Accounting Standards Board prescribes updated accounting standards, known as the Standards of Generally Recognized Accounting Practices, which are to be applied in the preparation of the annual financial statements of SOCs.⁵⁷⁰ The board is required to adopt these standards when preparing the financial statements of SOCs in order to ensure transparency and uniformity of the measures for the control of expenditure for all organs of state.⁵⁷¹

The board of the SOC is required to prepare and submit annual budgets and a three-year corporate plan to the Minister and the National Treasury.⁵⁷² The board of the SOC is also required to conclude an annual shareholder compact with the Minister which sets out the agreed key performance indicators to be attained by the SOC.⁵⁷³ The shareholder compact is the document of communication between the Minister and the board of the SOC and must be prepared with reference to the previous year's indicators and their fulfilment, together with future expectations and indicators which the board of the SOC can reasonably be expected to achieve.⁵⁷⁴

The board of an SOC is required to provide any information requested by the Auditor-General or the National Treasury or by prescribed by legislation.⁵⁷⁵ There are certain transactions for which the board of an SOC must obtain approval from the Minister, and inform the National Treasury, in writing, prior to their conclusion.⁵⁷⁶ There is a default acceptance provision, wherein the SOC can assume approval has been given for conclusion of the transaction from the Minister if the board of the SOC receives no response from the Minister within 30 days (or a further agreed period)

⁵⁶⁸ Ibid at section 83, 86 (2).

⁵⁶⁹ Ibid at sections 52 to 55.

⁵⁷⁰ Ibid at ch 11 & section 55 (1)(a) & (b); Accounting Standards Board 'Standard of Generally Recognised Accounting Practices Presentation of Financial Statements' (2010) Version May 2019 available at <http://www.asb.co.za/wp-content/uploads/2019/04/GRAP-1-Presentation-of-Financial-Statements-1-April-2019-clean.pdf>, accessed on 14 August 2020.

⁵⁷¹ PFMA op cit note 11 at section 55 (1)(b); Constitution op cit note 11 at section 216.

⁵⁷² Ibid PFMA at section 52; Treasury Regulations op cit note 291 at reg 29.

⁵⁷³ Ibid at reg 29.2.

⁵⁷⁴ PWC op cit note 70 at 11.

⁵⁷⁵ PFMA op cit note 11 at section 54 (1).

⁵⁷⁶ Ibid at section 54 (2).

from the date of submission.⁵⁷⁷ The Minister may also exempt an SOC from this statutory approval requirement.⁵⁷⁸

The PFMA contains stringent provisions regarding the preparation and submission of annual financial statements and the annual report, on those financial statements, for SOCs.⁵⁷⁹ There are prescribed requirements and specific information which must be included in the annual financial statements of the SOC.⁵⁸⁰

The annual financial statements of an SOC must be submitted by the board to the external auditor and to the National Treasury within two months of the end of the financial year end of that SOC.⁵⁸¹ The board must then submit the audited annual financial statements, the auditor's report and an annual report, within five months of the end of the financial year for that SOC, to the Minister and the National Treasury.⁵⁸² The audited statements and report must also be submitted to the Auditor-General if the external audit of the SOC was not performed by the Auditor-General.⁵⁸³ These reports are usually combined in the annual integrated report of the SOC which is made public.

The internal auditors work closely with the board of the SOC, and specifically the members of the audit committee, in assisting with the achievement of their objectives.⁵⁸⁴ Maintaining the independence of the internal auditor is imperative to the effective functioning of its internal accountability role.⁵⁸⁵ However, the independence of the internal audit function is contradicted by the provisions in the PFMA relating to the duties of the board and the audit committee of the SOC.

According to section 51 of the PFMA, the board is under a statutory duty to ensure that the SOC has and maintains '*a system of internal audit **under the control and direction** of the audit committee*'.⁵⁸⁶ This subsection of the PFMA directly contradicts the regulations which prescribe complete independence of the internal audit function.⁵⁸⁷ The internal audit function cannot, simultaneously, be under the direction and control of the audit committee and maintain its

⁵⁷⁷ Ibid at section 54 (3).

⁵⁷⁸ Ibid at section 54 (4).

⁵⁷⁹ Ibid at section 55.

⁵⁸⁰ Ibid at section 54 & 55 (2).

⁵⁸¹ Ibid at section 55 (1)(c).

⁵⁸² Ibid at section 55 (1)(d).

⁵⁸³ Ibid.

⁵⁸⁴ Treasury Regulations op cit note 291 at reg 27.2.11.& 27.2.1.

⁵⁸⁵ Ibid at reg 27.2.8.

⁵⁸⁶ PFMA op cit note 11 at section 51 (1)(a)(ii).

⁵⁸⁷ Treasury Regulations op cit note 291 at reg 27.2.8.

independence. This statutory contradiction, between the PFMA and its regulations, is an oxymoron in its requirement of ‘controlled independence’ and should be amended to avoid confusion.

The importance of the internal audit function as a mechanism for ensuring the accountability of an SOC cannot be overstated. Although not binding on SOCs, the recommended practices in King IV highlight the importance of the internal audit function, in achieving the principles of accountability and transparency.⁵⁸⁸ From a theoretical perspective, all of the statutory provisions are in place to ensure an effective internal audit function for SOCs which should promote accountability and transparency.⁵⁸⁹ However, from a practical perspective, it is arguable that the internal audit function has not been effectively implemented by the boards of SOCs.⁵⁹⁰

3.9 External Accountability Mechanisms

The accountability of an SOC is best achieved through a combination of internal and external checks and balances. Notwithstanding the effectiveness of the internal accountability checks, the external accountability checks of an SOC should bring to the fore any discrepancies in the internal processes and controls. The external accountability checks for SOCs are embodied in four primary mechanisms. First, and perhaps most importantly, from a financial accountability perspective, the external audit. Secondly, through independent institutions such as the Auditor-General and the Public Protector. Thirdly, through the separation of powers doctrine, which comprise the checks and balances amongst the three arms of government: the executive, legislature and judiciary. Lastly, and as the last resort, through the public, including public activist watchdog groups such as Corruption Watch and the Organization Undoing Tax Abuse (‘OUTA’).

3.10 The External Audit and the Auditor-General

The auditors of SOCs are either the Auditor-General or an independent registered auditor, in terms of the Auditing Profession Act 26 of 2005 (‘APA’).⁵⁹¹ Every SOC is required to appoint a registered auditor at its annual general meeting of the shareholders each year.⁵⁹² An auditor is an individual or firm that has been registered as an auditor by the Independent Regulatory Board for Auditors (‘IRBA’).⁵⁹³ There are specific statutory requirements with respect to the appointment,

⁵⁸⁸ King IV op cit note 19 at 69.

⁵⁸⁹ PFMA op cit note 11 at sections 52 – 55; Treasury Regulations op cit note 291 at reg 27.

⁵⁹⁰ Makwethu (AGSA) op cit note 18 at 8.

⁵⁹¹ Ibid; Auditing Profession Act 26 of 2005 (APA).

⁵⁹² Companies Act op cit note 11 at section 90 (1).

⁵⁹³ Ibid, APA op cit note 591 at section 1.

removal and duties of the auditors of an SOC, as set out in the Companies Act.⁵⁹⁴ The role and function of the auditor is largely determined for an SOC by the Companies Act, the Auditing Profession Act and the Public Audit Act 25 of 2004 ('PAA').⁵⁹⁵ The provisions in the PFMA which related to the external auditors for SOEs were repealed by the PAA, which came into effect on 1 April 2004.⁵⁹⁶

SOCs are, therefore, subject to the PAA, together with applicable provisions from the APA and the Companies Act, if any, in respect of the external audit of their annual financial statements. The provisions of each statute must be applied concurrently. However, in the event of a conflict, the PAA prevails.⁵⁹⁷ The PAA is the supreme legislation in South Africa, in respect of and governing all aspects relating to the auditing of SOCs.⁵⁹⁸

The board of an SOC is required to submit, within two months of the end of every financial year, annual financial statements, in the required form, to its auditors and to the National Treasury, in the case of a national government business enterprise.⁵⁹⁹ The definitions of an '*authorised auditor*' and the '*Auditor-General*' are provided by the PAA, as the possible auditors of SOCs.⁶⁰⁰ In the event that the Auditor-General opts not to perform the external audit for an SOC, a registered auditor must be appointed by the SOC to perform the external annual audit.⁶⁰¹

3.10.1 Appointment and Removal

An SOC, for which the Auditor-General has elected not to perform the annual audit, must elect as its auditor a person who is registered in terms of the APA as an accountant and auditor and engaged in public practice as an auditor and accountant.⁶⁰² The registered auditor is usually a company which is appointed by the board of the SOC and such appointment is subject to the approval of the Auditor-General.⁶⁰³ The appointment of a registered auditor by the SOC is restricted to a period of one financial year.⁶⁰⁴ In the event that the Auditor-General elects to do so, he or she may perform

⁵⁹⁴ Companies Act op cit note 11 at section 90 - 3.

⁵⁹⁵ Ibid; APA op cit note 591; Public Audit Act 25 of 2004 (PAA).

⁵⁹⁶ PFMA op cit note 11 at section 58 – 62; PAA op cit note 595 at section 53 & 58 – 61.

⁵⁹⁷ PAA op cit note 595 at section 4 (4).

⁵⁹⁸ Ibid at sections 3 & 4.

⁵⁹⁹ PFMA op cit note 11 at section 55 (1)(c).

⁶⁰⁰ Ibid at section 1, 4 (3)(a), 11 & 12.

⁶⁰¹ Ibid at section 4 (3)(1) & 25 (1)(a) & (b).

⁶⁰² Ibid at section 25(1)(b); APA op cit note 591 at section 37 & 38.

⁶⁰³ PAA op cit note 595 at section 25 (2) & 3); Companies Act op cit note 11 at section 90 (1).

⁶⁰⁴ Ibid at section 25 (4).

the external audit of an SOC for its financial year-end, subject to the requirements under part one of chapter three of the PAA.⁶⁰⁵

The Auditor-General is a state institution which is appointed to strengthen constitutional democracy in South Africa.⁶⁰⁶ The Auditor-General is the supreme audit institution of the Republic, has full legal capacity, must be independent, is subject only to the Constitution and accountable to the National Assembly.⁶⁰⁷ The Auditor-General is an institution established to ensure the utmost accountability of all organs of state, in fulfilment of their constitutional accountability to the National Assembly.⁶⁰⁸ The Auditor-General must be appointed by the President, on recommendation of the National Assembly, for a fixed period of between five to ten years.⁶⁰⁹

There are specific statutory and constitutional requirements with which the registered auditor or the Auditor-General must comply in order to be appointed.⁶¹⁰ In the event of a firm being appointed as the registered auditor for the SOC, that firm must immediately after the appointment is made, take a decision as to the individual registered auditor who will be responsible and accountable for the audit of the SOC.⁶¹¹ Legislation prescribes certain categories of persons which cannot be appointed as the registered auditors for SOCs, which predominantly relate to maintaining the capacity, independence and integrity of the external auditor.⁶¹² There are also specific requirements for firms which are appointed as the registered auditors of the SOC.⁶¹³

The independence and impartiality of the registered auditor, or Auditor-General, is emphasized in order to effectively discharge his or her statutory duties.⁶¹⁴ The Code of Professional Conduct for Registered Auditors, published by the IRBA, sets out mandatory rules with which every registered auditor must comply.⁶¹⁵ Amongst others, the rules stress the importance of the independence of

⁶⁰⁵ Ibid at section 11 & ch 3 part 1.

⁶⁰⁶ Constitution op cit note 11 at section 181 (1)(e).

⁶⁰⁷ Ibid at section 181 (2).

⁶⁰⁸ Ibid at section 181 (5); PAA op cit note 595 at section 10.

⁶⁰⁹ Ibid at section 189 & 193; Ibid at section 6.

⁶¹⁰ Ibid; APA op cit note 591 at section 37 & 38.

⁶¹¹ Companies Act op cit note 11 at section 90 (3); APA at section 38 & 44 (1).

⁶¹² Ibid at section 90 (2); Ibid at section 37 (3).

⁶¹³ Ibid APA at section 38.

⁶¹⁴ Ibid at section 44 (4), (5) & (6); PAA op cit note 595 at section 3 (c).

⁶¹⁵ Ibid APA at section 42 & 10 (1)(a); Auditing Profession Act, Adoption of Revised Code of Professional Conduct for Registered Auditors in Board Notice No 25 GG 37392 of 7 March 2014.

the registered auditor in effectively discharging his duties in conducting an audit of the SOC.⁶¹⁶ Independence is predominantly preserved through the rotation of the registered auditors and the avoidance of conflicts of interest.⁶¹⁷ The Companies Act promotes the independence of the auditor by prescribing a mandatory rotation of the registered auditors every five years as well as the satisfaction of the independence of the auditor by the audit committee.⁶¹⁸

The removal processes are different for discharging the Auditor-General or the registered auditor, as the case may be, as the external auditor of the SOC. The Auditor-General may resign on three months written notice to the President.⁶¹⁹ The office of the Auditor-General is vacated if that person resigns, his or her term expires or if he or she is removed from office, in terms of section 194 of the Constitution.⁶²⁰ The grounds for removal of the Auditor-General by the President, on a finding by a committee of the National Assembly, include: misconduct, incompetence or incapacity.⁶²¹ Alternatively, the Auditor-General must be removed from his or her office by the President on the passing of a resolution, calling for the removal of the Auditor-General, by at least two thirds of the members of the National Assembly.⁶²² The Deputy Auditor-General assumes the role of the Auditor-General until the appointment of another Auditor-General.⁶²³

The registered auditor of an SOC may be discharged by the board, before expiry of its one year term, on written notice and after being given an opportunity to make representations, subject to the consent of the Auditor-General and Minister.⁶²⁴ The Auditor-General is required to report any discharge of an auditor by an SOC to the National Legislature.⁶²⁵ An auditor's registration may also be terminated in accordance with the provisions of the APA, at which point the auditor may not carry on with its audit function, as he or she no longer meets the requirements of the PAA⁶²⁶

The Companies Act allows for the registered auditor to include in the annual financial statements of the SOC, a statement as to the reasons, in auditor's opinion, for his or her removal.⁶²⁷ However,

⁶¹⁶ Ibid at section 290.

⁶¹⁷ Ibid.

⁶¹⁸ Companies Act op cit note 11 at 90 – 2.

⁶¹⁹ PAA op cit note 595 at section 8 (2).

⁶²⁰ Constitution op cit note 11 at section 194; Ibid PAA at section 8 (1).

⁶²¹ Ibid Constitution at section 194 (1)(a)(b).

⁶²² Ibid at section 194 (1)(c), (2) & (3)(b).

⁶²³ PAA op cit note 595 at section 9.

⁶²⁴ Ibid at section 26 (1) and (2).

⁶²⁵ Ibid at section 26 (3).

⁶²⁶ APA op cit note 591 at section 39; Ibid PAA at section 25 (1)(b).

⁶²⁷ Companies Act op cit note 11 at section 91 (6) & 89.

the PAA does not allow for the same and as the prevailing legislation, it is unlikely that an SOC will be required to provide reasons for removal of the auditor in its annual financial statements.⁶²⁸

3.10.2 Duties and Powers

The PAA confers extensive powers on the auditor of an SOC, whether it be the Auditor-General or an independent, registered auditor.⁶²⁹ The auditor has such wide powers in order to give effect to the purpose of the PAA in enshrining the constitutional principle of accountability by all organs of state.⁶³⁰ There are two predominant duties which the auditor is obliged to fulfil when performing the annual audit function of the SOC: to audit the annual financial statements and to compile a report on the audited financial statements.⁶³¹

If the auditor of the SOC is the Auditor-General, the processes and requirements of the audit function are prescribed under part one of chapter three of the PAA.⁶³² The Auditor-General, in consultation with the Standing Committee on the Auditor-General, must set the standards to be complied with in performing the audit of the SOC, as well as the nature and frequency of the audit of certain institutions by the Auditor-General.⁶³³ If the auditor of the SOC is a registered auditor, the audit function must be performed in terms of the processes and requirements set out in the APA, read together with part two of chapter three of the PAA.⁶³⁴

The PAA prescribes the minimum requirements on which the auditor must express an opinion or conclusion, which are to be contained in the auditor's report on the annual financial statements of the SOC ('Auditor's Opinion').⁶³⁵ In addition to the Auditor's Opinion, the Auditor-General or the auditor (if requested by the Auditor-General) must report on two issues. First, on whether the SOC has procured its resources in an economic fashion and utilized them efficiently and effectively.⁶³⁶ Secondly, the auditor must report on any matters arising out of an investigation required by the Auditor-General that should, in public interest, be brought to the attention of the national

⁶²⁸ PAA op cit note 595 at section 3 (a) & 4 (4).

⁶²⁹ Ibid at section 15 and section 27 (2).

⁶³⁰ Ibid preamble.

⁶³¹ Ibid at ch 3 Part 1 and Part 2 & preamble & section 1.

⁶³² Ibid at ch 3 Part 1.

⁶³³ Ibid at section 13.

⁶³⁴ Ibid at ch 3 part 2 & section 27 (1); APA op cit note 591.

⁶³⁵ PAA op cit note 595 at section 20 (2) & 28 (1).

⁶³⁶ Ibid at section 20 (3) & 28 (2)(a).

legislature.⁶³⁷ The auditor is required to report to the legislature any matter, ascertained within the audit investigation and which, in the opinion of the auditor, is in public interest.⁶³⁸ A copy of the report on any of the two aforementioned issues, by the auditor of an SOC, must be sent to the Minister for submission to the national legislature.⁶³⁹

The Auditor's Opinion, contained in the auditor's report, must be submitted by the auditors to the Auditor-General, the SOC, the Minister and the National Treasury.⁶⁴⁰ The board of the SOC is required to ensure that the Auditor's Opinion, in the auditor's report, is submitted to the relevant institutions within five months of every financial year end of the SOC.⁶⁴¹

If the Auditor-General performed the external audit, he or she must submit the report to the SOC in respect of whom the audit was performed and to the national legislature for tabling in Parliament.⁶⁴² In the event that the report is not tabled within one month after Parliament's first sitting after the report was submitted, the Auditor-General must promptly publish the report.⁶⁴³ The Auditor-General also has the power to submit any report which may be in the public interest to any legislature or organ of state.⁶⁴⁴

In addition to the constitutional audit function, the Auditor-General may, without compromising its independence, provide other functions. Amongst these other functions is the discretion to carry out an investigation or conduct a special audit of any SOC if it is in the public interest to do so or upon the receipt of a complaint or request.⁶⁴⁵ The registered auditor must, at the request of the Auditor-General, also carry out such an investigation or conduct a special audit of an SOC.⁶⁴⁶

The scope and enforceability of the powers of the Auditor-General, in the performance of audit functions, investigations and special audits, was extended by the enactment of the Public Audit Amendment Act 5 of 2018, which came into effect on 1 April 2019 ('PAAA').⁶⁴⁷ The PAAA specifically widened the powers of the Auditor-General to include three primary powers. First, the

⁶³⁷ Ibid at section 28 (2)(b).

⁶³⁸ Ibid at section 28 (5).

⁶³⁹ Ibid at section 28 (4)(a).

⁶⁴⁰ Ibid at section 28 (3).

⁶⁴¹ PFMA op cit note 11 at section 55 (1)(d).

⁶⁴² PAA op cit note 595 at section 21.

⁶⁴³ Ibid at section 21 (3).

⁶⁴⁴ Ibid at section 21 (4).

⁶⁴⁵ Ibid at section 5 (1)(d).

⁶⁴⁶ Ibid at section 29.

⁶⁴⁷ Public Audit Amendment Act 5 of 2018 (PAAA).

conducting of performance audits to refer material irregularities arising from an audit to the relevant institutions for investigation in order for appropriate remedial action to be taken.⁶⁴⁸ Secondly, to issue a certificate for the collection of debt by the Minister.⁶⁴⁹ Thirdly, to make requirements pertaining to audit fees and the remuneration of the Auditor-General.⁶⁵⁰ The Auditor-General published specific regulations which allow for the facilitation of these additional duties and powers, as set out in the PAAA.⁶⁵¹

The implementation of the PAAA and its regulations, appears to be an effort to identify and prevent financial mismanagement and the occurrence of material irregularities of SOCs which may result in significant financial loss.⁶⁵² The Auditor-General will identify these issues by conducting a special audit and investigation of the SOC.⁶⁵³ Recommendations to remedy such irregularities and prevent future occurrences will then be prescribed to the board of the SOC by the Auditor-General.⁶⁵⁴ In the event of the board of the SOC failing to implement the recommendations provided by the Auditor-General, the Auditor-General will prescribe remedial action which must be taken by the board of the SOC.⁶⁵⁵

A failure to implement the remedial action prescribed by the Auditor-General by the board of the SOC will result in the issuing of a certificate of debt by the Auditor-General.⁶⁵⁶ The certificate of debt stipulates an amount to be collected from the board of the SOC, jointly and severally, due to the failure to implement the remedial action.⁶⁵⁷ Those persons who were directors of the SOC when the failure to implement the remedial action occurred will be liable to pay the amount specified in the certificate of debt to the state.⁶⁵⁸

The PAA also emphasizes the role which auditing of the annual financial statements of SOCs plays as a mechanism to prevent irregular, wasteful and fruitless expenditure by the SOC.⁶⁵⁹ Such

⁶⁴⁸ Act preamble; PAA op cit note 595 at section 5 (1A) & (1B); 5A & 5B.

⁶⁴⁹ Act preamble; Ibid at section 5 (1B)(b).

⁶⁵⁰ Act preamble; Ibid at section 7.

⁶⁵¹ Ibid at section 52 (1A); Public Audit Act, Investigations and Special Audit Regulations in GN 525 GG 42368 of 1 April 2019; Public Audit Act, Material Irregularity Regulations in GN 526 GG 42368 of 1 April 2009; Public Audit Act, Regulations on Audits by Auditors in Private Practice in GN 527 GG 42368 of 1 April 2009.

⁶⁵² Makwethu (AGSA) op cit note 18 at 10.

⁶⁵³ Investigations and special audit regulations op cit note 669.

⁶⁵⁴ Material Irregularity Regulations op cit note 669 at part 2

⁶⁵⁵ Ibid at part 4; PAA op cit note 595 at section 5A.

⁶⁵⁶ Ibid at part 5; Ibid at section 5B.

⁶⁵⁷ Ibid at part 5; Ibid at section 5B (2).

⁶⁵⁸ Ibid.

⁶⁵⁹ Makwethu (AGSA) op cit note 18 at 9.

expenditure will be detrimental to the SOC's financial and operational performance.⁶⁶⁰ Although the Act allows for the provision of secrecy in certain instances, any such secrecy provision may not be abused in order to prevent detection or disclosure of an audit finding by the Auditor-General or disclosure of any unauthorized, irregular or fruitless and wasteful expenditure.⁶⁶¹

The PFMA defines irregular expenditure as '*expenditure, other than unauthorized expenditure incurred in contravention of, or that is not in accordance with a requirement of any applicable legislation*'.⁶⁶² Unauthorised expenditure is defined as the overspending of a vote or main division within a vote, or expenditure not in accordance with the purpose of the vote or main division within a vote, as the case may be.⁶⁶³ A vote is defined as one of the main segments into which an appropriation Act is divided and which specifies the total amount which is usually appropriated per department in an appropriation Act and is separately approved by Parliament before it approves the relevant draft appropriation Act.⁶⁶⁴ Fruitless and wasteful expenditure is defined, under the PFMA, as '*expenditure which was made in vain and would have been avoided if reasonable care had been exercised*'.⁶⁶⁵

In an attempt to bolster the importance of the PAA and its purpose, any person who hinders or interferes with the ability of the Auditor-General in the performance of his or her functions will be guilty of an offence and, on conviction, subject to a fine and/or imprisonment for a maximum of one year.⁶⁶⁶ Similarly, the IRBA has the power to investigate and review the practice of any registered auditor and, in the event of a finding of improper conduct, disciplinary measures may be implemented against the auditor.⁶⁶⁷ A registered auditor may be guilty of an offence if found guilty on a charge of improper conduct, if he fails to report an irregularity or if he recklessly or knowingly expresses an opinion or makes a report which is materially false and may be subject to a fine or a maximum of five years imprisonment.⁶⁶⁸ Any person who hinders the performance of

⁶⁶⁰ Ibid.

⁶⁶¹ PAA op cit note 595 at section 18 (2).

⁶⁶² PFMA op cit note 11 at section 1.

⁶⁶³ Ibid.

⁶⁶⁴ Ibid.

⁶⁶⁵ Ibid.

⁶⁶⁶ PAA op cit note 595 at section 51.

⁶⁶⁷ APA op cit note 591 at ch 5.

⁶⁶⁸ Ibid at ch 6.

the auditor may be guilty of an offence and subject to a fine or imprisonment of a maximum of one year.⁶⁶⁹

The PAA also provides for the administrative requirements of the Auditor-General, which include an external, independent audit, an audit committee and disciplinary measures for non-compliance with legislative requirements.⁶⁷⁰ The Auditor-General remains, at all times, accountable to the National Assembly for the performance of his or her duties and functions.⁶⁷¹ The National Assembly established the Standing Committee on the Auditor-General in 2004 as the oversight mechanism of the Auditor-General to ensure fulfilment of his or her duties and compliance with the Constitution and relevant legislation, to advise the National Assembly and to ensure the independence and impartiality of the Auditor-General.⁶⁷²

The imposition of certain liability provisions against the board of an SOC and its directors, as well as the registered auditors, under the PAA and the APA are meant to act as retribution-based mechanisms to ensure an effective and efficient annual audit of an SOC.⁶⁷³ The enactment of the PAAA provides for the implementation of additional, harsh remedies against the recalcitrant board of an SOC in the event that they fail to implement recommendations made by the Auditor-General.⁶⁷⁴ Stringent audit requirements provided by the PAA and APA ensure the uniformity and certainty of the standards against which all SOCs are to be audited.⁶⁷⁵ There are numerous statutory requirements with which the auditors of SOCs must comply and which should, if actually enforced, project an accurate display of the financial and operational performance of an SOC for every financial year.

3.11 The Public Protector

The office of the Public Protector was established as a state institution with the purpose of strengthening constitutional democracy in South Africa.⁶⁷⁶ The Public Protector was essentially established in order to provide a guard for the guardians themselves, a watchdog over the watchers

⁶⁶⁹ PAA op cit note 595 at section 54 (2).

⁶⁷⁰ Ibid at part 4.

⁶⁷¹ Ibid at section 10.

⁶⁷² Ibid at section 2 (c) & 10 (3); Constitution op cit note 11 at section 55 (2)(b)(ii).

⁶⁷³ Ibid at section 5B; APA op cit note 591 at ch 4, 5 & 6.

⁶⁷⁴ Ibid at section 5B & 20 (1).

⁶⁷⁵ Ibid at ch 3.

⁶⁷⁶ Constitution op cit note 11 at section 181 (1)(a).

and an indispensable tool for ensuring the accountability of all organs of state.⁶⁷⁷ The Public Protector is required to be independent and to exercise its powers and perform its functions impartially, without fear, favour or prejudice, subject only to the Constitution.⁶⁷⁸ Other organs of state are to protect and assist the Public Protector to ensure his or her independence, effectiveness, impartiality and dignity, and no organ of state is to interfere in the functioning of the Public Protector.⁶⁷⁹ As the name aptly suggests, the office of the Public Protector was ultimately established in order to serve and protect the interests of the public against those in power with unscrupulous intentions and nefarious motives.⁶⁸⁰

3.11.1 Appointment, Removal and Powers

The Public Protector is appointed by the President, on recommendation of the National Assembly, for a non-renewable tenure of seven years.⁶⁸¹ The Constitution and the Public Protector Act 23 of 1994 ('PPA') stipulate statutory qualification criteria that a nominated person must meet in order to be appointed as the Public Protector.⁶⁸² The Public Protector can only be removed, prior to expiry of his or her tenure, on a finding of misconduct, incompetence or incapacity, with a two-third majority resolution by the National Assembly calling for such removal.⁶⁸³ Upon adoption of the National Assembly resolution, the President must remove such person from the office of the Public Protector.⁶⁸⁴ In certain instances the Public Protector may be allowed to vacate his or her office, on three months written notice to the National Assembly.⁶⁸⁵

The constitutional function of the Public Protector requires the discharging of three primary powers. First, the power to investigate the conduct of state affairs or public administration, in any sphere of government, which includes SOCs, that is alleged or suspected to be improper or result in impropriety or prejudice.⁶⁸⁶ Secondly, to report on such conduct.⁶⁸⁷ Thirdly, to take appropriate

⁶⁷⁷ *SABC case supra note 167 para 29 and 53; Economic Freedom Fighters v Speaker of the National Assembly and Others* 2016 (3) SA 580 (CC) para 54.

⁶⁷⁸ Constitution op cit note 11 at section 181 (2).

⁶⁷⁹ Ibid at section 181 (3) and (4).

⁶⁸⁰ *Democratic Alliance v Public Protector* 2019 (3) ALL SA 127 (GP) para 20; *Public Protector v South African Reserve Bank* 2019 (6) SA253 (CC) para 2.

⁶⁸¹ Constitution op cit note 11 at section 193 and 183.

⁶⁸² Ibid at section 193 (1); Public Protector Act 23 of 1994 at section 1A (PPA).

⁶⁸³ Ibid Constitution at section 194 (2).

⁶⁸⁴ Ibid at section 194 (1) & (2).

⁶⁸⁵ PPA op cit note 682 at section 2 (3).

⁶⁸⁶ Ibid at section 6 (5); Constitution op cit note 11 at section 182 (1)(a).

⁶⁸⁷ Ibid Constitution at section 182 (1)(b).

remedial action to correct any improper conduct.⁶⁸⁸ Additional powers of the Public Protector are contained in the PPA which attempt to assist in the effective performance of the three overarching constitutional powers.⁶⁸⁹ The Public Protector may not investigate court decisions and must be accessible to all persons and all communities.⁶⁹⁰

The Public Protector may investigate any matter referred to him or her by a complainant or at his or her own initiative or may refuse to investigate a complaint, in certain instances.⁶⁹¹ The method and procedure of an investigation is determined by the Public Protector, subject to certain specified rules and requirements.⁶⁹² Unless exceptional circumstances exist, the Public Protector shall not investigate a complaint if it is not reported within two years from the date on which the alleged incident occurred.⁶⁹³ Any person who: interferes with the office of the Public Protector, contravenes sections of the PPA or fails to disclose a personal interest, as required, may be guilty of an offence and subject to a fine or imprisonment.⁶⁹⁴

The Public Protector is one of the most important accountability checks on the powers exercised and the functions performed by organs of state, including SOCs.⁶⁹⁵ In order to ensure that the Public Protector can perform his or her essential watchdog function and strengthen constitutional democracy, he or she is given extensive statutory powers.⁶⁹⁶ The investigative powers of the Public Protector centre around allegations of maladministration, abuse or unjustifiable exercises of power, improper or dishonest conduct, corruption or improper or unlawful enrichment in government affairs, public administration or any public entity, which includes SOCs.⁶⁹⁷

⁶⁸⁸ Ibid at section 182 (1)(c).

⁶⁸⁹ Ibid at section 182 (2); PPA op cit note 682 at section 6.

⁶⁹⁰ Ibid at section 182 (3) and (4).

⁶⁹¹ PPA op cit note 682 at section 6.

⁶⁹² Ibid at section 7; Public Protector Act, Rules Relating to Investigations by the Public Protector and Matters Incidental Thereto in GN 945 *GG 41903* of 14 September 2018.

⁶⁹³ Ibid at section 6 (9).

⁶⁹⁴ Ibid at section 11.

⁶⁹⁵ Madonsela op cit note 256; Thulisile Madonsela 'Secure in Comfort' (2014) Public Protector South Africa report no. 25 of 2013/2014 Available at http://www.pprotect.org/sites/default/files/Legislation_report/Final%20Report%2019%20March%202014%20.pdf, accessed on 13 August 2020; Thulisile Madonsela 'Derailed' Public Protector South Africa (2015) Report No. 3 of 2015/2016 available at http://www.pprotect.org/sites/default/files/Legislation_report/PRASA_FINAL_28_August_2015.pdf, accessed on 13 August 2020.

⁶⁹⁶ PPA op cit note 682 at section 6; *EFF* case supra note 677 para 54.

⁶⁹⁷ Ibid at section 6; *Democratic Alliance v PP* case supra note 680 para 25.

Any report issued by the Public Protector must be made public unless exceptional circumstances exist, which are embodied in legislation, dictating the confidentiality of the report.⁶⁹⁸ The Public Protector is accountable to the National Assembly and must report on its activities and performance of his or her functions at least once a year.⁶⁹⁹

3.11.2 Binding Nature and Enforceability of Remedial Action

The Public Protector is constitutionally empowered to ‘*take appropriate remedial action*’.⁷⁰⁰ The power of the Public Protector to take appropriate remedial action against the improper conduct or maladministration is essential to enforcing the accountability of SOCs.⁷⁰¹ The binding nature of the remedial action issued by the Public Protector in her reports has been pronounced and confirmed by the Constitutional Court.⁷⁰²

Notwithstanding bolstering from the Constitutional Court, remedial action prescribed to, and binding upon, an SOC by the Public Protector is, arguably, perceived as voluntary.⁷⁰³ Acting outside of the bounds of their discretion, the board of an SOC and the Minister undertake a unilateral review of the remedial action dictated by the Public Protector and then disregard it entirely.⁷⁰⁴ An application for a formal review is the proper channel for challenging the scope and implementation of any remedial action prescribed by the Public Protector.⁷⁰⁵ Unless an application for review is made to the appropriate court with jurisdiction, there is no statutory provision for a unilateral review and the setting aside of a remedial action contained in a Public Protector’s report by the board of an SOC or the Minister.⁷⁰⁶

The remedial action taken by the Public Protector is binding and enforceable and it should not have to be made an order of court before being effectively implemented by an SOC.⁷⁰⁷ A failure to abide by and implement the remedial action stipulated in the Public Protector’s report dilutes the entire purpose for which the office was established, as an accountability check on organs of

⁶⁹⁸ Ibid at section 8; Constitution op cit note 11 at section 182 (5).

⁶⁹⁹ Ibid at section 181 (5).

⁷⁰⁰ Ibid at section 182 (1)(c).

⁷⁰¹ *SABC* case supra note 167 para 26; *Public Protector v Mail & Guardian* 2011 (4) SA 420 (SCA) para 19 & 22; *New National Party v Government of the Republic of South Africa & Others* 1999 (3) SA 191 (CC) para 98 & 99.

⁷⁰² *EFF* case supra note 677 para 194.

⁷⁰³ *SABC* case supra note 167 para 60.

⁷⁰⁴ Ibid para 47.

⁷⁰⁵ Ibid.

⁷⁰⁶ Ibid para 47, 48 & 60.

⁷⁰⁷ Ibid para 42; *EFF* case supra note 677 para 40.

state.⁷⁰⁸ Therefore, the enforceability of binding remedial action prescribed by the Public Protector on the board of an SOC and the Minister is paramount to ensuring the effective fulfilment of the function of the Public Protector, as a mechanism for upholding the accountability of SOCs.

Enforcement mechanisms, in general, are either reward or retribution based.⁷⁰⁹ The current enforcement mechanism to guarantee the implementation of remedial action stipulated by the Public Protector is largely retributive in nature. The board of an SOC and its directors may be held liable for failing to discharge their statutory duties which may include failing to implement remedial action directed by the Public Protector.⁷¹⁰

Furthermore, unless set aside by an order of court on an application for review, remedial action is enforceable by the Public Protector in terms of the rules of the PPA.⁷¹¹ The enforceability of the remedial action directed by the Public Protector rests in his or her right to report non-compliance to the Minister.⁷¹² The Public Protector may also enforce the implementation of remedial action by requesting assistance from the National Assembly or by initiating contempt proceedings against any person failing or neglecting to comply with the remedial action.⁷¹³

The remedial action directed by the Public Protector is undoubtedly binding on organs of state, including SOCs. In order for remedial action to be truly binding on SOCs, it needs to be enforced to ensure compliance by the board of the SOC and the Minister. The retributive measures, including liability for non-compliance and contempt of court proceedings, need to actually be implemented on recalcitrant directors of SOCs and the Minister. Idle threats of retribution, as opposed to the actual imposition of retribution, will continue to render the binding nature and subsequent enforceability of the remedial action taken by the Public Protector an exercise in futility.

⁷⁰⁸ Madonsela op cit note 16; Madonsela op cit note 695.

⁷⁰⁹ Davies, John et al 'Risk and Reward: tempering the pursuit of profit' (2010) *Association of Chartered Certified Accountants* at 18.

⁷¹⁰ Companies Act op cit note 11 at section 77; PFMA op cit note 11 at section 86; *SABC* case supra note 167 para 60.

⁷¹¹ *Democratic Alliance v PP* case supra note 680; PPA Rules op cit note 692 at rule 44.

⁷¹² *Ibid* at rule 44 (3)(a).

⁷¹³ *Ibid* at rule 44 (3) (b) & (c).

3.11.3 ‘Appropriateness’ of Remedial Action

There are a number of cases where applicants have approached the court to have the remedial action, prescribed by the Public Protector, set aside.⁷¹⁴ The Public Protector is authorized to ‘*take appropriate remedial action*’.⁷¹⁵ The rules of the PPA shed light on how ‘appropriate remedial action’ by the Public Protector may be taken.⁷¹⁶ The Public Protector must, if remedial action is taken, provide timelines within which the plan for the implementation of the remedial action by the SOC must be submitted to the Public Protector.⁷¹⁷

The Public Protector shall monitor implementation of the plan by the SOC or any agreement reached between the parties to resolve the complaint.⁷¹⁸ Save for these limited rules, there is no statutory definition of what would constitute appropriate remedial action to be taken by the Public Protector. The task of interpreting the appropriateness of the constitutional power of the Public Protector is, therefore, left to the judiciary.

The Constitutional Court has held that taking appropriate remedial action by the Public Protector means ‘*providing a proper, fitting, suitable and effective remedy for whatever complaint and against whomever the Public Protector is called upon to investigate*’.⁷¹⁹ The court must, on the facts and circumstances of each case, ascertain whether the remedial action prescribed by the Public Protector was appropriate.⁷²⁰ The court has also held that the remedial action directed by the Public Protector must be rationally connected to her reasoning for taking the action and to the purpose for which his or her power was given, otherwise the remedy will be arbitrary.⁷²¹ The

⁷¹⁴ De Vos, Pierre ‘Nonsensical? How the Public Protector and Others use Motive to Avoid Talking about the Facts and the Law’ (2019) Available at: <http://constitutionallyspeaking.co.za/nonsensical-how-the-public-protector-and-others-use-motive-to-avoid-talking-about-the-facts-and-the-law/>, accessed on 14 August 2020; *Democratic Alliance v PP* case supra note 680; *ABSA Bank Limited and Others v Public Protector and Others* 2018 (2) ALL SA 1 (GP); *Minister of Home Affairs and Another v Public Protector of the Republic of South Africa* 2018 (3) SA 380 (SCA) para 37; *South African Reserve Bank v Public Protector & Others* 2017 (6) SA 198 (GP).

⁷¹⁵ Constitution op cit note 11 section 182 (1)(c).

⁷¹⁶ PPA Rules op cit note 692.

⁷¹⁷ Ibid at rule 44 (1).

⁷¹⁸ Ibid at rule 44 (2).

⁷¹⁹ *EFF* case supra note 677 para 68 & 71 (e).

⁷²⁰ Ibid para 71; *SABC* case supra note 167 para 31; *Mail & Guardian* case supra note 701 para 5; *Democratic Alliance v President of South Africa* 2013 (1) SA 249 para 39.

⁷²¹ *Democratic Alliance* case supra note 720 para 38 & 149; *Pharmaceutical Manufacturers Association & Others v President of the Republic of South Africa & Others* 2000 (2) SA 674 (CC) para 85; *Reserve Bank* case supra note 714 para 57.

proposed remedial action taken by the Public Protector must be based on accurate findings of fact and a correct application of the law in order to pass legal muster.⁷²²

The appropriateness of the remedial action taken by the Public Protector may have a bearing on its enforceability, with respect to the board of an SOC or its Minister. If the Public Protector erred in his or her findings of fact or on an application of the law, the remedial action will not be appropriate, rational, effective or capable of enforcement by the Public Protector or any court.⁷²³

Therefore, the Public Protector should take care in the formulation of the remedial action to ensure that it is effective, rational, proper and fitting in order to be enforceable and not set aside by the court on an application to review.

3.12 The Separation of Powers Accountability Mechanism

An SOC is under the supervision and control of the executive branch of government as set out under the provisions of the PFMA.⁷²⁴ South Africa, as a constitutional democracy, subscribes to the doctrine of the separation of powers which requires that the three tiers of government: the executive, legislature and judiciary provide accountability checks over one another's actions.⁷²⁵

The legislature and the judiciary act as the separation of powers accountability mechanism for an SOC, as part of the checks and balances they provide over the actions of the executive.⁷²⁶ As a precursor to their accountability checks over the executive, and particularly SOCs, a brief description of the structure and roles provided by the executive, legislature and judiciary is necessary.

⁷²² *Chairman of the State Tender Board v Digital Voice Processing (Pty) Ltd* 2012 (2) SA 16 (SCA) para 40.

⁷²³ *EFF* case supra note 677 para 68 & 69.

⁷²⁴ Constitution op cit note 11; PFMA op cit note 11.

⁷²⁵ *EFF* case supra note 677 para 90 -2; Constitution op cit note 11 at section 40 (1); *Glenister* case supra note 511 para 123

⁷²⁶ Interim Constitution Act 200 of 1993 sch 4; *Certification of the Constitution of the Republic of South Africa, 1996* 1996 (4) SA 744 (CC); Timothy Hodgson 'The mysteriously appearing and disappearing doctrine of the separation of powers: toward a distinctly South Africa doctrine for a more radically transformative Constitution' (2018) 34 *South African Journal on Human Rights* 57 – 90; *South African Association of Personal Injury Lawyers v Heath* 2001 (1) BCLR 77 (CC) para 46.

3.12.1 The Executive

An SOC is a juristic person under the ownership control of the national executive.⁷²⁷ The PFMA does not provide a definition for the national executive.⁷²⁸ However, it defines the ‘*executive authority*’ for an SOC as ‘*the Cabinet member who is accountable to Parliament for that public entity or in whose portfolio it falls.*’⁷²⁹ Most SOCs fall under the portfolio of the Department of Public Enterprises under the auspices of the Minister.⁷³⁰ Therefore, many SOCs are accountable to the Minister, as their executive authority under the PFMA and representative of the state, as the sole shareholder.⁷³¹

The accountability check which the state, specifically the Minister, performs over an SOC as its sole shareholder is discussed previously under the internal accountability mechanisms. This discussion now revolves around the broader measures which the executive takes in order to hold SOCs accountable. Therefore, a brief overview of the structure of the executive and its accountability mechanisms is required in order to understand the accountability of an SOC.

The executive is responsible for the implementation of national legislation.⁷³² Therefore, the executive is responsible for ensuring that an SOC complies with all of its statutory duties, obligations and responsibilities to ensure the effective implementation of legislation and to accurately account for its decisions to the executive. The accountability of an SOC to the executive is hierarchical in nature in that the board is accountable to the Minister, the Minister is accountable to Cabinet and Cabinet is accountable to Parliament.⁷³³

Parliament consists of the National Assembly and the NCOP.⁷³⁴ The National Assembly is expected to account to the public, as their representative, by overseeing and scrutinizing executive action, including the implementation of legislation and to establish mechanisms to ensure the

⁷²⁷ E, Ljeoma & A Sambumbu ‘A framework for improving public accountability in South Africa’ (2013) 48 *Journal of Public Administration* 282 – 298 at 287; King IV op cit note 19 at 115.

⁷²⁸ Ibid.

⁷²⁹ Ibid PFMA op cit note 11 at section 1; National Treasury of South Africa ‘Governance Oversight Role over State-Owned Entities’ (2005) Available at: <http://www.treasury.gov.za/publications/other/soe/Governanceper cent20Oversightper cent20Role.pdf>, accessed on 13 August 2020 at 2.

⁷³⁰ DPE op cit note 128.

⁷³¹ PFMA op cit note 11 at section 1 & 49.

⁷³² Ibid at section 85 (2)(a).

⁷³³ Ibid at section 91 & 92 (2); PFMA op cit note 11 at section 1 & 49; National Treasury op cit 729 at 5.

⁷³⁴ Constitution op cit note 11 at section 42 (1).

accountability to it of all executive organs of state, in the national sphere of government.⁷³⁵ The national sphere of government would include SOCs which indicates that the National Assembly has the responsibility to provide for mechanisms which ensure the accountability to it of all SOCs. The NCOP represents the provinces and has a mandate to ensure that the interests of the respective provinces are taken into account in the national sphere of government.⁷³⁶

Cabinet consists of the President, as the head of cabinet, the Deputy President and the ministers.⁷³⁷ The President exercises the executive authority of the Republic, together with the Deputy President and ministers.⁷³⁸ The ministers and Deputy President are appointed and removed by the President.⁷³⁹ The President also assigns the powers and functions of each minister as well as the Deputy President.⁷⁴⁰ The Deputy President and Ministers are selected from the members of the National Assembly, save for two ministers which may be appointed from outside of the National Assembly.⁷⁴¹

Although the Constitution confers wide powers on the President in respect of the ministers and the Deputy President, all members of Cabinet are accountable, collectively and individually, to Parliament for the exercise of their powers and the performance of their functions and are bound by the Constitution.⁷⁴² The Cabinet members are to abide by a code of conduct as directed by the Executive Member's Ethics Act 82 of 1998.⁷⁴³ Ministers may assign any of their powers or functions to an executive provincial council or municipal council but remain responsible for the performance of the function or power and accountable to the National Assembly.⁷⁴⁴

The President is required to uphold, defend and respect the Constitution, as head of the Republic and national executive and is specifically responsible for fulfilling certain constitutional duties.⁷⁴⁵ The President has the sole discretion to dismiss ministers and there are no constitutional

⁷³⁵ Ibid at section 42 (1), (3) & 55 (2)(b).

⁷³⁶ Ibid at section 42 (4).

⁷³⁷ Ibid at section 91 (1).

⁷³⁸ Ibid at section 85 (1) & (2).

⁷³⁹ Ibid at section 91 (2).

⁷⁴⁰ Ibid at section 91 (2).

⁷⁴¹ Ibid at section 91 (3).

⁷⁴² Ibid at section 92.

⁷⁴³ Ibid at section 96; Executive Member's Ethics Act No 82 of 1998.

⁷⁴⁴ Ibid t section 92 & 99.

⁷⁴⁵ Ibid at section 83 and 84.

requirements pertaining to such dismissal which confers a wide, often abused, power to reshuffle un-cooperative ministers.⁷⁴⁶

The President may only be removed, on certain grounds, on a resolution of a two-third majority vote of the National Assembly.⁷⁴⁷ The National Assembly, through a majority, may pass a vote of no confidence in the President or in the Cabinet, excluding the President.⁷⁴⁸ If a vote of no confidence in Cabinet is passed, the President must reconstitute the Cabinet.⁷⁴⁹ If a vote of no confidence in the President is passed, the President, the Deputy President and the ministers must all resign.⁷⁵⁰

The national executive consists of a clustered system of government portfolios which comprise various government departments.⁷⁵¹ Each government portfolio has a specific aim and objective and the government departments are then categorized according the portfolio they will best serve.⁷⁵² The main objective of the portfolio system is to ensure the alignment of government strategies, plans and policies, to monitor the implementation of such and to create a platform for consulting on matters which are to be taken to Cabinet.⁷⁵³

Many SOCs report to the Department of Public Enterprises which is under the purview of the Minister.⁷⁵⁴ The Department of Public Enterprises falls under two government portfolios: the cluster for economic sectors, investment, employment and infrastructure development and the cluster for governance, state capacity and institutional development.⁷⁵⁵ Whilst each government department is distinct in its portfolio categorization, they are inter-related and interdependent in overlapping functions and provide oversight and accountability checks on one another.⁷⁵⁶

The National Treasury was established by the PFMA, in accordance with the Constitution and comprises the Minister of Finance and the Department of Finance.⁷⁵⁷ The National Treasury is

⁷⁴⁶ Ibid at section 91 (2); Hodgson op cit note 726 at 80.

⁷⁴⁷ Ibid at section 89.

⁷⁴⁸ Ibid at section 102 (1).

⁷⁴⁹ Ibid at section 102 (1).

⁷⁵⁰ Ibid at section 102 (2).

⁷⁵¹ South African Government 'Structure and Functions of the South African Government' available at <http://www.gov.za/node/537988> accessed on 26 August 2020.

⁷⁵² Ibid.

⁷⁵³ Ibid.

⁷⁵⁴ DPE op cit note 128; Makwethu (AGSA) op cit note 18 at 138.

⁷⁵⁵ South African Government op cit note 751.

⁷⁵⁶ Bronstein & Oliver op cit note 5.

⁷⁵⁷ PFMA op cit note 11 at section 5 (1)(a) & (b); Constitution op cit note 11 at section 216 (1).

essential to ensuring transparency and expenditure control for each sphere of government.⁷⁵⁸ As a result of its importance, the Department of Finance falls under almost all of the government clusters.⁷⁵⁹ The PFMA, and the treasury regulations, dictate the powers and functions which are to be performed by the National Treasury.⁷⁶⁰ The Minister of Finance exercises an accountability check over SOCs by ensuring that the board complies with the provisions of the PFMA.⁷⁶¹

One of the functions which must be performed by the National Treasury is to prepare consolidated annual financial statements for public entities under the ownership control of the national executive which includes SOCs.⁷⁶² In the preparation of the financial statements, the National Treasury may uncover certain financial issues for SOCs, and therefore provides an important accountability check over the financial affairs of SOCs.⁷⁶³

There are stringent statutory provisions which are meant to ensure the accountability of SOCs to the executive, as the sole shareholder. However, in order to ensure compliance with these statutory provisions, the executive should be ready and willing to impose retributive measures against the boards of SOCs which fail to fulfil their obligations. An unwillingness from the executive to enforce the accountability of an SOC will, by necessary implication, increase the need for the judiciary and legislature to ensure the accountability of SOCs.

3.12.2 The Legislature

The national legislative authority vests in Parliament which consists of two houses: the National Assembly and the NCOP.⁷⁶⁴ The National Assembly and the NCOP discharge legislative powers and processes, designated with respect to national, provincial and local spheres of government, in accordance with the provisions of the Constitution.⁷⁶⁵ The National Assembly has the legislative authority to make and amend the Constitution and national legislation.⁷⁶⁶ As SOCs fall under the

⁷⁵⁸ Constitution op cit note 11 at section 216 (1).

⁷⁵⁹ South African Government op cit note 751.

⁷⁶⁰ PFMA op cit note 11 at ch 2.

⁷⁶¹ Ibid at section 63 (2).

⁷⁶² Ibid at section 8 (1)(a)(ii).

⁷⁶³ Makwethu (AGSA) op cit note 18 at 138.

⁷⁶⁴ Constitution op cit note 11 at section 42 (1) & 43.

⁷⁶⁵ Ibid at section 42.

⁷⁶⁶ Ibid at section 43 (a) & 44 (1)(a).

purview of national legislation, a further discussion on the legislative authority vested in the provincial and local legislatures is not germane to this research.

The National Assembly comprises no more than four hundred members who are citizens and qualified to vote for the National Assembly.⁷⁶⁷ Members of the National Assembly are elected in terms of a proportional representation electoral system, based on the common voters roll and national legislation.⁷⁶⁸ The composition of the members of the National Assembly is proportional to the number of votes every political party wins in the national elections.⁷⁶⁹ Therefore, the majority of the members of the National Assembly will be members of the political party who won the national elections, on a proportional representation basis.⁷⁷⁰

The National Assembly has two primary constitutional powers.⁷⁷¹ First, the National Assembly is required to initiate or prepare legislation (except money bills) and to consider, pass, amend or reject legislation which comes before it.⁷⁷² Secondly, the National Assembly is required to maintain oversight over: the exercise of national executive authority (including the implementation of legislation) and any organ of state and to provide for mechanisms which ensure that all organs of state in the national sphere of government are accountable to it.⁷⁷³ This constitutional obligation of the National Assembly corresponds to the constitutional requirement placed on Cabinet, to account to the National Assembly.⁷⁷⁴

The National Assembly utilises its constitutional function of passing legislation to maintain oversight and accountability of SOCs.⁷⁷⁵ Various legislative enactments contain mandatory reporting, disclosure and accountability provisions with which the boards of SOCs are required to comply, the most predominant of which being the PFMA together with the treasury regulations.⁷⁷⁶ The efficiency and accuracy of the legislature, in passing national legislation, will assist the executive in its function of implementing legislation.⁷⁷⁷ The power and functions of the executive

⁷⁶⁷ Parliamentary Monitoring Group ‘Structure-of Government (2018) available at <http://www.pmg.org.za/page/structure-of-government>, accessed on 14 August 2020.

⁷⁶⁸ Ibid; Constitution op cit note 11 at section 46.

⁷⁶⁹ Ibid at 5.

⁷⁷⁰ Constitution op cit note 11 at section 46 (1).

⁷⁷¹ Ibid at section 55 (1) & (2).

⁷⁷² Ibid at section 55 (1)(a) & (b).

⁷⁷³ Ibid at section 55 (2)(a) & (b).

⁷⁷⁴ Ibid at section 92.

⁷⁷⁵ National Treasury op cit note 729 at 2.

⁷⁷⁶ PFMA op cit note 11; Treasury Regulations op cit note 291.

⁷⁷⁷ National Treasury op cit note 729 at 3.

are determined and prescribed by the legislature through the passing of national legislation, to that effect.⁷⁷⁸

The National Assembly establishes committees in order to assist with its constitutional obligation to provide mechanisms to ensure that the executive is accountable to it and to maintain oversight of any organ of state and the exercise of the executive authority to implement legislation.⁷⁷⁹ The establishment, composition, powers, functions, procedures and duration of the committees are provided for by the National Assembly.⁷⁸⁰ There are various types of committees which may be established by the National Assembly namely: portfolio' committees, standing committees and ad hoc committees.⁷⁸¹

Portfolio committees are established by the National Assembly to monitor and supervise each government department of the executive.⁷⁸² Permanent committees are known as standing committees and a committee combining both members of the National Assembly and the NCOP are joint committees.⁷⁸³ Ad hoc committees are once off, temporary committees, established to consider specific issues and are disbanded once their mandates are fulfilled.⁷⁸⁴

These committees do not take decisions but make recommendations to the legislature, generally in the form of reports submitted to the National Assembly.⁷⁸⁵ Committees are also empowered, subject to legislation and the Constitution, to: summon persons to appear before them to give evidence, conduct public hearings, consult any assembly or council committee, determine their own working arrangements and exercise any other powers assigned to them by the Constitution, legislation, the Rules of the National Assembly or a resolution of the National Assembly.⁷⁸⁶

There are a number of committees established under the rules of the National Assembly, legislation and the NCOP to supervise and monitor the performance of SOCs.⁷⁸⁷ The powers and functions

⁷⁷⁸ Ibid.

⁷⁷⁹ Ibid at 4; Constitution op cit note 11 at section 55 (2).

⁷⁸⁰ Constitution op cit note 11 at section 57 (2)(a); Parliament of the Republic of South Africa 'Rules of the National Assembly' (2016) 9 ed. Available at http://www.parliament.gov.za/storage/app/media/Rules/NA/2016-09-28_NA_RULES.pdf, accessed on 14 August 2020 ch 12 rule 167.

⁷⁸¹ National Treasury op cit note 729 at 5 – 8; Parliament op cit note 780 at rule 225, 243 & 253.

⁷⁸² Ibid at rule 150 (1)(v) & 225.

⁷⁸³ Ibid at rule 150 (vi).

⁷⁸⁴ Ibid at rule 150 (vii).

⁷⁸⁵ Ibid at rule 227 (1)(c).

⁷⁸⁶ Ibid at rule 167.

⁷⁸⁷ Makwethu (AGSA) op cit note 18 at 16 & 37.

of the various committees, pertaining to the oversight and monitoring of SOCs may overlap and are usually inter-related and performed simultaneously or concurrently to ensure the accountability of the national executive for the performance of SOCs under its ownership control. These committees include: The Portfolio Committee on Public Enterprises (‘Portfolio Committee’), the Standing Committee on Public Accounts (‘SCOPA’), the Standing Committee on Finance and the Standing Committee on the Auditor-General.⁷⁸⁸

The two most influential of these committees are, arguably, the SCOPA and the Standing Committee on Finance.⁷⁸⁹ Over the last decade, both committees have held numerous meetings and published reports concerning the oversight and monitoring of various SOCs, including SAA and Eskom.⁷⁹⁰

Even though the doctrine of the separation of powers implores a strict separation between the legislature and the executive, the appointment of ministers, by the President, from the members of the National Assembly makes an overlap of membership between the two spheres, a practical eventuality.⁷⁹¹ As a result of the concurrent membership of the ministers, in terms of the executive and legislative spheres, the accountability check which these two spheres have over each other is relatively diluted, as their respective independence from each other may be compromised.⁷⁹² As a result, the judiciary is considered the most vital accountability check over the legislature and the executive.⁷⁹³

3.12.3 The Judiciary

The third sphere of government is the judiciary, whose authority is vested in the court system.⁷⁹⁴ The judiciary is independent and subject only to the Constitution and the law of the Republic, which must be applied without fear, favour or prejudice.⁷⁹⁵ The independence of the judiciary is

⁷⁸⁸ Parliament op cit note 780 at rules 150 (1)(v)(vi), (b)(ii) & (iv).

⁷⁸⁹ Parliamentary Monitoring Group ‘National Assembly Committee: Standing Committee on Public Accounts (SCOPA) available at <http://pmg.org.za/committee/42>, accessed on 14 August 2020.

⁷⁹⁰ Kevin Brandt & Jartta Kassen ‘ITS NOT ALL BLUE SKIES FOR SAA AS SCOPA NOW WANTS IT TO ACCOUNT’ (2019) *EWN* available at <http://ewn.co.za/2019/11/23/it-s-not-all-blue-skies-for-saa-as-scopa-now-wants-it-to-account>, accessed on 14 August 2020; Sibongile Khumalo ‘SCOPA places Eskom on its Priority “watch list” ‘ *Fin24* 29 August 2019 available at <http://www.fin24.com/Economy/South-Africa/scopa-places-eskom-on-its-priority-watch-list-20190829>, accessed on 14 August 2020.

⁷⁹¹ National Treasury op cit note 729 at 40; Constitution op cit note 11 at section 91 (3)(b) & 47(1)(a)(i).

⁷⁹² *Ibid* at 41.

⁷⁹³ *Ibid*; *Certification* case supra note 726 para 123; *Personal Injury Lawyers* case supra note 726 para 25.

⁷⁹⁴ Constitution op cit note 11 at section 165 (1); *Certification* case supra note 726 para 45.

⁷⁹⁵ *Ibid* at section 165 (2).

integral to its effectiveness and must be maintained, protected and upheld by the legislature and executive spheres of government and all organs of state.⁷⁹⁶ The judicial authority of the courts is paramount to a constitutional democracy and any order of court is binding on all persons and all organs of state to whom it applies.⁷⁹⁷

The court system comprises the magistrates courts, high courts, the Supreme Court of Appeal and the Constitutional Court.⁷⁹⁸ Any other court may also be established by an Act of Parliament which will be included in the court system, having similar status as that of the magistrates courts or high courts.⁷⁹⁹ The court system depicts a hierarchical judicial authority, from the magistrates courts to the Constitutional Court. The Constitutional Court is the highest court in South Africa and will only adjudicate upon constitutional matters, unless it decides otherwise that it is in the public's interest for a matter to heard within its jurisdiction.⁸⁰⁰

Judges of the courts are appointed by the President on the advice of the Judicial Services Commission which is established and mandated by the Constitution and national legislation.⁸⁰¹ The Chief Justice and Deputy Chief Justice of the Constitutional Court and the President and Deputy President of the Supreme Court of Appeal are all appointed by the President after consulting the Judicial Service Commission and the leaders of the political parties represented in the National Assembly.⁸⁰² Other Constitutional Court judges are appointed by the President after consultation with the Chief Justice and leaders of the political parties represented in the National Assembly.⁸⁰³ All judicial officers must take an oath to uphold the Constitution prior to engaging in any of their judicial functions.⁸⁰⁴

The National Prosecuting Authority ('NPA') is structured according to national legislation, subject to the Constitution and is responsible for instituting criminal proceedings, and ancillary activities, on behalf of the state.⁸⁰⁵ The NPA is headed by the National Director of Public Prosecutions, who

⁷⁹⁶ Ibid at section 165 (3) & (4); *Personal Injury Lawyers* supra note 726 para 31.

⁷⁹⁷ Ibid at section 165 (5).

⁷⁹⁸ Ibid at section 166 (1).

⁷⁹⁹ Ibid at section 166 (2).

⁸⁰⁰ Ibid at section 167 (3).

⁸⁰¹ Ibid at section 174 (6).

⁸⁰² Ibid at section 174 (3).

⁸⁰³ Ibid at section 174 (4).

⁸⁰⁴ Ibid at section 174 (8).

⁸⁰⁵ Ibid at section 179 (1) & (2).

is appointed by the President.⁸⁰⁶ The Directors of Public Prosecutions and prosecutors are appointed in accordance with national legislation.⁸⁰⁷ Directors of Public Prosecutions are responsible for prosecutions in specific jurisdictions, subject to possible review by the National Director of Public Prosecutions.⁸⁰⁸ The ultimate responsibility over the functions and performance of the NPA rests in the Minister of Justice and Correctional Services.⁸⁰⁹

The judiciary provides an important, impartial and independent check on the executive and legislature.⁸¹⁰ Each sphere of government must respect the independency of the other and perform constitutional obligations without overstepping into the bounds of another sphere's functions.⁸¹¹ The judiciary is authorized to review executive conduct and national legislation to ensure compliance with the Bill of Rights and the Constitution.⁸¹² The judiciary is not subsuming the functions or powers of either the legislature or the executive by maintaining oversight and making the branches of government accountable to one another.⁸¹³

The judiciary exercises its oversight function over the executive by scrutinizing conduct, through applications or actions brought to the courts, to ensure compliance by all organs of state with the Constitution.⁸¹⁴ This includes supervision of the conduct of ministers and government departments who are required to supervise the conduct of the board of an SOC. The President also has the power to establish judicial commissions of inquiry to inquire into any actions or conduct of the executive.⁸¹⁵ A commission of inquiry would be able to scrutinize the conduct of the board of an SOC, as national public entity as well as the conduct of the Minister to whom the board is required to account.⁸¹⁶

The court system and judicial commissions of inquiry provide the most effective judicial check over the executive in an attempt to curb abuses of power and improve the constitutional precepts of accountability and transparency. The independence of the judiciary is paramount to its

⁸⁰⁶ Ibid at section 179 (1)(a).

⁸⁰⁷ Ibid at section 179 (1)(b); National Prosecuting Authority Act 32 of 1998.

⁸⁰⁸ Ibid at section 179 (3)(b) & 179 (5)(d).

⁸⁰⁹ Ibid at section 179 (6).

⁸¹⁰ *Certification* case supra note 726 para 123; *Personal Injury Lawyers* supra note 726 para 25.

⁸¹¹ *EFF* case supra note 677 para 92.

⁸¹² *Certification* case supra note 726 para 54; *Personal Injury Lawyers* case supra note 726 para 112.

⁸¹³ Ibid para 154.

⁸¹⁴ *President of the Republic of South Africa v Hugo* 1997 (4) SA 1 (CC); *President of the Republic of South Africa v SARFU* 2000 (1) SA (1) (CC).

⁸¹⁵ Constitution op cit note 11 at section 84 (1)(f); Commissions Act 8 of 1947.

⁸¹⁶ PFMA op cit note 11 at section 49; Madonsela op cit note 16 at 353

effectiveness as an external accountability check on the executive in its supervision over SOCs.⁸¹⁷ In an unstable economic climate, with many allegations of state corruption, it is imperative that the integrity and independence of the judiciary is maintained and any threat to it should be curtailed as a matter of priority to ensure our constitutional dispensation.

3.13 The Last Resort: The Public

The public is the ultimate stakeholder of SOCs as the executive may utilise taxpayer monies to fund SOCs.⁸¹⁸ The extent to which the board of an SOC is accountable to the public is limited through the provisions of the Constitution and national legislation. The Constitution makes provision for the government of South Africa to observe and adhere to the principles enshrined therein and to conduct their activities within the parameters of ensuring the well-being, security, national unity, peace and protection of the Republic and its people.⁸¹⁹

The government, and all organs of state, are to provide effective, transparent, accountable and coherent government for the Republic.⁸²⁰ Although there is a constitutional requirement for organs of state and public administration to be accountable, there is no specific constitutional requirement which states that the government must be directly accountable to the people of South Africa.⁸²¹

Similarly, the board of an SOC is accountable to the executive, particularly the Minister but there is no statutory requirement on the board of an SOC to specifically account to the public.⁸²² The Constitution allows for public access and involvement in the legislative processes and activities of the National Assembly and its various committees.⁸²³ However, the right of public access may be curtailed by the National Assembly, if it is reasonable and justifiable to do so in an open and democratic society.⁸²⁴

The only mechanism for holding the National Assembly, the President and his cabinet accountable is through a vote of no confidence, for which a two third majority resolution of the National Assembly is required.⁸²⁵ If the ruling party holds a two-third majority of the votes in the National

⁸¹⁷ *Certification* case supra note 726 para 154.

⁸¹⁸ *Futuregrowth* op cit note 10 at 30.

⁸¹⁹ Constitution op cit note 11 at section 41 (1).

⁸²⁰ *Ibid* at section 41 (1)(c).

⁸²¹ *Ibid* at section 41 (1)(c) & 195 (1)(f).

⁸²² *PFMA* op cit note 11 at section 49.

⁸²³ Constitution op cit note 11 at section 59 (1).

⁸²⁴ *Ibid* at section 59 (2).

⁸²⁵ *Ibid* at section 102.

Assembly, the likelihood of a motion of no confidence being passed is remote. Arguably, the Constitution did not make provision for any checks and balances for possible abuses of power by the ruling party which holds a two-third majority in the National Assembly. This Constitutional oversight has resulted in a lack of accountability for the ruling party to the public.⁸²⁶

A mechanism available to the public in attempting to hold an SOC, and the executive, to account is through activism including public protests, rallies and applications to court, where possible. The public have rallied behind institutional organizations, founded and funded by private citizens, such as OUTA and Corruption Watch.⁸²⁷ These institutions have motivated the public, in their stakeholder activism roles, by bringing court applications against directors of SOCs who have allegedly breached their duties or committed criminal offences.⁸²⁸ The most infamous of which is the successful delinquency order which the court granted against Duduzile Myeni ('Myeni'), former non-executive chairperson of SAA, in an application brought by OUTA.⁸²⁹

Although there are mechanisms for the public to act as an external accountability measure for SOCs, these should be considered an avenue of last resort. The impact brought about by public protests is meant to place pressure on the executive to hold SOCs accountable. This is especially evident when the protests gain local and international traction through media reports. However, it is unrealistic to expect the public to continually resort to protests in order to hold SOCs and the executive to account. Without having a direct interest in the performance of SOCs, as is the case with shareholders of private companies, the motivation of the public to continually hold the board of an SOC and its Minister to account, understandably wanes over time. With the advent of the Constitution, it remains the primary responsibility of the executive, legislature and judiciary to hold an SOC and the Minister accountable.⁸³⁰

3.14 Conclusion

There are numerous internal and external accountability measures available for SOCs, most of which are mandated through statutes. It is submitted that it was the intention of the legislature, with the enactment of numerous statutes to ensure that SOCs, as custodians of national assets are

⁸²⁶ Ljeoma op cit note 727 at 283

⁸²⁷ The Organisation Undoing Tax Abuse (OUTA) 'About Us' available at <http://www.oua.co.za/about> accessed on 27 August 2020; Corruption Watch 'About Us' available at <http://www.corruptionwatch.org.za/about-us/who-we-are/about-corruption-watch/> accessed on 27 August 2020.

⁸²⁸ Ibid.

⁸²⁹ *OUTA v Myeni* case Supra note 346.

⁸³⁰ Constitution op cit note 11 at section 41 (1)(c), 92 (2) & 195 (1)(f); *Certification* case supra note 726 para 123.

held to the utmost level of accountability. The board of an SOC and its directors, as the focal point for accountability, should discharge their duties at all times to ensure that the interests of the SOC are protected and that they remain accountable to the Minister, as the representative of the state as the sole shareholder. The external accountability measures should also be enforced to ensure that the board of an SOC remains accountable. However, without the continuous enforcement of the internal and external measures, the accountability of SOCs will remain an issue.

CHAPTER FOUR: A LACK OF ACCOUNTABILITY FOR SOCS

4 Introduction

It is submitted that many SOCs in South Africa have had significant accountability and performance issues over the last decade.⁸³¹ Notwithstanding the aforementioned internal and external measures, the omission of an adequate enforcement mechanism has effectively eroded the actual accountability of SOCs. A case study of SAA, based on research garnered from a direct analysis and interpretation of the SAA Reports, will be used as an illustration of an SOC which has exhibited accountability and performance issues over the last decade.⁸³² It is proposed that the enforcement of the accountability of SOCs, such as SAA, may assist in improving their future performance, on a holistic basis with a focus on financial performance.

4.1 The Performance of SOCs

South African SOCs have the ability to drive and accelerate national growth and development for the economy.⁸³³ Essential for the provision of certain service delivery and public policy functions, as well as the ability to discharge commercial mandates, the role of SOCs remains pivotal.⁸³⁴ Prolific in the strategic sectors of energy, transport, telecommunications and manufacturing, the performance of SOCs may heavily impact the growth and development of our economy.⁸³⁵

Unfortunately, the historical track record of almost all SOCs in South Africa is underwhelming.⁸³⁶ The worst performers of these SOCs are undoubtedly Eskom, the South African Broadcasting Corporation SOC Limited ('SABC') and SAA which has recently gone into business rescue.⁸³⁷ The dismal financial performance of these three SOCs, over the last decade, has had a direct negative impact on the growth of the economy.⁸³⁸

⁸³¹ Lynn McGregor 'Improving Corporate Governance of South African State-Owned Companies (SOCs)' 2014 available at: <http://pdfslide.net/download/link/improving-corporate-governance-of-south-african-state-documents-sa-socimproving>, accessed on 13 August 2020 at 6; Thomas op cit note 9 at 45; Kanyane op cit note 10; Futuregrowth op cit note 10.

⁸³² SAA reports op cit note 20.

⁸³³ Fourie op cit note 167 at 32.

⁸³⁴ Ibid at 31.

⁸³⁵ Ibid at 30.

⁸³⁶ McGregor op cit note 831 at 6; Thomas op cit note 9 at 452; National Treasury op cit note 1 at 90.

⁸³⁷ Fourie op cit note 167 at 35; National Treasury op cit note 1 at 93 – 4.

⁸³⁸ Ibid at 38; National Treasury at 90.

Arguably, the intention in the establishment of these SOCs was for them to discharge dual mandates, fulfilling commercial and non-commercial objectives.⁸³⁹ In order to effectively discharge their non-commercial goals these SOCs are to ensure the successful performance of their commercial mandates.⁸⁴⁰ The successful financial performance of these SOCs meant that they did not have to rely substantially or fully on state funding, in accordance with the definition of them as ‘Enterprises’ under the PFMA.⁸⁴¹ It was not the intention of the legislature, on the promulgation of the PFMA, that the state, with its limited resources, be the sole funder of SOCs, defined as ‘Enterprises’, such as Eskom and SAA.⁸⁴²

However, many SOCs, such as SAA and Eskom, have not been able to sustain their own commercial operations for many years and are now reliant on state funding to continue their commercial and non-commercial operations.⁸⁴³ It is conceivable that the very cause of the financial distress for these SOCs may have been the requirement to discharge a dual mandate.⁸⁴⁴ The conflicting goals, which are often present when attempting to fulfil both mandates, creates an inevitable strain on the ability of the SOC to perform either mandate effectively.⁸⁴⁵ SAA, for instance, has to comply with designated trade routes, in terms of policy directives issued by the state, notwithstanding the profitability considerations of such routes.⁸⁴⁶ The commercial objective of SAA may therefore be hindered by its non-commercial objective.

The financial performance of these SOCs is further compounded due to the costs of compliance with various pieces of legislation.⁸⁴⁷ The convoluted provisions of the PFMA and, possibly contradictory requirements of the Companies Act, make compliance a cumbersome and difficult task for the board of these SOCs.⁸⁴⁸ The compliance costs for these SOCs may far outweigh any such similar costs faced by their private counterparts which may then out compete SOCs operating in the same industry.⁸⁴⁹

⁸³⁹ Ibid at 39.

⁸⁴⁰ National Treasury op cit note 1 at 90.

⁸⁴¹ PFMA op cit note 11 at section 1.

⁸⁴² Ibid; Thabane op cit note 9 at 15 – 20.

⁸⁴³ Ibid at 94 -4; Fourie op cit note 167 at 39.

⁸⁴⁴ Kanyane op cit note 10 at 33.

⁸⁴⁵ Ibid; Fourie op cit note 167 at 38.

⁸⁴⁶ Ibid; Futuregrowth op cit note 10 at 14.

⁸⁴⁷ Ibid; McGregor op cit note 831 at 8.

⁸⁴⁸ Kanyane op cit note 10 at 33; Thomas op cit note 9 at 453.

⁸⁴⁹ Ibid at 34.

The cost of compliance with the legislation coupled with conflicting mandates, may result in an unlevel playing field for SOCs attempting to compete with their private counterparts in the same industry.⁸⁵⁰ The hindered competitiveness of SOCs may inevitably negatively affect their financial performance. South Africa's economy, can ill afford to completely subsidize these SOCs which are a heavy burden on the national purse.⁸⁵¹ Notwithstanding many of the reasons for their underperformance, SOCs exhibit a dire lack of accountability which may hinder their ability to effectively implement a solution to improve their future financial performance.⁸⁵²

4.2 The Accountability Issue

Numerous allegations of a complete lack of accountability from certain SOCs such as SAA, over the last decade, have been well documented.⁸⁵³ It is arguable that a lack of accountability will negatively impact the financial performance of an SOC, as may be illustrated with the use of SAA as a case study in the subsequent paragraphs of this chapter. It is submitted that the accountability of SOCs is further compounded by two predominant issues which are specific to SOCs due to their very nature. First, the issue associated with the concept of 'double agency'.⁸⁵⁴ Secondly, the issue arising from the fact that the state is an SOC's sole shareholder.⁸⁵⁵

The double agency issue represents the dual layer of accountability faced by SOCs.⁸⁵⁶ First, the board and its directors are accountable to the state, as sole shareholder of the SOC.⁸⁵⁷ Secondly, the shareholder representative of the state, the Minister, is then accountable to the National Assembly.⁸⁵⁸ This dual layer represents inherent risks which are specific only to SOCs, in that accountability needs to be actively enforced on two levels as opposed to just one level as would be the case for their private counterparts.

A breakdown in communication or transparency, at either level, may result in a lack of accountability for SOCs. The dual accountability structure of SOCs needs to be continually

⁸⁵⁰ Kanyane op cit note 10 at 33; Thabane op cit note 9 at 18; Robb op cit note 2 at 7.

⁸⁵¹ Thabane op cit note 9 at 25; National Treasury op cit note 1 at 90.

⁸⁵² Ibid; Futuregrowth op cit note 10 at 4; Kanyane op cit note 10 at 3; Thomas op cit note 9 at 450; McGregor op cit note 831 at 6; Fourie op cit note 167 at 38; Makwethu (AGSA) op cit note at 18 at 13; Thabane op cit note 9 at 6.

⁸⁵³ Ibid.

⁸⁵⁴ Thabane op cit note 9 at 6.

⁸⁵⁵ Ibid.

⁸⁵⁶ Ibid at 7.

⁸⁵⁷ Ibid.

⁸⁵⁸ Ibid.

applied, protected and enforced to counter the double agency issue. This is difficult task to perform given the complex structure of the executive, depicted in our three-tier government system which was explained in the previous chapter.⁸⁵⁹

The second issue facing SOCs is that an, arguably, complacent state and public are their predominant stakeholders.⁸⁶⁰ SOCs are the agents appointed by South Africans to care for the assets of the nation.⁸⁶¹ An SOC is therefore accountable to both the state and the public for its performance and the state and the public are under a reciprocal duty to ensure that an SOC is held accountable. However, neither the public nor the state are incentivized to watch over the interests of the SOC with the same vigilance as they would attribute to their own assets and interests.⁸⁶²

The public, as a stakeholder, should provide an oversight role for the performance of SOCs, but a complacent populace may often forget their watchdog role.⁸⁶³ Collective bodies, such as the public or the state, are not the best accountability mechanisms for SOCs as there is a presumption in a group of people that someone will hold SOCs accountable but no single party actually takes responsibility to enforce such accountability.⁸⁶⁴ There is a requirement for continuous analysis, on a multi-layered approach, for all stakeholders to ensure the actual accountability of SOCs for their performance.⁸⁶⁵ Without public outcry and activism the supervisory role of the public over the SOC is diluted.

Under this second issue, the accountability of SOCs is further exacerbated by the fact that the state is the sole shareholder.⁸⁶⁶ This removes the oversight role provided by serving the interests of multiple shareholders as opposed to just one.⁸⁶⁷ A failure to account by these SOCs is served by an environment in which corruption festers.⁸⁶⁸ A complacent state does not effectively monitor or oversee the functions and proper performance of an SOC.⁸⁶⁹ Corruption begets personal gain prompted by conflicts of interest which entails the subordination of the interests of the SOC in

⁸⁵⁹ Ljeoma op cit note 727 at 115.

⁸⁶⁰ Futuregrowth op cit note 10 at 3.

⁸⁶¹ Ibid.

⁸⁶² Thabane op cit note 9 at 24.

⁸⁶³ Futuregrowth op cit note 10 at 3; Thabane op cit note 9 at 8.

⁸⁶⁴ Ibid at 4.

⁸⁶⁵ Ibid; Robb op cit note 2 at 41.

⁸⁶⁶ Thabane op cit note 9 at 23.

⁸⁶⁷ Ibid.

⁸⁶⁸ Masuku op cit note 184 at 118.

⁸⁶⁹ Kanyane op cit note 10 at 39.

favour of the interests of those in power.⁸⁷⁰ As a result of complacency and corruption, the supervisory role of the state over the SOC is also significantly compromised.⁸⁷¹

Without a measure of enforceable accountability for SOCs they are not held to account to the state or the public for their poor performance. Arguably, the state tends to try to alleviate the negative impact caused by the poor performance of SOCs through state funding.⁸⁷² A side-effect of this short-term thinking is that it is only a temporary solution and by no means ensures the long-term sustainability and performance of SOCs.⁸⁷³

4.3 The Zondo Commission

The financial, governance and operational failures of South African SOCs have plagued media reports over the last decade.⁸⁷⁴ A series of scathing reports published by Advocate Thuli Madonsela during her seven-year tenure as Public Protector, from 2009 to 2016 highlighted the massive governance failures of SOCs, focusing on a failure by the board to discharge its statutory duties.⁸⁷⁵ Corruption, maladministration and unchecked abuses of state power, as the sole shareholder of SOCs, were also uncovered.⁸⁷⁶

The final nail in the coffin of state coffers was the last report issued by Advocate Madonsela, before her vacating of office in late 2016, which is infamously known as the State Capture Report.⁸⁷⁷ A slew of court cases followed the State Capture Report, which incriminated those in power as well as the boards of SOCs and which, following the recommendation of the Public Protector in her report, culminated in the establishment of the Zondo Commission in February 2018.⁸⁷⁸

The Zondo Commission was supposed to be established by the President, as recommended by Advocate Madonsela, within 30 days of the release of the State Capture Report on 2 November 2016.⁸⁷⁹ However, as a result of the delay caused by the state in its launching of an unsuccessful

⁸⁷⁰ Futuregrowth op cit note 10 at 6.

⁸⁷¹ Ibid at 43; Masuku op cit note 184 at 118.

⁸⁷² Thabane op cit note 9 at 25.

⁸⁷³ Futuregrowth op cit note 10 at 32.

⁸⁷⁴ Thabane op cit note 9 at 10; Thomas op cit note 9 at 450; McGregor op cit note 5; Kanyane op cit note 10.

⁸⁷⁵ Madonsela op cit note 695.

⁸⁷⁶ Ibid.

⁸⁷⁷ Madonsela op cit note 16 at 48.

⁸⁷⁸ Ibid at 353; Terms of reference op cit note 14; Constitution op cit note 11 at section 84 (2)(f).

⁸⁷⁹ Ibid at 353.

court application to review the remedial action provided in the State Capture Report, the Zondo Commission was only established on 23 January 2018.⁸⁸⁰ The Zondo Commission is a judicial commission of inquiry which is mandated to investigate allegations of state capture, corruption and fraud in the public sector, including organs of state.⁸⁸¹ The terms of reference for Zondo Commission align with the remedial action prescribed by the Public Protector in the State Capture Report.⁸⁸²

The Zondo Commission is mandated to: *'inquire into, make findings, report on and make recommendations'* in its investigation into matters of public and national interest concerning allegations of state capture, corruption and fraud, guided by the report of the Public Protector, legislation, policies and guidelines and the Constitution.⁸⁸³ SOEs are specifically referenced in relation to any improprieties in the appointments or removals of board members by the state and the unlawful awarding of tenders by SOEs as a result of a conflict of interest by the board or state.⁸⁸⁴

The investigation has brought into focus many of the operational and governance deficiencies of various SOCs, which subsequently opened the door for corruption, state capture and fraud.⁸⁸⁵ The SOCs which were highlighted under the State Capture Report, in terms of allegations relating to corruption, state capture and fraud, are subject to investigation by the Zondo Commission and these SOCs are: Eskom, Transnet, Denel, SAA and SABC.⁸⁸⁶ All of these SOCs have commercial mandates and, as Enterprises, their poor financial performance has had a far-ranging ripple effect on the economy.⁸⁸⁷

The Commission was to submit its report and make recommendations, on the basis of its investigation, to the President within 180 days of its commencement.⁸⁸⁸ The commencement date

⁸⁸⁰ *President of the Republic of South Africa v the Office of the Public Protector and Others* 2018 (2) SA 100 (GP); Terms of reference op cit note 14.

⁸⁸¹ Terms of reference op cit note 14; Constitution op cit note 11 at section 84 (2)(f).

⁸⁸² Ibid; Madonsela op cit note 16 at 353 - 5.

⁸⁸³ Ibid at ref 1.

⁸⁸⁴ Ibid.

⁸⁸⁵ Corruption Watch 'The Zondo Commission from a Corruption Watch Point of View' (2018) available at http://www.corruptionwatch.org.za/wp-content/uploads/2018/08/Zondo-Commission-overview-and-context-for-Corruption_Watch.pdf, accessed on 17 December 2019.

⁸⁸⁶ Madonsela op cit note 16 at 48; Commission of Inquiry into State Capture 'Hearings, recent' available at <http://www.statecapture.org.za/site/hearings>, accessed on 14 August 2020; Ngatane op cit note 17.

⁸⁸⁷ Ibid.

⁸⁸⁸ Terms of Reference op cit note 14 at ref 5.

of the Commission was 1 March 2018 and the first public hearing was held on 20 August 2018.⁸⁸⁹ The deadline for the submission of the report from the Zondo commission was extended by the North Gauteng High Court to 1 March 2020 and was subsequently extended again by the court to 31 March 2021.⁸⁹⁰

There were numerous concerns raised by the High Court in granting the extension as the interests of justice and the public would be best served if finality was reached by the Zondo Commission and its investigation concluded and report submitted.⁸⁹¹ As a result, the court granted this extension as a final extension for the Zondo Commission which indicates that it cannot approach the court to grant a further extension of the submission deadline of 31 March 2021.⁸⁹²

The extensions granted to the Zondo Commission serve to dilute one of its main purposes which is to act as a preventative measure in deterring future unethical and corrupt behaviour from the state and the board of an SOC and its directors. Whilst the Zondo Commission conducts its investigation, current and future boards of SOCs and members of the state are not dissuaded from similar behaviour in future.

The Public Protector and the Zondo Commission are authorised to refer any matter for prosecution, further investigation or the convening of a separate enquiry, to the appropriate law enforcement agency, government department or regulator regarding the conduct of certain persons.⁸⁹³ The tenure of Advocate Madonsela expired before she could bring any matters, identified as alleged crimes in her State Capture Report, to notice of the NPA for possible prosecution. The current Public Protector, Advocate Busisiwe Mkhwebane, has yet to bring any matters to the notice of the NPA and is accused of failing to effectively monitor the conduct of the Zondo Commission in accordance with the remedial action set out in the State Capture Report.⁸⁹⁴ Chairperson of the Zondo Commission, Deputy Chief Justice Raymond Zondo has also not referred any persons to the NPA for prosecution.

⁸⁸⁹ Commission of Inquiry into State Capture ‘Media Advisory of 18 May 2018’ available at <http://www.sastatecapture.org.za/site/files/announcements/7.pdf>, accessed on 28 August 2020.

⁸⁹⁰ *Chairperson of the Judicial Commission of Inquiry into State Capture v President of the Republic of South Africa and Others* [2020] ZAGPPHC 74.

⁸⁹¹ *Ibid* para 24 – 25.

⁸⁹² *Ibid* para 29.

⁸⁹³ Terms of Reference op cit note 14 at 8 – 9; PPA op cit note 682 at section 6 (4)(c).

⁸⁹⁴ De Vos op cit note 714.

There are no time limits prescribed for the referral of matters for prosecution to the NPA and the chairperson of the Zondo Commission or the Public Protector need not wait until submission of the report in order to make a referral. A referral would serve as an effective deterrent, as those in breach of their duties, as directors of SOCs, may be held criminally and personally liable. There are reports of a special directorate to be implemented by the NPA which will be mandated to deal with criminal prosecutions, following the evidence gathered by the Zondo Commission's investigation.⁸⁹⁵ Until there is an effective enforcement mechanism, whether retribution or reward-based, to hold recalcitrant boards and directors of SOCs to account, their dismal performance is likely to continue unabated.

4.4 SAA Case in Point

SAA is utilized as a prime illustration of the lack of accountability exhibited by the board of an SOC and its directors, despite a plethora of statutory requirements and the possibility of liability being imposed due to breaches of duties.⁸⁹⁶ This research will be conducted directly from an analysis and interpretation of the SAA Reports.⁸⁹⁷ SAA is an SOC and classified as an Enterprise and is, therefore, capable of being financially self-reliant although it has been unable to do so in the recent years due to its financial underperformance.⁸⁹⁸

SAA was chosen as the case study for this chapter primarily because, unlike other failing SOCs, such as Eskom, SAA has a non-commercial mandate which does not involve a public interest objective, such as the provision of free electricity for indigent households.⁸⁹⁹ The non-commercial mandate of SAA involves the creation of trade routes in order to facilitate trade relations with various countries.⁹⁰⁰ SAA is not tasked with the performance of a service delivery function, which would, to a certain extent, make its continued existence inevitable. The main objective of SAA is the provision of services as passenger airline and cargo transporter.⁹⁰¹ Therefore, utilising the

⁸⁹⁵ Raeesa Pather 'Special NPA unit to deal with Zondo commission evidence to be set up' *Mail & Guardian* 7 February 2019 available at <http://mg.co.za/article/2019-02-07-special-npa-unit-to-deal-with-zondo-commission-evidence-to-be-set-up> accessed on 28 August 2020.

⁸⁹⁶ Makoni op cit note 13 at 21 – 23, National Treasury op cit note 1 at 93.

⁸⁹⁷ SAA Reports op cit note 20.

⁸⁹⁸ Makoni op cit note 13 at 23.

⁸⁹⁹ Department of Minerals and Energy op cit note 30.

⁹⁰⁰ Kanyane op cit note 10 at 33.

⁹⁰¹ SAA Act op cit note 118 at section 6(1).

failures of SAA as the SOC under the spotlight paves the way for reform of SOCs with similar mandates.

The continuous systematic failures of SAA will be highlighted as a case in point for the ineffectiveness of the current retributive measures which are utilized in an attempt to hold directors of SOCs accountable.⁹⁰² As an enforcement mechanism for accountability, the available legislated, retributive measures have had little effect on the governance failures of almost all SOCs over the last decade.⁹⁰³ Plagued with internal and external accountability failures, spanning over the past 10 years, SAA finally succumbed when it entered into voluntary business rescue on 5 December 2019.⁹⁰⁴ Although certainly not the only SOC with governance and financial failures, SAA is the only SOC to date to have entered business rescue proceedings.⁹⁰⁵

4.5 Accountability Failures of SAA

The financial performance of SAA has progressively declined since as early as 2011.⁹⁰⁶ This poor financial performance has a hugely detrimental impact on the scarce national resources, as taxpayers' monies are constantly being utilized to fund the struggling airline, despite the presence of its commercial mandate.⁹⁰⁷ It is submitted that SAA's continued financial and operational failures, primarily stem from a lack of accountability exhibited by its board and directors which is exacerbated by ineffective supervision from the Minister.⁹⁰⁸ The internal and external accountability measures, allegedly implemented by the board of SAA, have, arguably, failed and the performance of the SOC continues to decline.⁹⁰⁹

⁹⁰² Kanyane op cit note 10 at 4; Thomas op cit note 460; Makoni op cit note 13 at 21; Makwethu (AGSA) op cit note 18 at 113; Thembekile Kimi Makwethu 'PFMA Consolidated General Report on National and Provincial Audit Outcomes 2017/2018' (2018) available at: <http://www.agsa.co.za/Portals/0/Reports/PFMA/201718/GR/PFMA2017-18%20Consolidated%20General%20Report.pdf>, accessed on 12 August 2020 at 119

⁹⁰³ Thomas op cit note 9 at 460.

⁹⁰⁴ SAA op cit note 18.

⁹⁰⁵ Makoni op cit note 13 at 21 – 22; Tankiso Moloi 'Assessing Corporate Governance Disclosures in South Africa's National Government Departments: the State and Corporate Governance' (2015) 17 *Southern African Journal of Accountability and Auditing Research* 1 at 3 – 4; Kanyane op cit note 10 at 30; Thomas op cit note 9 at 460.

⁹⁰⁶ Ibid; SAA reports op cit note 20.

⁹⁰⁷ National Treasury op cit note 18; Makwethu (AGSA) op cit note 902 at 117.

⁹⁰⁸ Makoni op cit note 13 at 22; Madonsela op cit note 16 at 66.

⁹⁰⁹ Ibid; National Treasury op cit note 1 at 90; SAA op cit note 18.

4.6 Internal Accountability Failures

The internal accountability mechanisms available to the board of SAA include the statutory director duties, the responsibilities of the board and committees, the supervision of the state as its sole shareholder and the functions performed by the internal audit and the company secretary.

4.6.1 The Directors

In terms of the PFMA and the Companies Act, the board of SAA and its directors are required to discharge their statutory, fiduciary duties and the duty of care and skill, taking decisions in the best interests of the SOC.⁹¹⁰ The duties of the board will be discussed in the subsequent chapter and the duties of the directors of SAA, under the Companies Act, will be initially discussed.

The conduct of many of the directors of SAA, spanning the last couple of years, has resulted in a failure of one of the core internal accountability checks for the SOC.⁹¹¹ A complete lack of corporate governance structures also contributed to the directors' inability to effectively discharge their fiduciary duties and the duty of care and skill.⁹¹² Numerous decisions, riddled with conflicts of interest, have been taken which cannot be said to have been in the best interests of the SOC.⁹¹³ A stellar example lies in the delinquency order which OUTA sought from the North Gauteng High Court under section 165 (2) of the Companies Act against former non-executive chairperson of SAA, Myeni.⁹¹⁴

OUTA sought to declare Myeni a delinquent for her conduct, during her tenure as non-executive chairperson of SAA from 2012 to 2017, claiming a gross abuse of her position as director and a breach of her duties under the PFMA which constituted criminal offences which should also be referred to the NPA for prosecution.⁹¹⁵ The court granted the order declaring Myeni a delinquent under section 162 (5)(c) of the Companies Act for grossly and intentionally abusing her position as director and breaching the duties she owed to SAA.⁹¹⁶

In addition, the court ordered that the delinquency declaration subsist against Myeni for her lifetime, that she pay the costs of the action and that the judgement and evidence led be referred to

⁹¹⁰ PFMA op cit note 11 at section 50 & 51; Companies Act op cit note 11 at section 76.

⁹¹¹ Makoni op cit note 13 at 21.

⁹¹² Moloi op cit note 905 at 1.

⁹¹³ Makoni op cit note 13 at 22; Madonsela op cit note 16 at 66.

⁹¹⁴ *OUTA v Myeni* case supra note 346 para 2 – 4.

⁹¹⁵ Ibid para 6.

⁹¹⁶ Ibid para 270 & 285.

the NPA for possible criminal prosecution.⁹¹⁷ The court sought to impose the highest possible punishment on Myeni, as a result of her actions which contributed to the inevitable downfall of SAA which, as an SOC, has a drastic impact on the economy of South Africa.⁹¹⁸ This landmark judgement serves as a precedent and warning to all directors on the boards of SOCs that they are not untouchable and that a breach of their duties will lead to severe consequences.

Notwithstanding the obvious negligent conduct of Myeni during her tenure, it is submitted that her appointment to the board of SAA, as a non-executive, independent chairperson, was heavily flawed and ultimately should never have occurred. The board of SAA has repeatedly stated its application of the King Codes in the SAA Reports.⁹¹⁹ Following the King Codes, as the chairperson, Myeni was meant to act as an independent non-executive director to ensure the objective and effective discharging of the roles and responsibilities of the directors on the board.⁹²⁰

On her appointment date in 2012 as chairperson, Myeni had already been a non-executive director on the board of SAA since 2009 and, as a result, her independence may have already been compromised.⁹²¹ Furthermore, Myeni had close links to the former President, Jacob Zuma, and served on the board of one of his foundations, the JZ Foundation (SA), at the time that she was appointed as director to the SAA board.⁹²² The potential for conflicts of interest which may arise when the chairperson is so closely linked to the state, as sole shareholder of SAA, would have been inevitable.

It is conceivable that this conflict of interest materialized as Myeni would go on to take numerous unilateral decisions, as a result of a complacent board, which were not in the best interests of SAA.⁹²³ Therefore, Myeni could not reasonably have been regarded as independent which is a crucial recommendation of the King Codes for the chairperson, as the leader of the independent, non-executive directors on the board.⁹²⁴

⁹¹⁷ Ibid para 285.

⁹¹⁸ Ibid para 267.

⁹¹⁹ SAA reports op cit note 20; 2013 report at 61; 2014 report at 2; 2015 report at 2; 2016 report at 66; 2017 report at 81.

⁹²⁰ Ibid para 35, King III op cit note 217 at principle 2.16; King IV op cit note 19 at 43 & 115.

⁹²¹ SAA report 2013 op cit note 20 at 12.

⁹²² Ibid.

⁹²³ *OUTA v Myeni* supra note 346 para 270.

⁹²⁴ King IV op cit note 19 at principle 38 at 53.

Furthermore, Myeni was appointed with no previous knowledge or experience of the role of an independent non-executive chairperson and seemingly did not receive any training on the duties she owed, in such capacity, to SAA.⁹²⁵ This lack of knowledge and experience undoubtedly compromised her ability to effectively lead the board of SAA in fulfilling its governance objectives and responsibilities.⁹²⁶ In addition to the lack of independence, Myeni was also completely unqualified to fulfil the important role of the chairperson of SAA.

The fact that SAA has no separate nominations committee to assist in the appointment of directors may also have contributed to the unsuitable appointment of Myeni, initially as an executive director and then subsequently as the chairperson of the board.⁹²⁷ The nominations committee of SAA was always established together with another committee, usually the social and ethics or governance committee.⁹²⁸ Jointly combining the important mandate of a nominations committee with that of another committee may have subverted its importance which lead to the unsuitable appointment of Myeni.

The state, as the sole shareholder of SAA, has sole discretion in the appointment of directors, and with her close ties to the former President Jacob Zuma at the time, it is arguable that Myeni's appointment to the board of SAA was due to political and personal motives rather than to benefit the composition of the board of SAA in its best interests.

The frequent turnover of the position of CEO of SAA has also provided an aspect of instability to the board.⁹²⁹ As a pivotal position on the board of directors and as one of the two executive directors, the CEO has an important role to play in the strategic management and control of the SOC.⁹³⁰ Since 2013, SAA has seen over four CEO's take the helm, a position which requires skill, experience and expertise and the constant rotation has placed strain on the rest of the board.⁹³¹ The inconsistency of the vital position of CEO, who provides a crucial link to the information around the strategic management and control of the SOC for the non-executive director also contributed

⁹²⁵ SAA report 2013 op cit note 20 at 12.

⁹²⁶ Ibid at principle 31 at 53.

⁹²⁷ SAA reports op cit note 20.

⁹²⁸ 2013 report at 63; 2014 report 84; 2015 report at 12; 2016 report at 67; 2017 report at 81.

⁹²⁹ Makoni op cit note 13 at 22.

⁹³⁰ Ibid; King IV op cit note 19 at 53 & 115.

⁹³¹ SAA Reports op cit note 20; 2013 report at 18; 2014 report at 19; 2015 report at 78; 2016 report at 87; 2017 report at 46.

to Myeni's reign of tyranny.⁹³² Unchecked by the CEO, Myeni was able to conduct the affairs of SAA as if she was its sole executive director and shareholder.⁹³³

Myeni's tenure ran over a period of nine years, commencing in 2012 and contributed to the downfall of the airline, which was profitable in 2012 and which voluntarily applied for business rescue in 2019.⁹³⁴ During Myeni's nine-year tenure, the board of directors were mere puppets who amicably agreed, by silent omissions, to her decisions, which were not taken in the best interests of SAA.⁹³⁵ As is evident from testimony given to the Zondo Commission by former CFO of SAA, Phumeza Nhantsi, Myeni was given unfettered discretion to take complete control of the board and to take unilateral, executive decisions on behalf of SAA.⁹³⁶

It is submitted that the rest of the directors who served on the board of SAA during Myeni's tenure should also have delinquency applications brought against them for a breach of their fiduciary duties in failing to take decisions for a proper purpose and with an independent mind.

Therefore, from an examination of the SAA Reports, it is submitted that the lack of accountability exhibited by the board of the SOC, in allowing Myeni to unilaterally take decisions which were not in the best interests of SAA, had a negative effect on financial performance of the SOC from 2012, when Myeni was appointed as the non-executive chairperson.

4.6.2 The Board and Committees

The composition of the board and the delegation of responsibility to management and committees are also important aspects to achieving the accountability of SOCs.

(a) The Board

The composition of the board of an SOC is an important factor in promoting accountability and enhancing performance.⁹³⁷ The composition of the board of an SOC is not regulated (save for members of the social and ethics and audit committees) and should comprise directors of an appropriate mix of knowledge, skills, experience, diversity and independence, in order to

⁹³² Makoni op cit note 13 at 22 – 23.

⁹³³ Ibid at 23.

⁹³⁴ *OUTA v Myeni* supra note 346 para 3 & 276.

⁹³⁵ Ibid para 240.

⁹³⁶ The Commission of Inquiry into State Capture 'P Nhantsi – Statement & Annexures' available at http://www.sastatecapture.org.za/site/files/documents/138/DD_2._P_Nhantsi_-_Statement_&_Annexures.pdf, accessed on 29 August 2020.

⁹³⁷ King IV op cit note 19 at principle 7 at 115.

effectively manage and control the SOC.⁹³⁸ For an SOC, the directors are appointed by the state as the sole shareholder which may do so without consultation with the board which may shroud the principles of transparency and disclosure.⁹³⁹ The state, as shareholder, may abuse its power in appointing directors due to political or personal motivations, rather than in the best interests of the SOC.⁹⁴⁰

The composition of the board of SAA makes an interesting case in point for the apparent application of the recommendations provided by the King Codes. It may appear as though SAA has applied the recommendations, alleging a description of their board composition as a majority of independent non-executive directors, over the last decade.⁹⁴¹ Following the recommendations of the King Codes, there were only two executive directors on the board of SAA, the CEO and CFO, at any given time with the rest of the board comprising non-executive directors.⁹⁴²

The value which a majority of independent, non-executive directors provides in respect of the performance of an entity has been a hotly contested issue.⁹⁴³ It is argued that a majority of independent, non-executive directors does not necessarily result in improved supervision, fewer conflicts of interest, greater accountability and overall better corporate performance.⁹⁴⁴ SAA may be evidence in support of this argument, as its board composition seemingly complied with the majority recommendation for over a decade but still managed to be placed under business rescue in 2019 and have a delinquency order granted against its former chairperson.⁹⁴⁵

However, the value of a majority of independent, non-executive directors may not have been the primary issue for SAA and there may have been other underlying factors which inevitably led to the downfall of the airline.

First, the actual independence of the non-executive directors serving on the board of SAA may have been questionable. A continual analysis of the board may have illustrated the compromised

⁹³⁸ Companies Act op cit note 11 at section 94 & 72 (4); King IV op cit note 19 at principle 7 at 115.

⁹³⁹ Shirley N Matsiliza 'Corporate Governance of the State-Owned Enterprises In an Emerging Country: Risk Management and Related Issues' (2017) 7 *Risk Governance & Control: Financial Markets & Institutions* 35 – 43 at 39; Makoni op cit note 13 at 22.

⁹⁴⁰ Matsiliza op cit note 939 at 39; Makoni op cit note 13 at 22.

⁹⁴¹ SAA reports op cit note 20; 2013 report at 62; 2014 report at 82; 2015 report at 10; 2016 report at 64; 2017 report at 80.

⁹⁴² Ibid.

⁹⁴³ Wiese op cit note 63 at 32; Bhagat op cit note 440 at 235; Olson op cit note 399 at 237.

⁹⁴⁴ Ibid.

⁹⁴⁵ SAA op cit note 18; *OUTA v Myeni* supra note 346.

independence of many of the non-executive directors serving on the board of SAA. An independent non-executive director is a director who is not involved in the day to day management of the company, is not a representative of the shareholder, has not been employed by the SOC in any executive capacity and has no contractual relationship or interest in the SOC or any of its subsidiaries.⁹⁴⁶ King IV provides a detailed assessment of the independence of a non-executive director which can be applied by the shareholder, in collaboration with the board, in the appointment of the directors.⁹⁴⁷

At the outset of the appointment of Myeni as the chairperson, her independence was conceivably compromised due to her relationship with the former President Zuma and his foundation.⁹⁴⁸ Myeni was described as a non-executive director and included, on several occasions, as one of the independent, non-executive directors.⁹⁴⁹ In the 2013 integrated report of SAA, the first mention of the independence of the board is made, which was followed by a statement that all the non-executive directors appointed to the board, by the Minister were independent.⁹⁵⁰ This amounted to a blanket claim by SAA, as opposed to an individual assessment, despite reference to the implementation of a system to determine the independence of the directors.⁹⁵¹ There were references made in the SAA Reports to declarations of conflicts of interest which are submitted annually by each director, however, the actual submission of these declarations is not certain.⁹⁵²

Independence also seems to have been evaluated solely from the point of view of conflicts of interest between directors, or their related parties and SAA or its subsidiaries.⁹⁵³ However, the test for independence for the director of an SOC should be much broader and include potential conflicts of interest that directors might have due to their relationship with the state. For these directors, the temptation to act as a puppet director of the state and not in the best interests of the SOC is, inevitable and an appointment where this conflict is even a possibility should be avoided.⁹⁵⁴ The nominations committee should have been consulted and a proper reference and analysis on each

⁹⁴⁶ Makoni op cit note 13 at 22.

⁹⁴⁷ King IV op cit note 19 at principle 7.28 at 52 & 115.

⁹⁴⁸ SAA report 2013 op cit note 20 at 12.

⁹⁴⁹ SAA 2015 report at 10, 11 & 78; 2016 report at 64; 2017 report at 80

⁹⁵⁰ SAA 2013 report at 84.

⁹⁵¹ Ibid.

⁹⁵² SAA 2013 report at 65; 2014 report at 84; 2015 report at 82; 2016 report at 90.

⁹⁵³ SAA 2013 report at 82; SAA 2016 report at 64.

⁹⁵⁴ Wiese op cit note 63 at 69.

director carried out prior to their appointment to the board. Had this been the case, the appointment of Myeni may have been circumvented as the potential for conflicts of interest were too great.

Furthermore, there was never any distinction made, in the 2015 and 2017 annual integrated reports, between the non-executive directors and the independent non-executive directors serving on the board of SAA.⁹⁵⁵ It is therefore impossible for stakeholders to ascertain which directors are meant to act independently and serve as the majority on the board. An analysis of the directors' independence, including Myeni's could never have been accurate, given that her designation varied between being described as a non-executive and an independent, non-executive director.⁹⁵⁶ The independence being the key differentiating factor and the crux of the recommendations for independent supervision on the board.⁹⁵⁷ In stark comparison, Comair Limited, specifically designated each of their independent, non-executive directors in their annual reports and provided reference to an analysis of their independence.⁹⁵⁸

Adoption of the recommended practices in King IV in analysing the independence of Myeni and the other non-executive directors by the board of SAA, may have aided in their earlier removal.⁹⁵⁹ The board of SAA would also have done well to appoint an independent, non-executive director to lead the performance appraisal of the chairperson.⁹⁶⁰ On appointment or re-appointment of non-executive directors, there is no evidence of an evaluation of their independence or reasons provided for their appointment by the shareholder.⁹⁶¹

The section dedicated to the evaluation of the board of directors in the SAA Reports also reads as a brief curriculum vitae for each director.⁹⁶² There is no analysis of independence or reasons provided for the appointment of directors to enhance board composition, as suggested and

⁹⁵⁵ SAA 2015 report op cit note 20 at 10, 11 & 78; SAA 2017 report op cit note 20 at 80; SAA 2016 report op cit note 20 at 64.

⁹⁵⁶ SAA 2013 report at 12; 2014 report at 16; 2015 report at 10; 2016 report at 16.

⁹⁵⁷ King IV op cit note 19 at 53.

⁹⁵⁸ Comair Limited '2017 Annual Integrated Report' available at: <http://www.comair.co.za/Media/Comair/files/2017/comair-annual-report-2017-final.pdf> accessed on 29 August 2020 at 80; Comair Limited '2018 Annual Integrated Report' available at <http://www.comair.co.za/Media/Comair/files/2018/comair-annual-report-2018-final.pdf>, accessed on 29 August 2020 at 60; Comair Limited '2019 Annual Integrated Report' available at <http://www.comair.co.za/Media/Comair/files/2019/annual-report/comair-annual-report-2019.pdf>, accessed on 29 August 2020 at 90.

⁹⁵⁹ King IV op cit note 19 at 52 & 53.

⁹⁶⁰ Ibid.

⁹⁶¹ SAA reports op cit note 20; 2013 report at 62; 2014 report at 82; 2015 report at 10; 2016 report at 64; 2017 report at 80.

⁹⁶² Ibid.

recommended by King IV.⁹⁶³ The SAA Reports are indicative of a mindless ‘tick-box’ approach, which King III and IV seek to avoid, to the recommendations for the independence and majority of the non-executive directors in respect of board composition.⁹⁶⁴

Secondly, staggered rotation of the directors is important to introduce new skill sets whilst retaining valuable knowledge and experience.⁹⁶⁵ Continuity of the skillset, knowledge and experience of the board is paramount to achieving its effective composition.⁹⁶⁶ Considered succession planning and continual analysis of the independence of the non-executive directors are key factors for determining board rotation.⁹⁶⁷ The rotation of the directors serving on the board of SAA can be described as anything but staggered as is evident from the SAA Reports.⁹⁶⁸ The SAA Reports show that the number of directors, executive and non-executive, which were appointed and removed every year was almost tantamount to a complete board reconstitution.⁹⁶⁹

The frequent and numerous director turnarounds for the board of SAA holistically diluted the valuable skills, knowledge and experience of the board. It is recommended that the tenure of independent, non-executive directors does not exceed a period of nine years, in order to maintain actual independence.⁹⁷⁰ However, short tenures of one or two years may also hamper the beneficial impact provided by independent directors as they have not gained sufficient knowledge and experience of the workings of the SOC and its board to effectively discharge their duties. Constant board reconstitution at major SOCs such as SAA is disruptive and should only be undertaken if absolutely necessary.⁹⁷¹ In almost all instances no explanation was provided by the board as to resignation or removal of its directors.⁹⁷²

Thirdly, a failure by the independent non-executive directors to comprehend and understand their requisite roles is likely to result in a failure to effectively discharge the duties they owe to the SOC.

⁹⁶³ Ibid.

⁹⁶⁴ Thomas op cit note 9 at 463.

⁹⁶⁵ King IV op cit note 19 at principle 7.12 at 50 & 115.

⁹⁶⁶ PWC op cit note 70.

⁹⁶⁷ Institute of Directors South Africa ‘Challenges Facing Public Sector Boards’ available at http://cdn.ymaws.com/www.iodsa.co.za/resource/collection/49D62EF3-F749-403C-BE47-73C50F27F30F/Challenges_facing_Public_Sector_Boards.pdf accessed on 29 August 2020.

⁹⁶⁸ SAA Reports op cit note 20; 2013 report at 18; 2014 report at 19; 2015 report at 78; 2016 report at 87; 2017 report at 46.

⁹⁶⁹ Ibid.

⁹⁷⁰ King IV op cit note 19 at principle 7.29 at 53.

⁹⁷¹ IODSA op cit note 967.

⁹⁷² SAA Reports op cit note 20; 2013 report at 64; 2014 report at 85; 2015 report at 78; 2016 report at 87; 2017 report at 31.

There is no distinction between the executive and non-executive directors in light of the fact that they are all required to discharge their statutory and common law duties, in the best interests of the SOC.⁹⁷³ All directors are required to act in the best interests of the SOC at all times and not to use their position to gain a personal advantage.⁹⁷⁴ In order to achieve this duty, all directors are required to take decisions with an unfettered, independent and objective mind.⁹⁷⁵ However, the manner in which these duties are effectively discharged by each director may differ, in relation to their designation as an executive or non-executive director.

Non-executive directors are required to apply their minds in discharging their duties, utilizing the information provided to them in board packs and through questions raised at the board meetings.⁹⁷⁶ Executive directors are privy to much more information as they are involved in the daily management of the business.⁹⁷⁷ Independent, non-executive directors are required to understand that their continued independence from the SOC is primary to their role on the board. They should also understand that they are to discharge the same duties as those of executive directors, with often, less information and to provide a supervisory role over the executive directors to ensure the avoidance of conflicts of interest.⁹⁷⁸

Key questions and concerns are to be raised by all directors at board meetings, especially with reference to any perceived or real conflicts of interest amongst board members, pertaining to the matter on which a decision is to be taken.⁹⁷⁹ All information should be gathered to ensure that the directors are able to discharge their duties and if non-executive directors require further information in order to make an informed decision, they should request it instead of blindly acquiescing or deferring to other directors or the shareholder, due to time constraints or political influences and motivations.⁹⁸⁰

In many instances, such as was the case with Myeni at SAA, independent, non-executive directors overstep their bounds by becoming involved in the management and control of the business of the

⁹⁷³ Cassim op cit note 63 at 478; Companies Act op cit note 11 at section 1 & 76.

⁹⁷⁴ Ibid.

⁹⁷⁵ Ibid; Deloitte 'King IV Independent directors' 2017 available at http://www2.deloitte.com/za/en/pages/africa-centre-for-corporate-governance/articles/kingiv_independent_directors.html accessed on 30 August 2020.

⁹⁷⁶ Ibid at 2.

⁹⁷⁷ Ibid at 3.

⁹⁷⁸ Ibid; PWC op cit note 70 at 4.

⁹⁷⁹ Ibid; King IV op cit note 19 at principle 6 at 49.

⁹⁸⁰ Ibid at 3; IODSA op cit note 967.

SOC.⁹⁸¹ In this instance, such directors cease to be independent from the SOC and can no longer be described as forming part of the recommended majority of the independent, non-executive directors, serving on the board. A proper independence assessment by the board of SAA, on a continual basis, would have shown that Myeni was no longer considered as an independent, non-executive chairperson as she continually took unilateral decisions to control and manage SAA which is a role to be performed by the executive directors.⁹⁸² Although the SAA Reports mention that the board conducted independence assessments of their directors, the reality depicted by the *OUTA case* is evidence to the contrary.⁹⁸³

Uninformed and untrained non-executive directors also tend to follow the vote of the majority, as was the case with Myeni, where the rest of the board became puppet directors blindly acquiescing to the tyrant chairperson.⁹⁸⁴ These ‘puppet’ directors cannot be said to be discharging their duties if they are unable to take a decision with an unfettered, independent and objective mind.⁹⁸⁵ The board of SAA should have been properly trained in respect of the duties the directors owed to the SOC in performing their respective roles as executive and non-executive directors.

The SAA Reports refer to compliance training with the PFMA but do not specifically refer to training the directors as to their roles and duties, save for the 2015 report which sets out a detailed training programme for the board which was allegedly implemented.⁹⁸⁶ Continuous training and the provision of adequate information at board meetings may have prevented a complacent SAA board who acquiesced to seemingly unilateral decisions taken by Myeni which were not in the best interests of SAA.⁹⁸⁷

Fourth, a failure to properly conduct board evaluations at least once every two years may have negatively impacted SAA’s board performance. The board’s ability to evaluate its own performance is essential to achieving accountability.⁹⁸⁸ It is argued that there is a direct correlation between the performance of the board and the performance of the SOC for which the directors

⁹⁸¹ *OUTA v Myeni* supra note 346.

⁹⁸² Ibid para 264.

⁹⁸³ Ibid; SAA Reports op cit note 20; 2013 report at 63; 2014 report at 82; 2015 report at 80; 2016 report at 89; 2017 report at 82.

⁹⁸⁴ *OUTA v Myeni* supra note 346 para 271.

⁹⁸⁵ Ibid.

⁹⁸⁶ SAA Reports op cit note 20; 2013 report at 80; 2014 report at 36; 2015 report at 14; 2015 report at 67; 2017 report at 87.

⁹⁸⁷ *OUTA v Myeni* supra note 346 para 271.

⁹⁸⁸ King IV op cit note 19 at principle 9 at 58 & 115.

provide strategic management and supervision.⁹⁸⁹ The performance of the individual directors should also be continuously assessed to ensure the effective fulfilment of their duties.⁹⁹⁰ Evaluations of the directors and the board's performance should be disclosed to the shareholder and possibly included in the annual, integrated reports to ensure transparency and accountability.

The SAA Reports differ as to the evidence of conducting director and board evaluations, some reports refer to an independent assessment by a third-party institution and other reports do not mention them at all.⁹⁹¹ Therefore, the continuity of the assessments is uncertain which was undoubtedly impacted by the constant board reconstitutions.⁹⁹² Furthermore, there is no evidence of the board evaluations in that no reasons for the appointment or removal of directors was consistently provided and there is no transparency or disclosure of the evaluations.⁹⁹³

Fifth, a board comprising of only two executive directors may be counterproductive to its performance. King IV recommends a minimum of two executive directors on the board, at least the CEO and CFO, subject to the size of the board.⁹⁹⁴ Companies which have larger boards, such as SAA, comprising on average fourteen directors, may benefit from more executive directors serving on the board in order to achieve a balanced and appropriate composition.⁹⁹⁵ By comparison, the board of Comair Limited, also with an average of fourteen directors, comprises at least four executive directors.⁹⁹⁶

Whilst King IV recommends a majority of independent-non-executive directors on the board, the board must always be cognizant of its nature and size in applying this recommendation.⁹⁹⁷ Executive directors have their place on the board and are important to convey strategy and

⁹⁸⁹ Institute of Directors South Africa 'Practice Note: Board Performance Evaluations' available at http://cdn.ymaws.com/www.iodsa.co.za/resource/collection/49D62EF3-F749-403C-BE47-73C50F27F30F/Guidance_for_Boards_-_Board_Performance_Evalua.pdf, accessed on 30 August 2020.

⁹⁹⁰ Institute of Directors South Africa 'Practice Note: Individual Directors Assessments' available at <http://www.iodsa.co.za/page/Guidancenotes.>, accessed on 20 August 2020.

⁹⁹¹ SAA Reports op cit note 20; 2013 report at 62; 2014 report at 83; 2015 report at 79; 2016 report at 65; 2017 report at 97.

⁹⁹² Ibid.

⁹⁹³ Ibid.

⁹⁹⁴ King IV op cit note 19 at principle 7.9 at 50 & 115.

⁹⁹⁵ SAA reports op cit note 20; 2013 report at 12 – 16; 2014 report at 87; 2015 report at 10; 2016 report at 87; 2017 report at 80.

⁹⁹⁶ Comair Limited op cit note 958.

⁹⁹⁷ King IV op cit note 19 at principle 7.8 at 50.

management information to the non-executive directors.⁹⁹⁸ With only two executive directors on the board, the other non-executive directors may not be able to glean all of the information that they require to take an informed decision.

It is only a majority of non-executive directors that is the appropriate recommendation and not an outright majority, such as is the case with SAA where on average above 80 per cent of the board are non-executive directors.⁹⁹⁹ It is also a current corporate trend for boards to be much smaller which may be more beneficial from a time, cost and diversity perspective.¹⁰⁰⁰ Large boards tend to be less efficient at their meetings as too many conflicting and competing minds are difficult to co-ordinate and manage to ascertain a majority resolution.¹⁰⁰¹ SAA may have benefited from a board composition comprising only a 60 per cent majority of non-executive directors and reducing the size of their board contingent.

Finally, the governance of the board is essential to realizing its maximum potential as an internal accountability measure. The board should ensure that there are requirements in place to promote high board attendance at their meetings for all directors.¹⁰⁰² For an SOC such as SAA it is imperative that attendance at board meetings remains high, so that all of the directors are afforded the best opportunity to effectively discharge their duties. Directors who attend very few of the stipulated board meetings cannot be said to be abreast of the business operations of the SOC.

The SAA Reports show that on average the board of SAA only achieved an attendance of 57 per cent per annum.¹⁰⁰³ In comparison, Comair Limited maintained an average 76 per cent board attendance per annum over relatively the same period.¹⁰⁰⁴ The dismal level of board attendance at SAA may be directly related to the high turnover of directors over the last couple of years.

The average number of board meetings during the year should also be realistic, given the size of the board. The SAA Reports illustrate that the board held on average ten meetings a year in

⁹⁹⁸ Institute of Directors South Africa ‘Practice Note: Board Composition’ available at http://cdn.ymaws.com/www.iodsa.co.za/resource/collection/49D62EF3-F749-403C-BE47-73C50F27F30F/General_Guidance_Note_on_Board_Composition.pdf, accessed on 30 August 2020.

⁹⁹⁹ SAA reports op cit note 20; 2013 report at 12 – 16; 2014 report at 87; 2015 report at 10; 2016 report at 87; 2017 report at 80.

¹⁰⁰⁰ IODSA op cit note 1029.

¹⁰⁰¹ Ibid.

¹⁰⁰² King IV op cit note 19 at principle 6 at 49.

¹⁰⁰³ SAA Reports op cit note 20; 2013 report at 64; 2014 report at 85; 2015 report at 81; 2016 report at 90; 2017 report at 83.

¹⁰⁰⁴ Comair Limited op cit note 958; 2017 report at 80, 2018 report at 86; 2019 report at 94.

comparison to Comair Limited's four.¹⁰⁰⁵ The high number of board meetings held by SAA may have set an unrealistic expectation for board attendance given its average of fourteen directors.¹⁰⁰⁶ Fewer scheduled board meetings for SAA may have been more realistic and prevented an unnecessary expenditure of time, money and resources from holding too many poorly attended meetings.

It is submitted that the SAA Reports display a perceived implementation of corporate governance structures recommended by the King Codes for SAA's board composition.¹⁰⁰⁷ The SAA Reports mention implementation of the apparent governance structures which are applied by the board and a governance committee which is amalgamated with the social and ethics and nominations committee.¹⁰⁰⁸ There is reference to a '*full governance report*' in the 2017 integrated report for SAA however, no such report has been published.¹⁰⁰⁹

(b) *The Committees*

The board is able to delegate any of its responsibilities to a committee, to be executed on its behalf, in accordance with its terms of reference.¹⁰¹⁰ Delegation of a responsibility by the board to a committee does not result in an abdication of the accountability for the execution of that responsibility by the board.¹⁰¹¹ The board always remains accountable for the execution of its responsibilities, whether delegated to a committee or not. The line of communication between the board and its various committees should be direct, open and clear and effective reporting and disclosure mechanisms implemented, in order to achieve meaningful collaboration.¹⁰¹²

For SAA, the establishment of certain committees and the composition of its members is mandated by legislation. SOCs are required to establish an audit committee and a social and ethics committee, each of which is delegated mandatory responsibilities to execute.¹⁰¹³ SAA has complied with the mandatory establishment of these committees as well as the establishment of the following committees: a governance and nominations committee, a financial risk and

¹⁰⁰⁵Ibid; SAA Reports op cit note 995.

¹⁰⁰⁶ Ibid.

¹⁰⁰⁷ SAA Reports op cit note 20; 2013 report at 10; 2014 report at 46; 2015 report at 32; 2016 report at 64; 2017 report at 28.

¹⁰⁰⁸ Ibid.

¹⁰⁰⁹ Ibid 2017 report at 32.

¹⁰¹⁰ King IV op cit note 19 at principle 8.41 & 42 at 54.

¹⁰¹¹ Ibid at principle 8.49 at 55.

¹⁰¹² King IV op cit note 19 at principle 8 at 50.

¹⁰¹³ Companies Act op cit note 11 at section 90, 84 (4)(c) & 72 (4) read with regulation 43 (1).

investment committee, a remuneration and human resources committee, a long-term turnaround strategy committee and a procurement and tender processes committee.¹⁰¹⁴ In addition to these portfolio committees, ad hoc committees for specialized litigation matters and stakeholder management have also been established.¹⁰¹⁵

In order to effectively execute their delegated responsibilities, the composition of the committee must be carefully established, often in accordance with statutory prescripts, and the terms of reference must be clear, in writing and enforceable.¹⁰¹⁶ The performance of each committee should also be evaluated by the board, on a regular basis, in order to enforce execution of their mandated roles and responsibilities.¹⁰¹⁷ The number of board committees should be dependent on the size of the board, having regard to the nature of the business. Too many or too few a number of committees may be counterproductive to their goal to executive responsibilities on behalf of the board.

For SAA, a nominations committee which assists the board and shareholder in the appointment of its directors should have been a mandatory establishment. As the sole shareholder, the state, through the Minister, can wield extensive power over the appointment of directors to the board of an SOC.¹⁰¹⁸ Directors may be appointed who are not suitably qualified, compromised by conflicting interests or who do not possess the necessary skill, knowledge and expertise to effectively discharge their duties.¹⁰¹⁹ The appointment of directors through a unilateral decision of the shareholder, without consultation or collaboration with the board or its nominations committee may, be one of the greatest contributors to the demise of SAA, as is illustrated by the *OUTA v Myeni* case.¹⁰²⁰

SAA had a separate governance and nominations committee until 2012 when it was subsumed under the establishment of the mandatory social and ethics committee.¹⁰²¹ Under the auspices of the mandatory committee, the nominations committee played a secondary role. The mandatory social and ethics committee is required to comply with legislated responsibilities and as a result the role of the governance and nominations committee may be completely overshadowed. This is

¹⁰¹⁴ SAA Reports op cit note 20; 2013 report at 36; 2014 report at 82; 2015 report at 12 – 13; 2016 report at 64; 2017 report at 81.

¹⁰¹⁵ Ibid.

¹⁰¹⁶ King IV op cit note 19 at principle 8.39, 41, 42, 43 & 44.

¹⁰¹⁷ Ibid at principle 9.71 at 58.

¹⁰¹⁸ IODSA op cit note 967 at 5.

¹⁰¹⁹ Ibid.

¹⁰²⁰ *OUTA v Myeni* supra note 346.

¹⁰²¹ SAA 2013 report op cit note 20 at 36.

illustrated by the dismal appointment of Myeni, with little or no requisite skills, knowledge or experience which has also resulted in the high turnover rate of the board since 2013.¹⁰²² Without a competent and defined nominations committee in place, it is submitted that the state, as sole shareholder, was able to exercise unchecked power in appointing unsuitable directors to the board of SAA.

The constant dissolution and reconstitution of many of the committees of SAA may have caused instability with respect to the board's ability to effectively execute its delegated responsibilities.¹⁰²³ There were also a large number of committees and in 2015 there were six committees with only thirteen directors.¹⁰²⁴ With a recommended minimum of three members per committee, this resulted in the same directors sitting on numerous committees.¹⁰²⁵ Given the nature of each committee's terms of reference, the number of members and their capacities should be carefully considered by the board prior to establishing a committee.¹⁰²⁶

Ad Hoc committees established to assist with litigation against SAA's CEO and to improve stakeholder relations may have been an unnecessary expenditure of resources, given the numerous portfolio committees which were already in existence at the time.¹⁰²⁷ Board committees, when utilized effectively, serve an important purpose by unburdening the board of its numerous tasks and responsibilities. However, the committees should not be seen by the board as an escape hatch from the accountability of their responsibilities and duties to SAA.

4.6.3 The Shareholder

International corporate trends have seen an increase in the oversight role which shareholders can have over an entity.¹⁰²⁸ Whilst there are differing views as to the benefits of shareholder activism on the performance of the entity, the argument is almost moot when it comes to SOCs.¹⁰²⁹

¹⁰²² SAA Reports op cit note 20; 2013 report at 62; 2014 report at 83; 2015 report at 79; 2016 report at 65; 2017 report at 97.

¹⁰²³ SAA Reports op cit note 20; 2013 report at 36; 2014 report at 82; 2015 report at 12 – 13; 2016 report at 64; 2017 report at 81.

¹⁰²⁴ SAA Report 2015 at 12 – 13.

¹⁰²⁵ Ibid.

¹⁰²⁶ IODSA op cit note 967 at 5.

¹⁰²⁷ SAA reports op cit note 1054.

¹⁰²⁸ Wiese op cit note 63 at 104; Christopher Wood 'Shareholder Activism' Part 1: Steinhoff: Red-flagging the business mode' *Prudential Insights* 2018 available at http://prudential.co.za/media/31260/steinhoff_shareholder-activism.pdf, accessed on 31 August 2020.

¹⁰²⁹ Wiese op cit note 63 at 106; King IV op cit note 19 at 117.

For most SOCs, the state is the sole shareholder and, therefore, the impact of shareholder activism as an oversight mechanism for the performance of the board is diluted, if not redundant.¹⁰³⁰ King IV goes so far as to state that the principles surrounding the responsibilities of institutional investors and the corresponding recommended practices are not applicable to SOEs.¹⁰³¹ As discussed in the preceding chapter, a complacent and corrupt state, as the sole shareholder for an SOC, may be less incentivized to engage in shareholder activism than shareholders of private or public companies who expect a growth in their investment.

Over the last decade numerous allegations of fraud and corruption at SAA have indicated a lack of accountability by the board or sufficient, if any, supervision over the board by the state, as its sole shareholder.¹⁰³² Alleged mismanagement of resources and wasteful expenditure from SAA are particularly concerning, given its status as a major public entity.¹⁰³³ Political interference and governance transgressions at board level indicate that the shareholder is actually hampering the performance of the SOC, as opposed to providing effective monitoring and oversight.¹⁰³⁴ The failure of such an imperative internal accountability measure left the SOC vulnerable to an abuse of power from the state and a failure by the board of SAA to actually implement effective corporate governance structures may have compounded the issue.¹⁰³⁵

A distinct lack of communication between the board and the state resulted in increased operational and financial failures at SAA.¹⁰³⁶ The SAA Reports should have been sufficiently detailed and accurate to allow all the stakeholders to make informed assessments regarding the SOC's performance and its sustainability prospects.¹⁰³⁷ There should also have been detailed and constant communication between the board of SAA and the state, in terms of a continual analysis of the SOCs performance in the form of annual shareholder compacts.¹⁰³⁸

The SAA Reports set out the annual key performance indicators, drawn from the shareholder compacts, which were to be achieved by the board and brief reasons are provided for the indicators

¹⁰³⁰ Makoni op cit note 13 at 23.

¹⁰³¹ King IV op cit note 19 at 117.

¹⁰³² Thomas op cit note 9 at 464; Madonsela op cit note 16 at 66.

¹⁰³³ Ibid at 465.

¹⁰³⁴ Ibid at 463; Makoni op cit note 13 at 23.

¹⁰³⁵ SAA Reports op cit note 20; 2013 report at 10; 2014 report at 46; 2015 report at 32; 2016 report at 64; 2017 report at 28; Madonsela op cit note 16 at 67.

¹⁰³⁶ Thomas op cit note 9 at 463; *OUTA v Myeni* supra note 346 at 254.

¹⁰³⁷ King IV op cit note 19 principle 5 at 48 & 113 & principle 16 at 117.

¹⁰³⁸ Ibid at principle 16 at 117.

which were not achieved.¹⁰³⁹ The 2015 and 2017 annual integrated reports, however, do not depict reasons for all of the key performance indicators which were not achieved by the board.¹⁰⁴⁰ The SAA Reports provide no indication as to the repercussions or consequences for the board failing to achieve any of the indicators.¹⁰⁴¹

Therefore, there appears to be no enforcement mechanism implemented by the state, to whom the board of SAA is meant to account, for failing to achieve any of the key performance indicators. Whether by retribution or reward, accountability needs to be enforced, in order for it to be actually achieved by the board. In its shareholder compact, the state should set out the enforcement mechanism which it intends on utilising in the event of a failure to fulfil any of the key performance indicators by the board. Reasons for failing to fulfil the indicators does not absolve the board of SAA of its accountability for the SOC's performance. Unfortunately, shareholder compacts for SAA, although referred to as being concluded annually between the board and the state, were never made publicly available.¹⁰⁴²

From an analysis of the SAA Reports, and the 2011 and 2012 annual integrated reports, interesting conclusions regarding SAA's performance and the accountability of the board and the reciprocal duty on the state, as sole shareholder, to hold the board accountable, can be surmised. Despite having suffered net profit losses in 2007 and 2008, SAA brought itself back to profit making status in 2009, which continued until 2011.¹⁰⁴³

As illustrated in the 2012 annual report, the performance of SAA plummeted when the targeted retained earnings underperformed by a massive 303 per cent, with a target profit of R460 million and an actual stated loss of R935 million.¹⁰⁴⁴ It is now evident that the 2011 annual report was the last time SAA would should an annual profit as the record losses experienced by SAA continued

¹⁰³⁹ SAA reports op cit note 20; 2013 report at 59; 2014 report at 80; 2015 report at 77; 2016 report at 84; 2017 report at 97.

¹⁰⁴⁰ Ibid 2015 report at 77, 2017 report at 97.

¹⁰⁴¹ SAA Reports op cit note 1039.

¹⁰⁴² Ibid; 2013 report at 58; 2014 report at 10; 2015 report at 76; 2016 report at 28; 2017 report at 5.

¹⁰⁴³ South African Airways SOC Limited '2011 Annual Report' (2012) available at <http://www.flysaa.com/documents/51855150/51859528/SAA+Annual+Report+2011.pdf/5f682859-71ae-4520-9340-7bf1dc762510> accessed on 31 August 2020 at 68.

¹⁰⁴⁴ South African Airways SOC Limited '2012 Annual Report' (2013) available at <http://www.flysaa.com/documents/51855150/51859528/SAA+Annual+Report+2012.pdf/d6f0665d-e76a-4125-a417-b0b6fee98ba9>, accessed on 31 August 2020 at 53.

until their last published report for the 2017 financial year-end, which set a record loss for the airline at a monumental amount of R5, 569 million.¹⁰⁴⁵

Due to the significant discrepancy in the targeted earnings and the actual earnings of SAA in the 2012 annual report, it is submitted that the state, as its sole shareholder should have been extremely concerned. As is the case with private companies, the shareholder should have raised queries and concerns to the management of SAA and demanded reasons for the inaccuracies and discrepancies within the annual report and the overall poor performance of the airline.¹⁰⁴⁶ Austerity measures should have been set in place and the state should have exercised stringent supervision over SAA, in order to return the airline to profit-making status.

The continual annual losses should have been especially alarming given the status of SAA as an SOC and a major public entity which may have to rely on taxpayer monies for its future funding.¹⁰⁴⁷ However, the 2014 and 2015 annual reports show that there was a significant increase in the salaries of the non-executive chairperson and the CEO, despite the airline's continued reported loss of R2 590 million and R5 619 million, respectively.¹⁰⁴⁸ The chairperson's salary increased by 64 per cent in 2014 while the CFO's by 20 per cent in 2015, according to the annual reports.¹⁰⁴⁹ The report also illustrated contradictions where it stated that no performance bonuses were paid to board members, however, the acting CEO, received a performance bonus of approximately R2,8million.¹⁰⁵⁰

From an examination of the SAA Reports, it appears that, despite reporting significant annual losses, the remuneration of the executive directors increased.¹⁰⁵¹ Signing bonuses, performance bonuses or gratuities, arguably described as 'variable pay' from the 2015 report onwards, were paid to executive directors and housing allowances and travel benefits continued to increase, overall.¹⁰⁵² The King Codes promote a correlation between performance and remuneration as well as shareholder approval of remuneration every two years and a reasoned, transparent and disclosed

¹⁰⁴⁵ SAA 2017 report op cit note 20 at 97.

¹⁰⁴⁶ Ibid at 353.

¹⁰⁴⁷ Makoni op cit note 13 at 22.

¹⁰⁴⁸ SAA 2015 report op cit note 20 at 88.

¹⁰⁴⁹ Ibid at 130; SAA 2014 report op cit note 10 at 131.

¹⁰⁵⁰ Ibid 2014 report at 84 & 146

¹⁰⁵¹ SAA Reports op cit note 20; 2013 report at 124; 2014 report at 146, 2015 report at 130 & 143, 2016 report at 163, 2017 report at 165.

¹⁰⁵² Ibid.

remuneration process.¹⁰⁵³ Despite the presence of a remuneration committee, it cannot be reasonably deduced from the SAA Reports that there was in fact a correlation between the performance of the SOC and the remuneration of its board of directors.¹⁰⁵⁴

The state, as shareholder, cannot have been said to have effectively supervised the board of SAA during this tumultuous period.¹⁰⁵⁵ An examination of the SAA Reports showcased glaring discrepancies and concerns which should have been monitored and corrected by the state.¹⁰⁵⁶ It is submitted that the SAA Reports illustrate an example of a mindless compliance with statutory requirements and a ‘tick box’ method of applying the recommended practices in the King Codes.¹⁰⁵⁷ The SAA Reports depict lengthy extracts which are mirrored, or copied verbatim, year on year and which may, therefore, not be a true or accurate reflection of the annual performance of SAA.

Therefore, it can be surmised that the SAA Reports depict a lack of accountability from the board and a failure in the state’s reciprocal duty to hold the board accountable every year for the dismal financial performance of the SOC. Any mechanisms which the state used to supervise the performance of the SAA board were largely theoretical in nature and presumably a meagre attempt to show compliance with the PFMA.¹⁰⁵⁸

The establishment and review of shareholder compacts, board evaluation systems, independence tests, conflicts of interest declarations and a committee for long-term turnaround strategy were all internal accountability checks, alleged to have been performed by the state, mostly through the annual shareholder compacts.¹⁰⁵⁹ However, the minutes from the committee’s meetings, its terms of reference and the documentation concerning the shareholder compacts, declarations, tests, evaluations and systems were never published by SAA or the state. Due to the business rescue proceedings initiated by SAA in 2019, it may be argued that these mechanisms remained theoretical in nature and that their actual implementation was never achieved.

¹⁰⁵³ King IV op cit note 19 at principle 14 at 64 – 6 & 116.

¹⁰⁵⁴ SAA Reports op cit note 20; 2013 report at 124; 2014 report at 146, 2015 report at 130 & 143, 2016 report at 163, 2017 report at 165.

¹⁰⁵⁵ Matsiliza op cit note 939 at 40.

¹⁰⁵⁶ Ibid at 42; SAA Reports op cit note 20.

¹⁰⁵⁷ Ibid; Thomas op cit note 9 at 464.

¹⁰⁵⁸ PFMA op cit note 11 at section 49 & 65.

¹⁰⁵⁹ SAA reports op cit note 20; 2013 report at 58; 2014 report at 10; 2015 report at 76; 2016 report at 28; 2017 report at 5.

Once the state's shareholder supervision of an SOC fails as an internal accountability check on its performance, an inevitable downfall begins.¹⁰⁶⁰ The failure of the state, as shareholder, to effectively supervise and oversee the performance of the board of SAA was, arguably, its greatest internal accountability failure which had disastrous repercussions for the airline and the economy at large.¹⁰⁶¹

The uniqueness of this accountability failure of the state, as the sole shareholder of an SOC, was also highlighted in the case involving SABC.¹⁰⁶² The Supreme Court of Appeal recognized that, as absurd as it appears, there need to be checks and balances in place for instances where the state, as supervisor, is unable to effectively supervise the performance of a failing SOC.¹⁰⁶³ As a result of the wide powers given to the state, especially in its ability to solely appoint and remove directors to and from the board of an SOC, the political influences and motivations of the state may likely traverse into the decisions taken by the board and the best interests of the SOC are subverted.¹⁰⁶⁴

Although the state, as shareholder, does not owe fiduciary duties or the duty of care and skill to act in the best interests of the SOC, the state, as the executive, is held constitutionally accountable for the performance of its duties and responsibilities.¹⁰⁶⁵ The PFMA also requires that the board be held accountable and that the executive hold the board accountable for compliance with its provisions.¹⁰⁶⁶ Therefore, the supervision of an SOC, such as SAA, forms part of the constitutional and statutory duties of the state and any failures to discharge these duties may result in a breach by the state of its constitutional obligation.¹⁰⁶⁷

Despite constitutional accountability obligations corruption is always a risk, especially in a developing country.¹⁰⁶⁸ In the premise, there should be an effective and efficient enforcement mechanism available to ensure that the state, specifically the Minister, abides by his or her statutory and constitutional duties.¹⁰⁶⁹

¹⁰⁶⁰ Thabane op cit note 9 at 28; Kanyane op cit note 10 at 38.

¹⁰⁶¹ Matsiliza op cit note 939 at 40; Makoni op cit note 13 at 23.

¹⁰⁶² SABC case supra note 167 at 3; Ibid at 39.

¹⁰⁶³ Ibid.

¹⁰⁶⁴ Ibid para 117; Futuregrowth op cit note 10 at 19; Matzilisa op cit note 939 at 39.

¹⁰⁶⁵ Wiese op cit note 63 at 106; Constitution op cit note 11 at section 92 (2).

¹⁰⁶⁶ PFMA op cit note 11 at section 49 & 65.

¹⁰⁶⁷ Constitution op cit note 11 at section 92 (2).

¹⁰⁶⁸ Kanyane op cit note 10 at 30.

¹⁰⁶⁹ SABC case supra note 167 at 4.

4.6.4 Internal Controls: The Internal Audit and Company Secretary

Subsequent to the internal check provided by the state, as shareholder of the SOC, the internal audit and the company secretary are the next internal accountability mechanisms for SOCs.

(a) *The Internal Audit*

Given their utilisation of taxpayer monies SOCs should continuously seek to improve the effectiveness of risk management strategies, incorporated through the roles played by the internal audit function and the audit committee.¹⁰⁷⁰ It is the responsibility of the state, as the executive authority of an SOC, to ensure that the board complies with the statutory requirements set out by the PFMA.¹⁰⁷¹ However, the implementation of the internal audit by the audit committee as an accountability check for SOCs appears largely unenforceable, despite statutory retributive measures.¹⁰⁷² Certainly for the board of SAA a failure to submit the last two financial year-end statements for the 2018 and 2019 years has yet to result in the levying of any punishment on the board.¹⁰⁷³

Whilst statutory and, therefore, regulatory in nature, a failure by the board of an SOC to effectively carry out continuous internal audits and to set out an internal audit strategy plan for future financial and risk management, seems to have been met with little retribution.¹⁰⁷⁴ Without an enforceable mechanism for ensuring compliance with regulatory requirements, their mandatory nature is compromised and the requirements become more like guidelines which are voluntary in nature. This is evident from the annual report given by Auditor-General which illustrates SOE compliance with the PFMA and outlines the deteriorating state of the internal controls displayed by all SOEs across the board, with none of them receiving clean audits for the 2018 financial year-end.¹⁰⁷⁵

The Auditor-General, as the external auditor for many SOCs, has stated on numerous occasions when conducting the audit of SOCs, including SAA, that the implementation of an effective

¹⁰⁷⁰ Radasi, P ‘Internal Audit in State-Owned Enterprises: Perceptions, expectations and challenges’ (2015) 17 *South African Journal of Accountability and Auditing Research* 95 at 96 – 104.

¹⁰⁷¹ *Ibid* at section 63 (2).

¹⁰⁷² Thomas op cit note 9 at 458.

¹⁰⁷³ Makwethu (AGSA) op cit note 18 at 120.

¹⁰⁷⁴ Thomas op cit note 9 at 458; Makwethu (AGSA) op cit note 902 at 118 & 120.

¹⁰⁷⁵ Makwethu (AGSA) op cit note 18 at 114.

internal audit seems to be lacking.¹⁰⁷⁶ Whilst the internal audit function is mentioned in the SAA Reports it is impossible to ascertain whether or not the audit was actually carried out by the audit committee.¹⁰⁷⁷ From statements passed by the Auditor-General, for the years during which he carried out the external audit of SAA, it would appear that the internal audit was not actually carried out by the audit committee.¹⁰⁷⁸ The board of SAA may have been more concerned with the external audit, which was carried out religiously every year by allegedly independent auditors until 2017 when the Auditor-General carried out his first external audit of the flailing airline.¹⁰⁷⁹

The independent external auditors for SAA stated, in their reports attached to the SAA Reports, that there were no sufficiently significant deficiencies identified in the internal controls which were to be included such report.¹⁰⁸⁰ This was the official line of the external auditors of SAA from the financial year-ends from 2013 to 2016.¹⁰⁸¹ For the 2017 financial year-end, the external auditor of SAA was the Auditor-General who uncovered numerous deficiencies in the internal controls and a lack of financial and risk management.¹⁰⁸² It is surprising that the independent auditors, prior to the Auditor-General, did not uncover similar internal control deficiencies by the board of SAA, and its audit committee, in their financial and risk management analysis.

For the 2017 and 2018 financial year-ends SAA has failed to provide annual financial statements for auditing and review purposes.¹⁰⁸³ Therefore, any repercussions for board or the independent auditors, as a result of the deficiencies uncovered by the Auditor-General in 2017, are yet to be ascertained. The investigation into the board of SAA and its independent auditors, during the disastrous period from 2013 to 2017, may fall under the scope of the Zondo Commission. It is unquestionable that certain repercussions should be enforced against those found to have breached their statutory duties as directors of SAA during that period, as well as possibly against joint

¹⁰⁷⁶ Ibid; Makwethu (AGSA) op cit note 902 at 9; Thembekile Kimi Makwethu 'PFMA Consolidated General Report on National and Provincial Audit Outcomes 2016-2017' (2017) Auditor-General South Africa available at <http://www.agsa.co.za/Portals/0/Reports/PFMA/201617/GR/AG%20PFMA%202017%20Web%20SMALL.pdf>, accessed on 12 August 2020 at 12.

¹⁰⁷⁷ SAA Reports op cit note 20; 2013 report at 37; 2014 report at 9; 2015 report at 13; 2016 report at 63; 2017 report at 86.

¹⁰⁷⁸ Makwethu (AGSA) op cit note 902 at 119; Makwethu (AGSA) op cit note 18 at 125.

¹⁰⁷⁹ Makwethu (AGSA) op cit note 1027 at 21.

¹⁰⁸⁰ SAA Reports op cit note 20; 2013 report at 91; 2014 report at 69; 2015 report at 87; 2016 report at 93.

¹⁰⁸¹ Ibid.

¹⁰⁸² SAA 2017 report at 103.

¹⁰⁸³ Makwethu op cit note 18 at 125.

independent auditors, who failed to actively engage with obvious internal control deficiencies, exhibited by the board and audit committee of SAA from 2013 to 2017.

It is arguable that a failure by the board of SAA to implement an effective an internal audit led to the financial and operational downfall of the airline from 2013 and contributed to the dire lack of accountability for its performance. There have been no retributive measures implemented against directors who served on the board of SAA, for the 2013 to 2017 financial year-ends.

(b) *The Company Secretary*

SOCs are required to comply with the enhanced accountability and transparency requirements contained in the Companies Act.¹⁰⁸⁴ Unless exempted by the Minister, an SOC is required to appoint a company secretary, in accordance with the provisions of the Act.¹⁰⁸⁵ The board is required to appoint a company secretary for the SOC who has the requisite knowledge and experience to effectively comply with its statutory duties.¹⁰⁸⁶

For an SOC, the independent guidance provided by the company secretary may assist in negating possible abuses of power by the state, in its appointment and removal of board members.¹⁰⁸⁷ By consulting with the board and receiving guidance from the company secretary, the state can be steered into making director appointments which complement the board composition of the SOC and which will ultimately serve the best interests of the SOC.¹⁰⁸⁸ Informed, trained and educated directors are an asset to the board on which they serve which will ultimately be in the best interests of the SOC. Directors who are appointed without the requisite capacity, skill, knowledge or experience to effectively discharge their duties are burdensome and may actually hinder the performance of the SOC.

Directors who are unable to discharge their duties due to a lack of knowledge and information may well become puppet directors who blindly follow instructions given by other directors.¹⁰⁸⁹ This seemed to be the case with the entire board of SAA with former chairperson Myeni who unilaterally concluded transactions which were not in the best interests of the SOC.¹⁰⁹⁰ The

¹⁰⁸⁴ Companies Act op cit note 11 at ch 3 & section 84 (1)(b).

¹⁰⁸⁵ Ibid at section 86 & 87.

¹⁰⁸⁶ Ibid at section 88.

¹⁰⁸⁷ Matsiliza op cit note 939 at 42.

¹⁰⁸⁸ King IV op cit note 19 at 116.

¹⁰⁸⁹ *OUTA v Myeni* supra note 346.

¹⁰⁹⁰ Ibid para 276.

inability of the SAA board to effectively implement accountability mechanisms should be regarded as a collective breach of their duties and not only a breach by an individual chairperson.

The excuse of uninformed directors who act as puppets for the dominant chairperson and acquiesce to decision by omission cannot be justifiable.¹⁰⁹¹ Especially, in the context of SAA who had appointed a company secretary who was meant to be training, informing and guiding directors, as to the effective performance of their duties.¹⁰⁹² It is alleged in the SAA Reports that all directors had independent and separate access to the company secretary at all times.¹⁰⁹³ If this was in fact the case then there may have been three possible issues which could have contributed to the ineffectiveness of the board.

First, the company secretary was not adequately skilled, knowledgeable or competent to give advice when directors requested guidance on their duties. Secondly, the directors did not approach the company secretary for assistance or guidance and no mandatory training programmes were implemented on their induction to the board. Thirdly, the company secretary was approached by the directors for training and guidance, which was given, only for the director to ignore it or fail to put any such advice into practice.

The board of SAA should, therefore, have been held responsible in the event of the appointment of a company secretary for an SOC who was not adequately skilled, knowledgeable or experienced to effectively perform his or her duties.

4.7 External Accountability Failures

The external accountability mechanisms available to the board of SAA include: the external audit, the role of the Auditor-General and Public Protector, the executive, legislature and judiciary and the public. Following a failure of many of the internal measures, it would appear that these external measures did not significantly improved the accountability of the board of SAA or the Minister.

4.7.1 The External Audit

The external audit of an SOC is one of the paramount external accountability checks on the performance of the SOC and its board of directors.¹⁰⁹⁴ There is a plethora of rules and regulations

¹⁰⁹¹ Ibid para 267.

¹⁰⁹² SAA Reports op cit note 20; 2013 report at 62; 2014 report at 82; 2015 report at 14; 2016 report at 66; 2017 at 80.

¹⁰⁹³ Ibid.

¹⁰⁹⁴ Makwethu (AGSA) op cit note 18 at 4.

which govern the mandatory audit for all SOCs.¹⁰⁹⁵ It remains the responsibility of the board of the SOC, particularly its audit committee, to ensure compliance with statutory provisions pertaining to the mandatory, annual audit of the SOC.¹⁰⁹⁶

The SAA Reports show that an external auditor was appointed and considered independent by the board for every financial year up until 2017 when the Auditor-General elected to conduct the external audit.¹⁰⁹⁷ PricewaterhouseCoopers Inc and Nonki Inc were the joint external auditors for SAA, in terms of the 2013 to 2016 annual integrated reports.¹⁰⁹⁸ These joint auditors were in their fourth consecutive year of auditing SAA and the 2017 financial year-end should have been their last year to conduct the audit in accordance with the statutory five year rotation set by the Companies Act.¹⁰⁹⁹

The external auditors did not identify any material non-compliance with key legislation or any significant deficiencies in the internal control for inclusion in their report on the annual financial statements for SAA from 2013 to 2016 financial year-ends.¹¹⁰⁰ The Auditor-General identified numerous non-compliance issues and significant deficiencies in the internal controls for SAA for inclusion in their report on the annual financial statements for the 2017 financial year-end.¹¹⁰¹ Receiving clean audits for four years prior to the qualified audit opinion provided by the Auditor-General led to the Zondo Commission investigating the role played by joint external auditors, PricewaterhouseCoopers Inc and Nonki Inc, in the financial and operational demise of SAA.¹¹⁰²

SAA failed to submit annual integrated reports for their 2018 and 2019 financial year-ends and have since gone into business rescue.¹¹⁰³ Therefore, any further analysis into the external audit function of SAA is not possible. A brief summary of the results of the external audits conducted by the Auditor-General of other similar SOCs will be provided for the 2018 and 2019 financial year-ends.

¹⁰⁹⁵ Companies Act op cit note 11 at sections 90 -4; PAA op cit note 595; APA op cit note 591.

¹⁰⁹⁶ Ibid at section 94 (7); PFMA at 51 (1)(d) & (f).

¹⁰⁹⁷ SAA Reports op cit note 20; 2013 report at 65; 2014 report at 86; 2015 report at 82; 2016 report at 68; 2017 report at 86.

¹⁰⁹⁸ Ibid 2013 report at 65; 2014 report at 86; 2015 report at 82; 2016 report at 68.

¹⁰⁹⁹ Companies Act op cit note 11 at section 92 (2).

¹¹⁰⁰ SAA Reports op cit note 20; 2013 report at 69; 2014 report at 91; 2015 report at 87; 2016 report at 93.

¹¹⁰¹ SAA 2017 report at 102 – 104.

¹¹⁰² Ngatane op cit note 17.

¹¹⁰³ Makwethu (AGSA) op cit note 18 at 41.

In an effort to curb the recent increase in the excessive amounts of fruitless and wasteful expenditure by SOCs, there are newly legislated enforceability mechanisms.¹¹⁰⁴ The board of an SOC which fails to implement remedial action, stipulated by the Auditor-General to recover certain debt of the SOC caused by fruitless, wasteful and irregular expenditure, may be held jointly and severally liable for such debt.¹¹⁰⁵

This newly legislated accountability mechanism is still in the early phases of being implemented by the Auditor-General in respect of material irregularities which were reported during the audit process for various SOCs for the 2019 financial year-end.¹¹⁰⁶ Whilst there have been positive responses to the amended provisions, with boards taking immediate steps to address reported irregularities, the full impact of the amendments has yet to be realised.¹¹⁰⁷

Despite such stringently legislated, retributive provisions to curb the inadequate financial management of SOCs, the external audits conducted by the Auditor-General illustrate a drastic increase in the number of non-compliant SOCs over the last couple of years.¹¹⁰⁸ The Auditor-General identified three root causes which may have contributed to the deteriorating financial performance and non-compliance of SOCs.

First, a lack of internal control and oversight in the consistent monitoring of the SOC's financial and operational performance by its board and audit committee.¹¹⁰⁹ Secondly, the capacity constraints of SOC boards and their high director turnover rate negatively impacts the strategic continuity plans for improved performance and the effective implementation of financial risk management and internal controls.¹¹¹⁰ Thirdly, inadequate consequences levied against board members for the poor performance of SOCs and a lack of accountability for such performance.¹¹¹¹

As a result of the continuing lack of accountability of SOCs, the Auditor-General has implemented an accountability plan which consists of four pillars: plan, do, check and act.¹¹¹² The board of the SOC, together with the Minister, must strategically plan and set indicators and targets to be

¹¹⁰⁴ PAAA op cit note 647.

¹¹⁰⁵ Ibid at part 5.

¹¹⁰⁶ Makwethu (AGSA) op cit note 18 at 10.

¹¹⁰⁷ Ibid.

¹¹⁰⁸ Ibid at 11.

¹¹⁰⁹ Ibid at 10.

¹¹¹⁰ Ibid at 12.

¹¹¹¹ Ibid.

¹¹¹² Ibid at 18; Makwethu (AGSA) op cit note 902 at 10.

achieved by the SOC which are set out in the shareholders compact each year.¹¹¹³ In order for the plan to be achieved, there must be consistent implementation of effective internal controls to analyse the ongoing performance of the SOC.¹¹¹⁴ The internal controls and resultant performance of the SOC must be continually monitored and supervised by relevant assurance providers, such as the external auditors.¹¹¹⁵ In the event that an external check on the performance of the SOC yields mismanagement, the board of the SOC must be held accountable and consequences must be enforced.¹¹¹⁶

The accountability plan by the Auditor-General exhibits a formula for achieving the better future performance of SOCs. However, this plan has yet to be accurately implemented, as evidenced by the continued poor performance of SOCs, spanning the last five years.¹¹¹⁷ A lack of accountability and transparency in the governance of SOCs by the board and the Minister may have primarily contributed to their poor performance.¹¹¹⁸ These accountability issues arise due to non-compliance with legislation followed by an increase in the amount of irregular expenditure which is not curtailed, prevented or remedied by any enforceable mechanisms by the boards of SOCs or the Minister.¹¹¹⁹

In order to address the accountability issues, and as a result of increased allegations concerning state corruption and capture, the number of SOCs which the Auditor-General has opted to audit has increased.¹¹²⁰ The Auditor-General focused on SOCs which are expected to perform dual commercial and non-commercial mandates and whose budget makes up 27 per cent of the allocated budget for public entities, with financial guarantees amounting to R446 billion going to eleven SOEs.¹¹²¹ For the 2019 financial year-end only eight out of the 22 SOEs, categorized under schedule 2 of the PFMA, received clean audits.¹¹²²

The number of disclaimed Auditor opinions with findings increased, as did the number of outstanding audits for SOCs as a result of failing to submit financial statements in accordance with

¹¹¹³ Ibid.

¹¹¹⁴ Ibid.

¹¹¹⁵ Ibid.

¹¹¹⁶ Ibid.

¹¹¹⁷ Ibid; Masuku op cit note 184 at 123.

¹¹¹⁸ Masuku op cit note 184 at 123; Makwethu (AGSA) op cit note 902.

¹¹¹⁹ Ibid at 11 – 12.

¹¹²⁰ Ibid at 114.

¹¹²¹ Ibid at 117.

¹¹²² Ibid at 114 – 115.

the PFMA.¹¹²³ Such failures to submit financial reports by SOCs will cause inaccurate results for the consolidated reports of the Auditor-General.¹¹²⁴ Increases in non-compliance with legislation (up to 94 per cent non-compliance) and irregular expenditure were highlighted as major concerns for SOCs.¹¹²⁵

Whilst the outcome of the external audits of SOCs remains underwhelming, the performance of the Auditor-General has been above reproach under the leadership of Thembekile Kimi Makwethu.¹¹²⁶ The procedures and audit reports of the Auditor-General have been hailed as exemplary and the independence and impartiality with which audits have been conducted and investigations made are of the highest expertise.¹¹²⁷ A institution tasked with an important oversight and supervisory role over numerous SOCs, to strengthen constitutional democracy by ensuring the utmost accountability and transparency, the role of the office of the Auditor-General is essential.

The Auditor-General was appointed in 2014 for a period of seven years and his tenure expires in 2021.¹¹²⁸ If the Auditor-General utilises the new enforcement mechanism contained in the Public Audit Act during his tenure, the accountability and performance of SOCs may improve. The executive must also fulfil its duty under the PFMA to hold the board of an SOC accountable in terms of complying with its statutory financial reporting obligations.¹¹²⁹ Whatever the mechanism utilized, enforcement for compliance by the board of an SOC and its auditors with statutory requirements is essential to ensuring the effectiveness of the accountability check provided by the external audit.

4.7.2 The Public Protector

The office of the Public Protector is a constitutional institution established to strengthen democracy by holding the spheres of government accountable.¹¹³⁰ The Public Protector is constitutionally

¹¹²³ Ibid at 115 – 116; PFMA op cit note 11 at section 55 (1)(c).

¹¹²⁴ Ibid.

¹¹²⁵ Ibid.

¹¹²⁶ Auditor-General of South Africa ‘Annual Report 2018 – 2019: Enhanced Mandate for Enhanced Accountability’ (2019) available at <http://www.agsa.co.za/Reporting/AnnualReport.aspx>, accessed on 1 September 2020 at 23.

¹¹²⁷ Ibid at 23.

¹¹²⁸ Ibid.

¹¹²⁹ PFMA op cit note 11 at section 63 (2).

¹¹³⁰ Constitution op cit note 11 at section 181 (1)(a).

empowered to investigate, report on, and take appropriate remedial action against, allegedly improper conduct in state affairs or public administration which would include SOCs.¹¹³¹

The Zondo Commission has taken over the investigation into various SOCs as a result of the remedial action prescribed by the Public Protector in the State Capture Report. The conduct of SAA was investigated by the Public Protector due to allegations of corruption at the SOC raised by various media platforms.¹¹³² As a result, the Zondo Commission has carried on with this investigation into the alleged corrupt activities at SAA.¹¹³³

SAA has been under the spotlight of the Zondo Commission's inquiry on numerous occasions due to allegations of improper conduct, dishonesty, irregular and wasteful expenditure and maladministration at the SOC.¹¹³⁴ The Public Protector has the power to refer any of the board members of SAA to the NPA for prosecution if she is of the opinion that the facts uncovered at the Zondo Commission's inquiry disclose fraudulent conduct or financial misconduct by the board of SAA, which contravenes the provisions of the PFMA.¹¹³⁵ This referral and subsequent prosecution would serve as an effective deterrent for directors of other SOCs who are also currently under the spotlight for maladministration, such as Eskom and the SABC.¹¹³⁶

The initiation of voluntary business rescue proceedings by SAA, is, illustrative of the consequences of failing to enforce retributive measures against boards of SOCs for failing to account. SAA may have avoided such proceedings if the Public Protector had referred alleged offences made by the board to the NPA in 2016 when the State Capture Report was published.¹¹³⁷ The prolonged proceedings of the Zondo Commission and an inability to refer matters to the NPA by the Public Protector have contributed to the continued lack of accountability exhibited by the SAA board.

The office of the Public Protector has further been compromised, as the conduct of the current Public Protector, advocate Busisiwe Mkhwebane and the content of her reports have been the

¹¹³¹ Ibid at section 182 (1).

¹¹³² Madonsela op cit note 18 at 65.

¹¹³³ Commission of Inquiry into State Capture 'Recent Hearings Day 112 – 115, 207 - 212' available at <http://www.statecapture.org.za/site/hearings>, accessed on 2 September 2020.

¹¹³⁴ Ibid.

¹¹³⁵ PPA op cit note 682 at section 6 (4)(c)(i); PFMA op cit note 11 at section 86.

¹¹³⁶ Madonsela op cit note 16 at 48; Commission of Inquiry into State Capture 'Recent Hearings Day 155 - 163' available at <http://www.statecapture.org.za/site/hearings>, accessed on 2 September 2020.

¹¹³⁷ Madonsela op cit note 16.

subject of various court review applications.¹¹³⁸ The courts have been approached with various applications for the review of the Public Protector's remedial action, on allegations of its inappropriateness.¹¹³⁹ The power of the Public Protector to take appropriate remedial action must be rationally connected with its purpose to undo or redress prejudice or improper conduct.¹¹⁴⁰ Remedial action which cannot be rationally explained or justified by the Public Protector, based on accurate factual findings and a correct application of the law, calls into question not only the capacity but the motives of the Public Protector, in fulfilling her constitutional duties.¹¹⁴¹ The continuous court proceedings against the Public Protector detract from the effectiveness of her role to monitor the outcome of the Zondo Commission.¹¹⁴²

The Public Protector lacks the ability to enforce her own remedial action which may dilute from the effectiveness of her role as an external accountability measure over SOCs. The Public Protector is empowered to take remedial action against SOCs and the state, through the Minister, should enforce compliance with the remedial action in fulfilment of its constitutional accountability obligation. However, the state has not proven itself to be effective in enforcing any accountability measures over SOCs and therefore, it is submitted that the legislature should amend the PPA to empower the Public Protector to implement measures to ensure the enforcement of her own remedial action by SOCs.

4.7.3 The Separation of Powers

Constitutional, democratic dispensation is based on the doctrine of the separation of powers which entails a complex and intricate system of checks and balances amongst the three spheres of government.¹¹⁴³ The legislature, executive and judiciary are independent from one another and are accountable to one another.¹¹⁴⁴ SOCs fall under the executive arm of government and the

¹¹³⁸ De Vos op cit note 714.

¹¹³⁹ *ABSA Bank v PP* case supra note 714; *Minister of Home Affairs v PP* case supra note 714; *Reserve Bank* case supra note 714.

¹¹⁴⁰ Promotion of Administrative Justice Act 3 of 2000 at section 6(2)(f)(ii); *Minister of Home Affairs v PP* case supra note 714.

¹¹⁴¹ De Vos op cit note 714.

¹¹⁴² Madonsela op cit note 16 at 355.

¹¹⁴³ *Certification* case supra note 726 para 108.

¹¹⁴³ Ibid.

¹¹⁴⁴ Ibid.

legislature and judiciary provide external checks on the executive, in respect of the performance of SOCs.¹¹⁴⁵

(a) *The Executive*

The executive places internal accountability checks on its own actions by implementing a hierarchical structure, in accordance with its statutory and constitutional obligations.¹¹⁴⁶ This hierarchy of accountability is as follows: the board of the SOC reports to the Minister who then reports to Cabinet and members of the Cabinet report to Parliament.¹¹⁴⁷

It is submitted that the internal accountability check placed on SOCs by the executive has not been effective.¹¹⁴⁸ The executive established a number of institutions charged with the responsibility of supervising and monitoring executive action which included: the Scorpions, the HAWKS, the Anti-Corruption Task Team and the Special Investigating Unit.¹¹⁴⁹ None of these institutions, save for the Scorpions which have since been disbanded, made significant inroads into combating the lack of accountability and poor performance demonstrated by SOCs.¹¹⁵⁰

The Minister also seemed to be able to exert only a limited degree of control over the board of SAA which effectively compromised his or her ability to enforce the accountability of the SOC.¹¹⁵¹

It is not certain whether shareholder compacts were concluded annually between the state and SAA, which is a key tool for ensuring the accountability of the board, in the achievement of its key performance indicators.¹¹⁵² The Minister also failed to hold the board to account, as is evident

¹¹⁴⁵ PFMA op cit note 11 at section 63; Makwethu (AGSA) op cit note 18 at 184.

¹¹⁴⁶ Ibid; Public Service Act 103 of 1994; Constitution op cit note 11 at section 195 (1)(f).

¹¹⁴⁷ Constitution op cit note 11 at section 91 & 92 (2).

¹¹⁴⁸ Masuku op cit note 184 at 119.

¹¹⁴⁹ The Scorpions were a specialized law enforcement unit established by former president Thabo Mbeki to assist the South African police service with its fight against organized crime; The Scorpions were then dissolved and replaced by the Directorate for Priority Crime Investigation which is colloquially known as the Hawks; Business Tech 'What you need to know about the HAWKS and why they need to be more accountable' 24 August 2016 available at <http://businesstech.co.za/news/trending/134356/what-you-need-to-know-about-the-hawks-and-why-they-need-to-be-more-accountable/>, accessed on 2 September 2020.

¹¹⁵⁰ Gaye Davis 'Bathohi admits that ACTT has failed south africans' *Eyewitness News* 2019 available at <http://ewn.co.za/2019/10/16/batohi-admits-anti-corruption-task-team-has-failed-south-africans>, accessed on 2 September 2020; Marianne Thamm 'Anti-corruption-watchdogs call for integrity commission for the Hawks' *Daily Maverick* 2018 available at <http://www.dailymaverick.co.za/article/2018-09-27-anti-corruption-watchdogs-call-for-integrity-commission-for-the-hawks/>, accessed on 2 September 2020; Luke Daniel 'Corruption in South Africa to be stung by 'new 'scorpions'' *The South African* 8 February 2019 available at <http://www.thesouthafrican.com/news/scorpions-return-to-fight-corruption-in-south-africa>, accessed on 2 September 2020.

¹¹⁵¹ Thomas op cit note 9 at 454.

¹¹⁵² Makwethu (AGSA) op cit note 18 at 138.

from a lack of any retributive measures which were enforced against board of SAA, for failing to submit integrated reports for the 2018 and 2019 financial year-ends.¹¹⁵³

A failure in the direct accountability line between the board of SAA and the Minister was enabled by a failure from Cabinet to hold the Minister accountable.¹¹⁵⁴ Despite Pravin Gordhan being appointed as the new Public Enterprises Minister in 2018, the board of SAA have yet been held to account for the poor performance of the airline over the last decade.¹¹⁵⁵ It is possible that the Minister may be given additional statutory powers to dissolve SOC boards and step in when an SOC exhibits continuous financial mismanagement, non-compliance and performance issues.¹¹⁵⁶

SOCs are also held accountable for compliance with the PFMA under the supervision of the Minister of Finance.¹¹⁵⁷ The Minister of Finance stipulated conditions in the 2019 National Budget Review which were to be met by SAA prior to transfer of government funding or the issuing of further government guarantees.¹¹⁵⁸ These measures were not met by the board of SAA as it entered into voluntary business rescue proceedings in late 2019.¹¹⁵⁹ Without confirmation of the fulfilment of any of the previously stipulated requirements, government set aside a further R16.4 billion of its 2020 national budget for SAA.¹¹⁶⁰

The state has failed to provide an effective internal accountability check over SAA over the last decade. The Minister and the Minister of Finance have failed to hold the board of SAA and its directors accountable for financial, governance and operational failures which ultimately led to business rescue proceedings being initiated in 2019. The President, Deputy President or Cabinet have also failed to effectively supervise the board of SAA by failing to hold the Ministers accountable. Moreover, none of the executive institutions established by the state to oversee and monitor its own conduct, including that of SOC's, have ensured their accountability. The legislature

¹¹⁵³ Ibid at 120 & 138 – 139.

¹¹⁵⁴ Ibid at 138 – 139.

¹¹⁵⁵ Parliamentary Monitoring Group ‘Minister of Public Enterprises Update on State-Owned Companies; repeal of Overvaal Resorts Limited Bill’ available at <http://pmg.org.za/committee-meeting/26819/>, accessed on 2 September 2020.

¹¹⁵⁶ HR Pulse News Desk ‘Public enterprises minister wants to strengthen his legal power to remove SOE boards’ 20 August 2020 available at <http://www.hrpulse.co.za/news/latest-news/238093-public-enterprises-minister-wants-to-strengthen-his-legal-power-to-remove-soe-boards>, accessed on 1 September 2020.

¹¹⁵⁷ PFMA op cit note 11 at section 63 (2); *OUTA v Myeni* case supra note 346 para 27.

¹¹⁵⁸ National Treasury op cit note 38 at 112.

¹¹⁵⁹ National Treasury op cit note 1 at 4.

¹¹⁶⁰ Ibid at 4.

and judiciary are left a formidable task of enforcing the accountability of SOCs, as the internal check provided by the executive has become largely redundant.

(b) *The Legislature*

The legislature is constitutionally obligated to maintain oversight over the executive, by establishing mechanisms which require that all organs of state, in the national sphere of government, be held accountable to it.¹¹⁶¹

Whilst the SAA Reports state the board's continual compliance with the provisions of the PFMA, it is doubtful whether the executive actually effectively supervised and ensured such compliance.¹¹⁶² This is evidenced by the fact that SAA received a qualified audit opinion from the Auditor-General who conducted the external audit for their 2017 financial year-end which opinion set out various instances of non-compliance by the board of SAA with its statutory obligations.¹¹⁶³

Furthermore, the board of SAA failed to comply with its statutory obligation under the PFMA to submit annual financial statements for the 2018 and 2019 financial year-ends and no retribution has been levied against the board by the executive for its failure to comply with its statutory obligation.¹¹⁶⁴ Therefore, despite exercising its oversight function by passing legislation, the effectiveness of the legislature's supervisory role, in this capacity, is hindered by the executive's failure to implement the legislation and enforce statutory compliance by board of SAA.

The slightly more effective oversight role provided by the legislature over the actions of the board of SAA is provided by two primary committees, the SCOPA and the Portfolio Committee.¹¹⁶⁵ SCOPA was established by the rules of the National Assembly and draws its powers and functions therefrom.¹¹⁶⁶ SCOPA is primarily mandated to consider financial statements, audit reports and any other reports which review the expenditure of funds by SOCs.¹¹⁶⁷ SCOPA may report on those

¹¹⁶¹ Constitution op cit note 11 at section 55 (2)(a).

¹¹⁶² SAA Reports op cit note 20; 2013 report at 57, 2014 report at 79; 2015 report at 14; 2016 report at 67; 2017 report at 97.

¹¹⁶³ Ibid SAA 2017 report at 102 – 3.

¹¹⁶⁴ PFMA op cit note 11 at section 55 (1)(c)(i); Makwethu (AGSA) op cit note 18 at 41.

¹¹⁶⁵ Parliament of the Republic of South Africa 'SCOPA and public enterprises committee to keep close eye on SAA' 19 February 2020 available at <http://www.parliament.gov.za/press-releases/scopa-and-public-enterprises-committee-keep-close-eye-saa> accessed on 2 September 2020.

¹¹⁶⁶ Parliament op cit note 780 at rules at 150 (1)(vi) & 243.

¹¹⁶⁷ Ibid at rule at 245 (1)(a).

financial statements or reports to the National Assembly and may initiate an investigation into any matter which falls under its area of competence.¹¹⁶⁸

SCOPA has called upon the Minister to explain the non-submission by SAA of its annual financial statements for the 2018 and 2019 year-ends, requested updates from the Minister and engaged with the Business Rescue Practitioners over its plans to rescue the airline.¹¹⁶⁹ SOCPA is easily labelled as the most interactive and vocal committee in the fight against corruption. SCOPA has worked with various anti-corruption institutions, including the HAWKS, the Special Investigating Unit and the Anti-Corruption Task Team to investigate corruption allegations, many of which are levied against SOCs such as SAA and Eskom.¹¹⁷⁰ SCOPA continues to chisel away at corruption, with its recent report into the financial and governance failings at Eskom and providing numerous strict recommendations to resolve the SOC's many issues.¹¹⁷¹

The Portfolio Committee has a mandate to monitor, supervise and maintain oversight of the Minister, the Department of Public Enterprises and certain SOCs.¹¹⁷² This Portfolio Committee must ensure that the strategic plans and annual performance of SOCs in accordance with statutory requirements.¹¹⁷³ The Portfolio Committee, after monitoring the performance of the Minister and the Department of Public Enterprises, will provide recommendations which are to be followed by the Minister to improve the aforesaid Department's performance.¹¹⁷⁴ The Portfolio Committee will then also make a recommendation to the National Assembly on any matters pertaining to the Department of Public Enterprises and the Minister.¹¹⁷⁵

The Portfolio Committee has been very involved with the financial and governance issues for SAA as well as its turnaround strategy and has requested updates from the Minister on various

¹¹⁶⁸ Ibid at rule 245 (1)(b)(c).

¹¹⁶⁹ Parliamentary Monitoring Group 'Committee Meetings' available at <http://pmg.org.za/committee/42/?q=SAA> accessed on 2 September 2020.

¹¹⁷⁰ Parliamentary Monitoring Group 'Standing Committee on Public Accounts Legacy Report' 2019 available at <http://pmg.org.za/committee-meeting/28117>, accessed on 19 October 2019.

¹¹⁷¹ Parliamentary Monitoring Group 'Report of SCOPA on its oversight visit to ESKOM and its projects of Medupi and Kusile from 26 to 30 August 2019' 2019 available at <http://pmg.org.za/taled-committe-report/3937/>, accessed on 19 October 2019.

¹¹⁷² Parliamentary Monitoring Group 'Report of the Portfolio of Public Enterprises on budget vote 9: Public Enterprises and the Annual Performance Plan for 2019/2020 of the Department of Public Enterprises' 10 July 2019 available at <http://pmg.org.za/taled-committee-report/3867/>, accessed on 19 October 2019.

¹¹⁷³ Ibid at 2.

¹¹⁷⁴ Ibid at 9.

¹¹⁷⁵ Ibid at 10.

occasions.¹¹⁷⁶ The Portfolio Committee has also recommended the establishment of a State-Owned Enterprise Council by the Minister of Public Enterprises to provide feedback to the Portfolio Committee on the outcomes and implementation of all SOE reform proposals.¹¹⁷⁷

Under the instruction of the National Assembly, the Portfolio Committee has conducted its first investigation into state capture, through the submission of its report into the Eskom Inquiry.¹¹⁷⁸ This investigation by the Portfolio Committee has been hailed as an inroad into combating the endemic state corruption.¹¹⁷⁹ In its report the Portfolio Committee recommended to Parliament that the entire report be handed to the Zondo Commission for further investigation.¹¹⁸⁰

To a lesser extent, the Standing Committee on Finance also plays an oversight role in monitoring and reporting on the financial governance of SOCs. The Standing Committee on Finance was established by the rules of the National Assembly, in terms of the Money Bills Amendment and the Procedure and Related Matters Act.¹¹⁸¹ All of the powers and functions of the Standing Committee on Finance are mandated by the rules of the National Assembly, as well as legislation.¹¹⁸² The Standing Committee on Finance is responsible for considering macroeconomic, fiscal and revenue policy of all spheres of government and maintaining oversight over any organ of state which falls into its portfolio, including SOCs.¹¹⁸³ The Standing Committee on Finance may also monitor, investigate, enquire into and make recommendations to any SOC in respect of any matter which falls under its competence.¹¹⁸⁴

¹¹⁷⁶ Parliamentary Monitoring Group ‘Portfolio Committee on Public Enterprises: Committee Meetings’ available at <http://pmg.org.za/committee/73/?q=SAA>, accessed on 2 September 2020.

¹¹⁷⁷ PMG op cit note 1172 at 9.

¹¹⁷⁸ Parliament of the Republic of South Africa ‘Report of the Portfolio Committee of Public Enterprises on the Inquiry into Governance, Procurement, and the Financial Sustainability of Eskom dated 28 November 2018’ available at <http://www.parliament.gov.za/storage/app/media/Links/2018/November%202018/28-11-2018/Final%20Report%20-%20Eskom%20Inquiry%2028%20NOV.pdf>, accessed on 18 October 2019.

¹¹⁷⁹ Moira Levy ‘Applause as Public Enterprises Committee’s ends First Attempt at State Capture Inquiry’ Notes from the House 6 December 2018 available at <http://www.notesfromthehouse.co.za/news/item/294>, accessed on 2 September 2020.

¹¹⁸⁰ Ibid.

¹¹⁸¹ Parliament op cit note 780 rules at 230 & 150(b)(ii); Money Bills Amendment and the Procedure and Related Matters Act 9 of 2009.

¹¹⁸² Ibid at rules 227, 167, 230 – 235.

¹¹⁸³ Ibid at rules 227(1)(b)(ii) & 232.

¹¹⁸⁴ Ibid at rule 227(1)(c).

The financial reports and performance of SAA have been monitored by the Standing Committee on Finance, however, it has been largely inactive in the monitoring of SAA since June 2018.¹¹⁸⁵ In 2015, the Standing Committee on Finance received a report from the Parliamentary Budget Office setting out measures to strengthen SOCs financial operations through the sale of non-strategic state assets by specific SOCs, thereby reducing their reliance on state funding.¹¹⁸⁶ Given its financial responsibility and oversight mandate, the Standing Committee on Finance is primarily focused on the financing aspects of SOCs, such as SAA, and the ability of the Minister and the Department of Public Enterprises to curtail the unnecessary and wasteful expenditure of the SOCs.¹¹⁸⁷

Since early 2018, the activities of the various committees under the auspices of the National Assembly have been overshadowed by the establishment of the Zondo Commission. The Zondo Commission has become the primary vehicle of investigation into the activities and operations of many failing SOCS, of which SAA has been highlighted as one of the most deteriorating.¹¹⁸⁸

(c) *The Judiciary*

The judiciary, as the third sphere of government, acts as an external check on the executive by scrutinizing its conduct.¹¹⁸⁹ The independence of the judiciary is essential to its ability to hold the executive accountable for its conduct and the executive and legislature are bound to maintain, protect and uphold the integrity of the judiciary at all times.¹¹⁹⁰

The boards of Eskom and the SABC have had the most publicized cases involving allegations of a breach of their fiduciary duties which, arguably, stem from a chronic lack of accountability from these SOCs.¹¹⁹¹ The Minister and the Minister of Communications have also been accused of failing in their constitutional obligation to hold the boards of SOCs accountable.¹¹⁹² Although

¹¹⁸⁵ Parliamentary Monitoring Group ‘Standing Committee on Finance: Committee Meetings’ available at <http://pmg.org.za/committee/24/?q=SAA>, accessed on 2 September 2020.

¹¹⁸⁶ Parliamentary Monitoring Group ‘State Owned Enterprises Programme Report: Parliamentary Budget Office (PBO) Briefing 12 August 2015 available at <http://pmg.org.za/committee-meeting/21300/>, accessed on 2 September 2020.

¹¹⁸⁷ Ibid.

¹¹⁸⁸ The Commission of Inquiry into State Capture op cit note 936.

¹¹⁸⁹ Constitution op cit note 11 at section 165 (3) & (4).

¹¹⁹⁰ Ibid.

¹¹⁹¹ *SABC case supra note 167; Democratic Alliance v Minister of Public Enterprise and Others; Economic Freedom Fights v Eskom Holdings Limited and Others; Solidarity Trade Union v Molefe and Others [ZAGPPHC]* unreported cases numbers 33051/2017; 34568/2017; 34042/2017 of 25 January 2018.

¹¹⁹² Ibid *SABC case* para 80; Ibid *Eskom case* para 60.

personal liability was sought as the remedy for a breach of their fiduciary duties by two of the directors of SABC, it is not yet evident whether this form of retribution will deter future breaches by current directors on SOC boards.¹¹⁹³

The personal liability imposed on the directors of SABC was limited to the costs of the application.¹¹⁹⁴ It is conceivable that the longer the tenure of the director and the repeated breaches of duties during such tenure, the higher the amount of personal liability that should be imposed. In the premise, the loss suffered by the SOC during the director's tenure should be considered in the court's calculation of the personal liability claim. This causal link will serve as a better deterrent for future directors who are seeking to make undue personal gains, at the expense of the SOC.

Another popular method of seeking retribution against unruly directors of SOCs appears to be through the use of delinquency applications which are brought to court by interested parties. OUTA launched a successful delinquency application against former non-executive chairperson of SAA, Myeni who has now been declared a delinquent which order subsists for her lifetime.¹¹⁹⁵ Corruption Watch have launched delinquency applications against certain SOC directors at Eskom.¹¹⁹⁶ These applications are brought on the basis that, during the directors' tenure, huge losses were suffered by the SOCs which were allegedly caused by the directors' actions in terms of intentional or gross negligence, a gross abuse of power or undue personal advantage.¹¹⁹⁷

It is submitted that a delinquency order is a better form of retributive punishment against directors than the imposition of personal liability for a breach of their duties. While personal liability may be a painful but fleeting remedy, a delinquency order may be unconditional and endure for a seven-year period or subsist for the lifetime of the director depending on the circumstances which brought about the application.¹¹⁹⁸

The Companies Act does not distinguish between executive and non-executive directors in terms of a delinquency order and prevents the delinquent from serving on any board, whether as an

¹¹⁹³ *SABC* case para 225.

¹¹⁹⁴ *Ibid.*

¹¹⁹⁵ *OUTA v Myeni* case supra note 346.

¹¹⁹⁶ Corruption Watch 'All Correspondence in our Eskom Delinquency Application' April 2019 available at <http://www.corruptionwatch.org.za/all-cws-correspondence-in-our-eskom-delinquency-application/>, accessed on 3 September 2020.

¹¹⁹⁷ *Ibid.*; *OUTA v Myeni* case supra note 346 para 5.

¹¹⁹⁸ Companies Act op cit note 11 at section 162 (6)(a) & (b).

executive or non-executive director.¹¹⁹⁹ For non-executive directors, this delinquency order can have the effect of forcing them to seek other avenues of income if they were solely dependent on the income derived from serving on multiple boards. The delinquency order also protects future SOCs from the disastrous effects which may be suffered as a result of grossly negligent directors.¹²⁰⁰

At the conclusion of Zondo Commission's investigation there may be more cases instituted against SOC directors who are alleged to have breached their duties. From these cases, it may become evident whether the imposition of personal liability or a delinquency order against directors will serve as an effective retributive mechanism to enforce the accountability of SOCs.

In addition to bringing a court application against an SOC director, the NPA may criminally prosecute any director alleged to have committed an offence as a result of a breach of their statutory duties.¹²⁰¹ The Public Protector or the Zondo Commission may refer any matter for prosecution, further investigation or the convening of a separate enquiry to the appropriate law enforcement agency, government department or regulator regarding the conduct of certain persons.¹²⁰² The tenure of the previous Public Protector, advocate Thulisile Madonsela expired before she could bring any matters, identified as alleged crimes in her various reports, to the notice of the NPA. The current Public Protector has yet to refer any matters to the NPA and is accused of failing to effectively monitor the conduct of the Commission in accordance with the remedial action set out in the State Capture Report.¹²⁰³

It is arguable that criminal prosecution would serve as an even better deterrent than delinquency orders or the imposition of personal liability for directors of SOCs. There are reports of a special directorate to be set up by the NPA to deal with criminal prosecutions following the evidence gathered at the Zondo Commission.¹²⁰⁴ The actual enforcement of the prosecution of SOC directors or the Minister found guilty of committing criminal offences, through the Zondo Commission's investigation, has yet to be ascertained.

¹¹⁹⁹ Ibid.

¹²⁰⁰ *OUTA v Myeni* case supra note 346 para 276.

¹²⁰¹ PFMA op cit note 11 at section 82 (2).

¹²⁰² Terms of Reference op cit note 14 at 8 – 9; Madonsela op cit note 16 at 354; PPA op cit note 682 at section 6 (4)(c).

¹²⁰³ Madonsela op cit note 16 at 355; De Vos op cit note 714.

¹²⁰⁴ Pather op cit note 920.

Lastly, the establishment of the Zondo Commission, as a judicial commission of inquiry, places an external accountability check on SOCs and the Minister.¹²⁰⁵ SOCs have been under the spotlight following allegations set out in the State Capture Report.¹²⁰⁶ The Zondo Commission's mandate is wide and far-reaching and no executive action will escape scrutiny which will include: decisions taken by SOCs boards and their directors, the Minister's actions and the President's conduct.¹²⁰⁷ SAA has been implicated on numerous occasions in respect of corrupt activities and maladministration and the Zondo Commission has delved into an in-depth investigation of the various internal and external accountability failures by the SOC.¹²⁰⁸

There is an ongoing debate which revolves around the necessity and effectiveness of a judicial commission of inquiry. In conducting the inquiry of the commission, members of the judiciary are inevitably required to perform executive actions by investigating matters instead of adjudicating upon them.¹²⁰⁹ The appointment of judicial members to the commission may also be abused by the executive, as a result of political pressures which may erode the independence of the judiciary.¹²¹⁰ Judicial commissions are generally established where there are no applications or complainants to institute proceedings in a court setting.¹²¹¹ It is arguable whether the judicial commissions, established by the executive, are the most effective way to investigate executive maladministration and corruption.

Despite the fact that numerous judicial commissions of inquiry have been established in the past, they have not had the desired effect of preventing corruption.¹²¹² Costly and lengthy exercises,

¹²⁰⁵ Terms of Reference op cit note 14; Commissions Act 8 of 1947.

¹²⁰⁶ Madonsela op cit note 16 at 55 -71.

¹²⁰⁷ Terms of Reference op cit note 14 at term 1.

¹²⁰⁸ Commission of Inquiry into State Capture op cit note 1190.

¹²⁰⁹ *SARFU* case supra note 814 para 141; Okpaluba, Chuks & Mtendeweke Mhango 'Between separation of powers and justiciability: Rationalising the Constitutional Court's Judgement in the Gauteng E-tolling litigation in South Africa' (2017) 21 *Law, democracy & development* 1 at 6.

¹²¹⁰ Ibid.

¹²¹¹ Grant Hoole 'Reconceiving Commissions of Inquiry: as Plural and Participatory Institutions: A Critical Reflection on Magidiwana (2016) *Constitutional Court Review* 221 at 230; *Magidiwana & Others v President of the Republic of South Africa & Others* [2014] 1 ALL SA 61 (GNP) para 26.

¹²¹² Cliffe Dekker Hofmeyr 'Groundbreaking judgement redefines the role of Commissions of Inquiry and civil society – Part 2' 5 February 2020 available at <http://www.cliffedekkerhofmeyr.com/en/news/publications/2020/dispute/dispute-resolution-alert-5-february-groundbreaking-judgment-redefines-the-role-of-Commissions-of-Inquiry-and-civil-society-Part-2.html>, accessed on 3 September 2020.

judicial commissions of inquiry seem to be a method in placation as opposed to resolving the issue of a lack of enforceable accountability for underperforming SOCs.¹²¹³

The findings and recommendations of the Zondo Commission may be subject to judicial review and can be set aside by a court on application by an interested party.¹²¹⁴ There are two promising outcomes of a courts authority to set aside the findings of a judicial commission of inquiry. First, the findings of the commission cannot be used by any person as evidence in further court proceedings.¹²¹⁵ Secondly, precedent has been set for the importance of accurate findings to be ascertained by judicial commissions of inquiry which have a fact-finding mission mandate.¹²¹⁶

Therefore, even if the Zondo Commission finds that directors of SOCs have not breached their statutory duties, this finding cannot be used as evidence in a court case against that director for a breach of his or her duties. The Zondo Commission does not have the final say as to the liability which may be imposed on directors of SOCs who are alleged to have breached their duties and directors may still be taken to court, notwithstanding the outcome of the Zondo Commission's investigation and recommendations. It is still debatable whether the Zondo Commission has the necessary teeth to resolve the accountability issue of underperforming SOCs.¹²¹⁷

The Zondo Commission has a mandate to make recommendations on the findings of its investigation and is not empowered to take any other action against SOCs, their directors or Ministers, save for referrals to the NPA.¹²¹⁸ It is arguable that the outcome of the investigation is redundant if the Zondo Commission lacks the enforceability to take action itself against alleged perpetrators of corruption. In the premise, the lengthy proceedings of the Zondo Commission, whilst informative, will be anti-climactic if no further action is taken. The report of the Zondo Commission may not even be made public as it is submitted to the President to take further action.¹²¹⁹ A report on state corruption should be made public and not be solely submitted to the very executive on which the report is based.

¹²¹³ Ibid.

¹²¹⁴ *Corruption Watch and Another v Arms Procurement Commission and Others* 2020 (2) SA 165 (GP) para 72.

¹²¹⁵ Ibid para 70.

¹²¹⁶ Ibid; Cliffe Dekker Hofmeyr op cit note 1284.

¹²¹⁷ Kelly Kropman & Amanda Shivamba 'Do Commissions of Inquiry have Teeth?' News24 19 November 2017 available at <http://www.news24.com/Columnists/GuestColumn/do-commissions-of-inquiry-have-teeth-20171117>, accessed on 3 September 2020.

¹²¹⁸ Terms of Reference op cit note 14 term 1 at 1 & term 7 at 8.

¹²¹⁹ Ibid term 5 at 8.

The judiciary has been the most effective sphere of government which has acted as an external accountability check on SOCs over the last decade. Whilst the executive and legislature have provided some element of supervision, their ability to enforce the accountability of SOCs is unimpressive. In the unlikely event that even the judiciary fails as an external accountability mechanism for SOCs, the public will have to become involved as an avenue of last resort.

4.8 The Public

The public may only intervene to hold the board of an SOC and the Minister to account through limited methods. The methods available to the public include: a vote of no confidence in the President and his Cabinet, public protests and rallies, joining private institutions which fight against corruption and, possibly, through a section 218 (2) application of the Companies Act.¹²²⁰

In order to pass a vote of no confidence in the President or his Cabinet, a two-third majority vote from the members of the National Assembly is required.¹²²¹ In a constitutional democracy, a two-third majority should be difficult to achieve by one political party alone. However, this has been the case in South Africa for over two decades as the members of the ruling political party have held approximately a two-third majority vote in the National Assembly.¹²²² Therefore, there is little chance of a vote of no confidence being passed, unless the ruling party is pressurized to remove its own appointed President or Cabinet. The drafters of the Constitution may have seen no reason to include another mechanism for removing the President or his Cabinet, other than by a two-third majority vote.

Public protests have been held by private citizens, strongly voicing the public's discontent with the current government and its questionable activities which are in discord with the principles of the Constitution to respect and uphold the Republic and its people.¹²²³ Through citizen-funded organizations such as OUTA, Save South Africa and Corruption Watch, notable public protests against corruption and failing SOCs have gained local and international media recognition.¹²²⁴

¹²²⁰ Constitution op cit note 11 at section 102; Companies Act op cit note 11 at section 218 (2).

¹²²¹ Ibid at section 102.

¹²²² Parliament of the Republic of South Africa 'African National Congress party details' available at <http://www.parliament.gov.za/party-details/ANC>, accessed on 3 September 2020.

¹²²³ Masuku op cit note 184 at 123. Al Jazeera News 'Thousands March Against Corruption in South Africa' 27 September 2017 available at <http://www.aljazeera.com/news/2017/09/thousands-march-corruption-south-africa-170927092332199.html>, accessed on 3 September 2020.

¹²²⁴ Save South Africa 'About us' available at <http://www.savesouthafrica.org/wp-content/uploads/2017/11/savesa-statement-on-2-november-21.pdf>, accessed on 3 September 2020; The New York Times 'South Africa Ramaphosa

These institutions combat corruption through various methods including: peaceful protests and demonstrations, referendums to Parliament, applications to courts and investigations and reports conducted into government and made available to the public.¹²²⁵ Whilst not a realistic method for continually ensuring accountability, public activism has gained momentum over the last decade and is proving to be a powerful accountability mechanism.¹²²⁶ SAA's board is the focus for OUTA which launched a successful court application for a delinquency order granted against former non-executive chairperson Myeni.¹²²⁷ Similarly, Corruption Watch have launched a court application seeking a delinquency order against the board of Eskom.¹²²⁸

The Zondo Commission's current investigation seems to have placated the public to a certain degree. The investigation attempts to illustrate government's willingness to fight against corruption.¹²²⁹ However, without a measure of enforceability the recommendations made by the Zondo Commission in its unveiling of a corrupt executive which includes many SOCs may become redundant.

Another possible mechanism available to the public to hold the directors of an SOC liable for a breach of their duties may lie in the application of section 218 (2) of the Companies Act.¹²³⁰ This catch-all provision for liability may allow for a class action to be brought by the public against directors of SOCs. The public would have to prove that their loss was caused by the directors breaching their duties and that the loss suffered is not reflective of the loss suffered by the SOC.¹²³¹ The loss suffered by the public would arguably be a loss of earnings as the downgrade of the economy, due in large part to failing SOCs, increased their costs of living as a result of inflation and tax increases. The public's claim would be difficult to prove given the precedent set by recent case law.

Protests' 19 April 2018 available at <http://www.nytimes.com/2018/04/19/world/africa/south-africa-ramaphosa-protests.html>, accessed on 19 October 2018.

¹²²⁵ Ryan, Ciaran 'Corruption Watch goes to war against previous Eskom board' *Moneyweb* 1 April 2019 available at <http://www.moneyweb.co.za/news/south-africa/corruption-watch-goes-to-war-against-previous-eskom-board/>, accessed on 3 September 2020.

¹²²⁶ *Ibid.*

¹²²⁷ *OUTA v Myeni* case supra note 346.

¹²²⁸ Corruption Watch op cit note 1267.

¹²²⁹ Kropman op cit note 1217.

¹²³⁰ Companies Act op cit note 11 at section 218 (2).

¹²³¹ *Hlumisa* case supra note 309.

The shareholders of ABI and Steinhoff approached the court with a 218 (2) claim against the directors of the companies stating that the diminution of the value in their shares caused them to suffer a loss which was as a result of the directors breaching their duties.¹²³² On both occasions, the court held that the loss suffered by the shareholders, in a diminution of the value of their shares, was reflective of the loss suffered by the companies.¹²³³ Therefore, the shareholders had not proved that the loss was suffered by them and their claims under section 218 (2) were dismissed. In these circumstances, as in accordance with the common law, only the company suffering the loss has an action against the party causing the loss.¹²³⁴

The remedy under section 218 (2) has yet to be implemented by the public and the link between their loss and the breach of duties by the directors of SOCs may be too tenuous to sustain a cause of action. However, the action of the public in bringing such an application against the directors of SOCs may have the desired effect of illustrating the public's discontent with government and act as a warning to all future SOC directors. The public need to be given a realistic avenue for holding the executive and its failing SOCs to account.

4.9 Conclusion

Despite the numerous internal and external accountability measures which are available to SOCs, their practical implementation appears to be absent and accountability remains an issue. As is illustrated through an analysis and interpretation of the SAA Reports, it is submitted that the lack of accountability exhibited by SAA has contributed to its poor financial performance, since 2012. Once the Zondo Commission concludes its investigation into SAA, and various other SOCs, punishment may be levied against directors who are alleged to have breached their statutory or common law duties. However, the current retribution -based approach utilised in an attempt to enforce the accountability of SOCs, such as SAA, may not be effective and an alternative approach for enforcement may be required.

¹²³² Ibid; *De Bruyn* case supra note 353 at 189.

¹²³³ Ibid.

¹²³⁴ Ibid.

CHAPTER FIVE: CORPORATE GOVERNANCE OF SOCS

5 Introduction

The financial performance failures of many SOCs in South Africa over the last decade has been attributed to a lack of accountability.¹²³⁵ The principle of accountability has mainly been achieved through the implementation of effective corporate governance structures for SOCs although accountability may be achieved through other mechanisms.¹²³⁶ However, it is proposed that in order for accountability to be meaningfully achieved, a method of enforcement needs to be implemented. It is proposed that enforceable accountability for SOCs may be achieved in a cost-effective and efficient manner through the implementation of a reformed combination of retribution and reward-based mechanisms.

5.1 The Concept of Corporate Governance

The concept of corporate governance was borne out of a need for resolving the age-old agency issue which arises on the incorporation of a company as a separate juristic entity.¹²³⁷ The directors of a company are the managers who control the company on behalf of the shareholders who own the company.¹²³⁸ The agency issue arises due to a divergence between those who manage the company, the directors and those who own the company, the shareholders.¹²³⁹ The issue pertains to the potential conflicts of interest which may arise as a result of the divergence of interests between the directors and shareholders.¹²⁴⁰

Directors are required to exercise their fiduciary duties, and the duty of care and skill, in serving the best interests of the company at all times.¹²⁴¹ Shareholders, on the other hand, owe no fiduciary duties to the company and are primarily concerned in serving their own interests in terms of a growth in their investment in the company.¹²⁴² Potential conflicts of interest are inevitable when the competing interests of directors and shareholders collide. Whilst shareholders are free to act as

¹²³⁵ Makwethu (AGSA) op cit note 18 at 10; Thabane op cit note 9 at 25; Thomas op cit note 9; Kanyane op cit note 10 at 32; Futuregrowth op cit note 10 at 12; McGregor op cit note 831 at 5; Masuku op cit note 184 at 118; Makoni op cit note 13 at 23; Moloi op cit note 905 at 1 – 2.

¹²³⁶ King IV op cit note 19 at 1.

¹²³⁷ Wiese op cit note 63 at 2; Makoni op cit note 13 at 21; Makuta op cit note 205 at 56.

¹²³⁸ Ibid.

¹²³⁹ Thabane op cit note 9 at 6.

¹²⁴⁰ Wiese op cit note 63 at 2.

¹²⁴¹ Futuregrowth op cit note 10 at 4; Kanyane op cit note 10 at 30.

¹²⁴² Ibid.

selfishly as they wish, the directors are duty bound to act only in the best interests of the company.¹²⁴³

On occasion, circumstances arise which result in a misalignment of company's interests with that of its shareholders. In such an untenable situation, the directors are tasked with the duty of serving the best interests of the company.¹²⁴⁴ Ultimately, the directors owe their duties to the company as a separate juristic entity which comprises the interests of its various stakeholders and not just its shareholders.¹²⁴⁵ Directors are required to account to the shareholders for their decisions taken and should always be mindful of acting in the best interests of the company which should be the primary justification for any decision taken. Corporate governance is the popular method utilised to achieve the accountability of the board of an SOC.¹²⁴⁶

The more traditional and historic description of corporate governance stems from the United Kingdom's Cadbury Report which was published in 1992 and defines corporate governance as '*the practice by which companies are managed and controlled*'.¹²⁴⁷ This definition has been expanded upon and the concept of corporate governance has been further described as: '*the system and process by which organisations are directed and controlled in order to ensure the protection of the interests of the owners*'.¹²⁴⁸ As a result of evolving global corporate trends, the definition of corporate governance has been expanded even further to include the interests of other stakeholders and not just the shareholders as owners of the company.¹²⁴⁹ This is due to the increasing recognition of the role which society, the community and the environment play in the company's achievement of its aims and objectives.¹²⁵⁰

In South Africa, the King Codes provide recommended practices for good corporate governance which should be applied by all entities, irrespective of their form of incorporation.¹²⁵¹ The most recent report in the King Codes, King IV depicts a wider definition of corporate governance as:

¹²⁴³ Cassim at op cit note 78 at 394.

¹²⁴⁴ Ibid at 524.

¹²⁴⁵ Ibid.

¹²⁴⁶ Schulschenk op cit note 34 at 5; King IV op cit note 19 at 4.

¹²⁴⁷ Wiese op cit note 63 at 2; Committee on the Financial Aspects of Corporate Governance 'Report of the Committee on the Financial Aspects of Corporate Governance' ('UK Cadbury Report') (1992) available at <http://ecgi.global/sites/default/files//codes/documents/cadbury.pdf>, accessed on 13 August 2020.

¹²⁴⁸ Schulschenk op cit note 34 at 5.

¹²⁴⁹ Wiese op cit note 63 at 2; Jean J Du Plessis et al *Principles of Contemporary Corporate Governance 2ed* (2011) at 10.

¹²⁵⁰ Ibid at 2; Schulschenk op cit note 34 at 5.

¹²⁵¹ Ibid at 22; King IV op cit note 19 at 35.

*‘the exercise of ethical and effective leadership by the governing body towards the achievement of the following governance outcomes: ethical culture, good performance, effective control and legitimacy.’*¹²⁵² King IV advocates a stakeholder-inclusive approach which reinforces the concept that the directors of an entity must take into account the interests of all stakeholders and not just the owners.¹²⁵³ The stakeholder-inclusive approach and King IV’s definition of corporate governance aligns the South African corporate landscape with current international trends.

The expanded definition of corporate governance gives rise to a debate surrounding the definition of the ‘owners’ of the company. The owners of the company were traditionally solely defined as the shareholders.¹²⁵⁴ The directors were required to manage and control the company in the best interests of the shareholders which amounted to a goal of short-term profit maximization.¹²⁵⁵ Fundamental global shifts saw an extension of this traditional approach to include the interests of other stakeholders, in the decision taking of the directors, but only to the extent that it would be in the interests of the shareholders to do so.¹²⁵⁶ This evolved framework was deemed the ‘*shareholder-centric*’ or ‘*enlightened shareholder*’ approach.¹²⁵⁷

The ‘*shareholder-centric*’ or ‘*enlightened shareholder*’ approach again expanded and evolved to the ‘stakeholder inclusive’ approach.¹²⁵⁸ This approach ranks the interests of all stakeholders as equal and removes the shareholder from its predetermined place of priority as the primary stakeholder.¹²⁵⁹ Other such stakeholder interests, in addition to the shareholders, include: employees, customers, creditors, the community, environment and government.¹²⁶⁰

King IV supports the stakeholder-inclusive approach by recommending that ‘*the legitimate and reasonable needs, interests and expectations of all material stakeholders*’ should be taken into account when taking decisions in the best interests of the company.¹²⁶¹ The theory behind this approach is that all stakeholders have a vested interest in the sustainability of the company and

¹²⁵² Ibid at 20.

¹²⁵³ Ibid at 25.

¹²⁵⁴ Wiese op cit note 63 at 6.

¹²⁵⁵ Ibid.

¹²⁵⁶ Ibid at 7; Cassim op cit note 63 at 20.

¹²⁵⁷ Ibid.

¹²⁵⁸ Wiese op cit note 63 at 7.

¹²⁵⁹ Ibid.

¹²⁶⁰ Ibid at 8 – 9.

¹²⁶¹ King IV op cit note 19 at 25.

that companies do not operate in an archaic vacuum where the interests of all stakeholders are subordinated in favour of the shareholders.¹²⁶²

The advent of the Companies Act did not bring about any closure to the debate around the consideration of shareholder's and stakeholders' interests for directors in South Africa.¹²⁶³ Under the statutory duties, the directors are required to take decisions in the best interests of the company.¹²⁶⁴ The Companies Act provide for a basic definition of a company as a juristic person which is registered in accordance with its provisions.¹²⁶⁵ Directors are therefore left to interpret and apply their statutory duties in accordance with case law in order to ascertain the parameters of what would constitute a decision which is taken in the best interests of the company.

Whilst there may be a growing need to recognize the effect which all stakeholders have on the company, the aim and purpose for which the company was established should always be the primary consideration. Most companies are established in order to achieve commercial goals and whereas the directors may consider the interests of the community or environment, in their decision taking, the interests of the company are paramount.

5.1.1 The Importance of Corporate Governance

The central purpose and importance of corporate governance is an ever-debated topic. Opponents of corporate governance argue the relevance and impact which a voluntary set of recommended practices can have on the accountability of entities and their ultimate performance.¹²⁶⁶ The costs of compliance with corporate governance structures are also a deterrent for their implementation, especially, when entities are unconvinced of the relative importance of corporate governance.¹²⁶⁷ Proponents of corporate governance will argue that effective corporate governance structures can

¹²⁶² Wiese op cit note 63 at 12; Anna Ramalho 'The distinctive stance of the King Reports on corporate governance from a global perspective' (2019) 11 *Journal of Global Responsibility* 173 at 174.

¹²⁶³ Ibid at 9.

¹²⁶⁴ Companies Act op cit note 11 at section 76 (3)(b).

¹²⁶⁵ Ibid at section 1.

¹²⁶⁶ Charles Gubert 'The Importance of Corporate Governance' 2011 Gale Academic OneFile available at <http://www.link.gale.com/apps/doc/A280689321/AONE?u=unict&sid=AONE&xid+edc4bc7d>, accessed on 2 September 2020.

¹²⁶⁷ Schulschenk op cit note 34 at 21.

serve as preventative measures for massive corporate failures and attract local and foreign investors thereby improving financial performance.¹²⁶⁸

The King Codes stipulate that the implementation of effective corporate governance structures results in the achievement of the overarching principles of fairness, accountability, transparency and responsibility.¹²⁶⁹ Other objectives of corporate governance include: good leadership, oversight of management (by the board and the shareholder), ethical compliance with rules and regulations, risk management, sustainability and long-term growth, transparency, disclosure, accountability and responsibility to all stakeholders.¹²⁷⁰ King IV provides the following outcomes which can be realized by entities practicing good corporate governance: ethical culture, good performance, effective control and legitimacy.¹²⁷¹

Over the last decade, the attainment of these principles by the boards of entities, as the ultimate decision-making body, has become a prominent priority.¹²⁷² Since the economic and financial crises of 2008, the importance of establishing effective corporate governance structures has been emphasized.¹²⁷³ It is argued that a lack of corporate governance mechanisms has been a contributing factor to many of the recent, local and global corporate and operational failures of various entities.¹²⁷⁴

In the United States, the large-scale corporate failures of the Enron Corporation and the Lehman Brothers Holdings Inc, emphasized the need for efficient corporate governance structures.¹²⁷⁵ Both scandals rocked the financial and operational stability of the American economy, which would suffer the drastic after-effects for many years to come.¹²⁷⁶ In the United Kingdom, weak corporate governance structures of the local banks was found to be one of the predominant causes of the

¹²⁶⁸ Gubert op cit note 1266; Makuta op cit note 205 at 60; Ramalho op cit note 1262at 175; Isaih Dzingai & Michael Fakoya 'Effect of Corporate Governance Structure on the Financial Performance of Johannesburg Stock Exchange (JSE) Listed Mining Companies' (2017) 9 *DOAJ Directory of Open Access Journals* 867.

¹²⁶⁹ King III op cit note 217 at 7; King IV op cit note 19 at 41.

¹²⁷⁰ Wiese op cit note 63 at 3; Du Plessis op cit note 1249 at 11 – 13.

¹²⁷¹ King IV op cit note 19 at 41.

¹²⁷² Makuta op cit note 205 at 68; Davies op cit note 709 at 9.

¹²⁷³ Ibid Makuta at 58; Davies at 26; Dzingai op cit note 1268 at 870.

¹²⁷⁴ Ibid.

¹²⁷⁵ Ibid Davies at 26 – 27; Kirkpatrick, Grant 'The Corporate Governance Lessons from the Financial Crises. Financial Market Trends' (2009) *OECD Journal: The Financial Market Trends* 61-87 at 63.

¹²⁷⁶ Ibid.

2008 financial banking crises.¹²⁷⁷ As a result of these massive international corporate failures, which superseded many other corporate failures around the world, a renewed interest in the value of corporate governance was sparked.¹²⁷⁸

South African entities alike had their own corporate failures, the notable examples of which include: the Fidentia Group and Leisurenets scandals and most recently the Steinhoff and ABI sagas.¹²⁷⁹ SOCs have also been highlighted as the most culpable entities which have exhibited signs of massive governance failures which have been attributed to their downfall.¹²⁸⁰ The unequivocal financial, operational and corporate failures of SOCs such as Eskom, SABC, SAA and Telkom SA SOC Limited have greatly depleted investor and public confidence in the state's ability to successfully improve the national growth of the economy.¹²⁸¹

The South African economy has been weakened, and almost depleted, as a result of the significant failures of these SOCs, especially over the last decade.¹²⁸² It is argued that at the heart of these failures is a lack of accountability which may be attributed to an inability to implement effective corporate governance structures.¹²⁸³ This was the finding of the former Public Protector in her State Capture Report which depicted the detrimental impact which these SOC failures have, not only on the SOC itself, but the economy and community at large.¹²⁸⁴

Many of the local and global corporate failures may have also resulted from the effects of short-termism in the form of profit maximization as the sole objective for many entities.¹²⁸⁵ Directors are pressured into ensuring and protecting the shareholder, as the primary stakeholder, often in lieu of the best interests of the entity.¹²⁸⁶ Whilst profit maximization is an important goal, directors

¹²⁷⁷ Jean Dermine 'Bank Corporate Governance: Beyond the Global Banking Crises' (2011) INSEAD The Business School for the World available at: <http://sites.insead.edu/facultyresearch/research/doc.cfm?did=47338>, accessed on 4 September 2020.

¹²⁷⁸ Davies op cit note 709 at 26.

¹²⁷⁹ Thabane op cit note 10 at 2; *S v Brown* 2015 (1) SACR 211 (SCA); *Hlumisa* case supra note 309; *De Bruyn* case supra note 353; University of Stellenbosch Business School 'Business Perspectives on the Steinhoff Saga' (2018) Available at: http://www.usb.ac.za/wp-content/uploads/2018/06/Steinhoff_Revision_28_06_2018_websmall.pdf, accessed on 13 August 2020.

¹²⁸⁰ Thabane op cit note 9 at 4; Thomas op cit note 9 at 453; Futuregrowth op cit note 10 at 10; Kanyane op cit note 10 at 32; Makwethu (AGSA) op cit note 18 at 10; National Treasury op cit note 1 at 1; Madonsela op cit note 16 at 50 – 70.

¹²⁸¹ Ibid.

¹²⁸² Thabane op cit note 9 at 5.

¹²⁸³ Madonsela op cit note 16 at 50 – 70.

¹²⁸⁴ Ibid.

¹²⁸⁵ Deniz, Ozden 'The Importance of Corporate Governance for a Well-Functioning Financial System: Reforming Corporate Governance in Developing Countries' (2010) 14 *Duquesne Business Law Journal* 219.

¹²⁸⁶ Ibid at 220.

should also focus on long-term growth and sustainability in order to ensure the future protection of the interests of all stakeholders' and not only the shareholder.¹²⁸⁷

Following the 2008 financial crises, international corporate trends have shown a fundamental shift from short-term profit maximization to long-term growth, development and sustainability in an effort to protect the interests of all stakeholders.¹²⁸⁸ It is submitted that sound corporate governance practices promote the sustainability and protection of all stakeholder interests which in turn boosts investor confidence in the entity.¹²⁸⁹ Entities with effective corporate governance structures have been associated with greater market value, an increase in financial and operational performance and provide a valuable contribution to the economy.¹²⁹⁰

The sound corporate governance of SOCs attracts local and international investors, serves to boost public confidence and accelerates growth and development for our developing economy.¹²⁹¹ SOCs are especially important as their performance is often mirrored in the performance of the state as the primary shareholder.¹²⁹² Ineffective corporate governance structures may result in a lack of accountability for SOCs which may negatively impact their performance.

On a worldwide stage and as result of globalization, privatization and massive corporate failures, the accountability of the board of directors has become essential. Accountability may be achieved through the implementation of effective corporate governance structures or as a standalone principle which may be achieved through other methods.¹²⁹³ South Africa, as a developing economy, and with numerous allegations of corruption can ill afford to subsidize financially underperforming SOCs who should be self-sustaining.¹²⁹⁴ Increased accountability for SOC performance may result in their improved future performance, thereby adding value to the economy instead of draining scarce state resources.¹²⁹⁵

¹²⁸⁷ Pricewaterhousecoopers 'King IV An Outcomes-Based Corporate Governance Code Fit for a Changing World' (2016) Available at <http://www.pwc.co.za/en/assets/pdf/king-iv-steering-point.pdf>, accessed 15 August 2020.

¹²⁸⁸ Deniz op cit note 1285 at 220.

¹²⁸⁹ Ibid at 221.

¹²⁹⁰ Ibid; Gubert op cit note 1266; Dzingai op cit note 1268 at 15.

¹²⁹¹ Ibid; Thabane op cit note 9 at 5.

¹²⁹² Ibid.

¹²⁹³ Deniz op cit note 1285 at 228; Gubert op cit note 1266 at 212.

¹²⁹⁴ Thabane op cit note 9 at 25.

¹²⁹⁵ Ibid; Kanyane op cit note at 32.

5.1.2 The Evolution of Corporate Governance in South Africa

The corporate governance framework in South Africa depicts a hybrid structure, comprising a combination of a regulatory, rule-based and a voluntary, principle-based, system.¹²⁹⁶ Legislation stipulates a number of governance rules for entities as well as duties for directors which are mandatory and for which a failure to comply will result in retribution.¹²⁹⁷ With the exception of companies listed on the Johannesburg Stock Exchange, for which certain provisions of the King Codes are mandatory, the application of the recommended practices in the King Codes are voluntary.¹²⁹⁸

The King Codes were first implemented with the publication of the King Report on Corporate Governance for South Africa, 1994 ('King I') followed by the King Report of Corporate Governance for South Africa, 2002 ('King II'), King III in 2009 and the most recent King IV which became effective on 1 April 2017.¹²⁹⁹ King IV replaced King III in its entirety.¹³⁰⁰ This hybrid structure of corporate governance calls for mandatory compliance with rules whilst simultaneously applying voluntary recommended practices in order to achieve good governance principles such as accountability.¹³⁰¹

The King Codes contain recommended practices which should be applied by entities to achieve the paramount principles of good governance: accountability, responsibility, transparency and fairness.¹³⁰² Application of the recommended practices has evolved from a compliance-based approach towards an outcomes-based approach focusing on the understanding and comprehension of the principles to be achieved.¹³⁰³ This shift resulted from a mindless 'tick-box' mentality which many boards adopted in their efforts to comply with the King II report.¹³⁰⁴

¹²⁹⁶ Wiese op cit note 63 at 22.

¹²⁹⁷ Ibid; Companies Act op cit note 11 at section 76 & 77.

¹²⁹⁸ Ibid Wiese at 23; JSE Limited 'Listing Requirements' available at <http://www.jse.co.za/content/JSERulesPoliciesandRegulationItems/JSE%20Listings%20Requirements.pdf>, accessed on 4 September 2020.

¹²⁹⁹ Walker op cit note 125 at 275; King III op cit note 217; King IV op cit note 19; Wiese op cit note 63 at 22; Institute of Directors Southern Africa (IODSA) *The King Report of Governance for South Africa* (1994) Johannesburg: IODSA (King I); Institute of Directors Southern Africa (IODSA) *The King Report on Governance for South Africa* (2002) Johannesburg: IODSA (King II).

¹³⁰⁰ King IV op cit note 19 at 38.

¹³⁰¹ PWC op cit note 1287 at 2.

¹³⁰² King IV op cit note 19 at 21; Wiese op cit note 63 at 2.

¹³⁰³ PWC op cit note 1287 at 2; Schulschenk op cit note 34 at 7.

¹³⁰⁴ Schulschenk op cit note 34 at 7; King II op cit note 1299; King III op cit note 217; Ramalho op cit note 1262 at 175.

In order to foster a board culture of comprehension and understanding, King IV adopted an ‘*apply and explain*’ approach in comparison to King III’s ‘*apply or explain*’ approach.¹³⁰⁵ Under the King IV approach, the board is required to apply a recommended practice and explain how such practice resulted in the achievement of the desired principle.¹³⁰⁶

King IV states that the recommended practices of corporate governance are applicable to all organisations, regardless of their nature or incorporation.¹³⁰⁷ This indicates the expansive application of the King Codes and enhances the ability of every entity, including SOCs, to actively engage in the practice of becoming a good corporate citizen.¹³⁰⁸ Proponents of corporate governance submit that good governance attracts investment to an entity, thereby promoting its long term sustainability, future growth and development.¹³⁰⁹ Therefore, the motivation in applying good corporate governance structures, despite the voluntary nature of the King Codes, lies in the future rewards to be gained by entities.¹³¹⁰

King IV does not largely depart from the objectives enshrined in King III which include: ethical leadership, integrated thinking, sustainable development and stakeholder inclusivity.¹³¹¹ However, the number of principles to apply and explain in King IV reduced to 17 from the previous 75 contained in King III.¹³¹² One of the key distinguishing features of King IV is its resolute focus on the principles of transparency and accountability which are to be achieved through the mindful application of the recommended practices.¹³¹³

King IV’s approach to corporate governance conforms to international corporate trends where mindless compliance has been relegated to the past and comprehension and understanding have come to the forefront.¹³¹⁴ King IV also dedicates specific chapters to various organisations in sector specific supplements which attempt to prevent a ‘one size fits all’ approach to corporate

¹³⁰⁵ King IV op cit note 19 at 7; King III op cit note 217.

¹³⁰⁶ Ibid; PWC op cit note 1287 at 3; Ramalho op cit note 1262 at 175

¹³⁰⁷ Ibid King IV at 35.

¹³⁰⁸ PWC op cit note 1287 at 2; Ramalho op cit note 1262 at 176.

¹³⁰⁹ Gubert op cit note 1266 at 212; Thomas op cit note 9 at 449; Thabane op cit note 9 at 8; Kanyane op cit note 10 at 29; Ramalho op cit note 1262 at 173. Dzingai op cit note 1268 at 867.

¹³¹⁰ Thomas op cit note 9 at 449; Dzingai op cit note 1268 at 867.

¹³¹¹ King IV op cit note 19 at 23; PWC op cit note 1287 at 2.

¹³¹² Ibid at 4.

¹³¹³ Ibid at 2; King IV op cit note 19 at 18.

¹³¹⁴ PWC op cit note 1287 at 3; Ramalho op cit note 1262 at 173.

governance.¹³¹⁵ Under these sector supplements, there are corporate governance recommendations which are applicable to SOCs.¹³¹⁶

5.2 The Corporate Governance of South African SOCs

The evolution of corporate governance for SOCs in South Africa has been a slow progression. The director's duties for SOCs are legislated and mandatory but corporate governance has remained a voluntary application of principles.¹³¹⁷ King IV remains the predominant source for corporate governance in South Africa and many SOC boards allege a religious application of the recommended practices.¹³¹⁸ Boards of SOCs utilise King IV as the successor to the outdated Protocol.¹³¹⁹ The effectiveness of corporate governance structures in achieving the accountability of the board of an SOC and its directors remains debatable.¹³²⁰ Given the current abhorrent state of many of our SOCs, it is arguable that the corporate governance mechanisms implemented by various SOCs have not improved their accountability.¹³²¹

5.3 The Evolution of SOC Corporate Governance

For SOCs, the application and explanation of the recommended practices for corporate governance are set out in chapter six of King IV.¹³²² King IV, echoing the sentiments of the Presidential Review Committee on State-Owned Enterprises, emphasizes the importance of good corporate citizenship of all SOEs as accelerators of national growth and development of the economy.¹³²³ The chapter six supplement under King IV applies to all SOEs including SOCs such as SAA.¹³²⁴ King I and King II contained various recommendations for which could be applied by the directors of private and public companies in South Africa, but they made no reference specifically to SOEs.¹³²⁵ The Protocol which was launched in 2002 by government is based on the contents of King I and attempted to promote the principles contained in King II but with specific application

¹³¹⁵ Ibid at 2.

¹³¹⁶ King IV op cit note 19 at 112.

¹³¹⁷ Ibid; PFMA cit note 11 at section 50 & 51; Companies Act op cit note 11 at section 76.

¹³¹⁸ SAA reports op cit note 20; Thomas op cit note 9 at 454; Thabane op cit note 9 at 12; Kanyane op cit note 10 at 32.

¹³¹⁹ Masuku op cit note 184 at 118; PRC *Protocol* op cit note 3.

¹³²⁰ Ibid; Gloeck op cit note 33 at 15.

¹³²¹ Ibid.

¹³²² King IV op cit note 19 at 111.

¹³²³ Ibid; PRC *Protocol* op cit note 3 at 1.

¹³²⁴ King IV op cit note 19 at 111.

¹³²⁵ King I op cit note 1299; King II op cit note 1299.

to SOEs.¹³²⁶ The Protocol, which is largely outdated and seldom utilized, provides a roadmap for suggesting the mechanisms to be used by SOEs in terms of the management, strategic direction and accountability of the board.¹³²⁷ Subsequent to the Protocol, the PFMA was enacted in 1999 which legislated certain duties the compliance with which became mandatory for the board of an SOC.¹³²⁸

King III took effect in 2009 and in contrast to King I and King II, it contained recommended practices which were applicable to all entities regardless of their form of incorporation.¹³²⁹ King III incorporated specific principles and practices which had been incorporated in the Protocol and were applicable to all SOEs.¹³³⁰ However, King III made no reference to SOEs in the application of its recommended practices.¹³³¹ King IV which took effect in 2017 was the first report in the series of King Codes to make specific reference to the application of recommended practices to SOEs which includes SOCs.¹³³² King IV contains a chapter dedicated to the governance of SOEs, including SOCS, which is meant to take into account the unique challenges and issues facing SOCs in large part due to the state sole shareholder.

All the principles contained in King IV apply to SOCs with the exception of principle 17 which pertains to the responsible investment of institutional investors.¹³³³ SOCs are partially or wholly owned by the state and do not have institutional investors which renders principle 17 redundant.¹³³⁴ Any organization referred to in King IV includes a reference to any SOE and SOC.¹³³⁵ Governing body members of SOCs are referred to as its '*accounting authority*' which is in line with the definition of the board of directors stipulated in the PFMA.¹³³⁶ The external auditor refers to the Auditor-General of South Africa.¹³³⁷ The shareholder is referred to as the '*executive authority*' of

¹³²⁶ PRC Protocol op cit note 3; Schulschenk op cit note 34 at 27; Parliamentary Monitoring Group, Public Enterprises Portfolio Committee 'Presentation on Corporate Governance in State-Owned Enterprises' 2002 available at <http://pmg.org.za/committee-meeting/4628/>, accessed on 4 September 2020.

¹³²⁷ PWC op cit note 70 at 7.

¹³²⁸ PFMA op cit note 11 at section 50 & 51; Schulschenk op cit note 34 at 27.

¹³²⁹ King III op cit note 217.

¹³³⁰ Ibid.

¹³³¹ Ibid.

¹³³² King IV op cit note 19 at 111; Schulschenk op cit note 34 at 4; Wiese op cit note 63 at 22.

¹³³³ Ibid King IV at 117.

¹³³⁴ Ibid at 117.

¹³³⁵ Ibid at 112.

¹³³⁶ Ibid; PFMA op cit note 11 at section 1 & 49.

¹³³⁷ Ibid at 112.

the SOC which aligns to the definition provided in the PFMA and indicates the Minister under whose portfolio SOCs fall.¹³³⁸

The principles and practices espoused in King IV, which are voluntary in nature, must be read in conjunction with the specific statutory requirements pertaining to SOCs set out in the PFMA, Companies Act and its own founding legislation.¹³³⁹ In the event of a conflict arising between the principles of King IV and the mandatory rules of legislation, legislation will prevail.¹³⁴⁰ An holistic approach to the implementation of corporate governance structures by the board of an SOC is required with reference to all of the mandatory rules and voluntary principles.¹³⁴¹

5.4 SOC Corporate Governance and Accountability

Over the last decade failing SOCs have been highlighted as their poor corporate governance coupled with a failure to account have been identified as central inhibitors to their performance.¹³⁴² Repeat offenders including Eskom, SAA and SABC are continuously reported on in media forums for their continuing poor performance, with allegations of fraud, corruption and a failure to be held accountable by the state.¹³⁴³ These SOCs are inevitably under the spotlight due to the significant impact which their financial underperformance has had on the economy.¹³⁴⁴

Despite a plethora of statutory requirements and corporate governance recommendations, these SOCs have yet to exhibit any significant measures of actual accountability for their continued dismal performance.¹³⁴⁵ As discussed in the preceding chapter, an examination of the SAA Reports illustrated a lack of accountability displayed by the board and the directors of SAA, despite apparent application of the King Codes.¹³⁴⁶ However, the last published annual integrated report of SAA, for their financial year-end on 31 March 2017, applied the recommendations set out in

¹³³⁸ Ibid; PFMA op cit note 11 at section 1.

¹³³⁹ Ibid at 114 – 115; Schulschenk op cit note 34 at 27 – 28; PFMA op cit note 11; Companies Act op cit note 11; Bronstein & Oliver op cit note 5.

¹³⁴⁰ Ibid at 115.

¹³⁴¹ Kanyane op cit note 10 at 32.

¹³⁴² Thabane op cit note 9 at 14; Terence Corrigan ‘Corporate Governance of Africa’s State-owned Enterprises: Perspectives on an Evolving System’ (2014) *The South African Institute of International Affairs* available at: <http://saiia.org.za/research/corporate-governance-in-africas-state-owned-enterprises-perspectives-on-an-evolving-system/>, accessed on 13 August 2020.

¹³⁴³ Thomas op cit note 9 at 460; Thabane op cit note 9 at 23; Kanyane op cit note 10 at 29.

¹³⁴⁴ Ibid Thabane at 12.

¹³⁴⁵ Kanyane op cit note 10 at 32.

¹³⁴⁶ SAA Reports op cit note 20; 2013 report at 10; 2014 report at 46; 2015 report at 32; 2016 report at 64; 2017 report at 28.

King III as King IV only came into effect on 1 April 2017.¹³⁴⁷ Therefore, the board of SAA was unable to apply the sector specific supplement created for SOCs by King IV which may have improved their accountability and performance.

There are many critics of King IV who argue that application of the recommended practices for good corporate governance does not necessarily result in improved accountability or performance of an entity.¹³⁴⁸ Furthermore, it may be argued that the sector supplement for SOCs in King IV does not really identify and cater for the unique challenges faced by SOCs which are largely as a result of the state being the sole shareholder. King IV focuses on the corporate governance recommendations to be applied by the board of an SOC which is the predominant body for ensuring accountability.¹³⁴⁹ However, SOCs are hamstrung in this respect as the fact of the state being the sole shareholder may have a direct impact on board's ability to actually achieve accountability under King IV.¹³⁵⁰

There are some adaptations made to the recommended practices for SOCs under King IV which act as a roadmap for good corporate governance.¹³⁵¹ King IV makes reference to the role of the state as the sole shareholder of an SOC and its reciprocal duty to hold the board to account in accordance with its constitutional obligations.¹³⁵² The state should also be transparent and effectively communicate to the board through the use of shareholder compacts.¹³⁵³ King IV also makes reference to the elevated accountability of SOCs given their status as service delivery providers on behalf of the state and, therefore, the need for accurate and transparent annual integrated reports which are available to all of their numerous stakeholders.¹³⁵⁴

¹³⁴⁷ SAA Reports op cit note 20; 2017 report at 1; King IV op cit note 19 at 38

¹³⁴⁸ Gloeck op cit note 33 at 15; Gubert op cit note 1266 at 212; Jonty Tshipa et al 'The effect of industry nuances on the relationship between corporate governance and financial performance: Evidence from South African listed companies' (2018) 21 *South African Journal of Economic and Management Sciences* 1.

¹³⁴⁹ King IV op cit note 19 at principle 6 at 114.

¹³⁵⁰ KA Mashamaite & PS Raseala 'Transgression of Corporate Governance in South Africa's State-Owned Enterprises' (2019) 16 *Bangladesh e-Journal of Sociology* 124 at 125.

¹³⁵¹ King IV op cit note 19 at 111.

¹³⁵² Ibid at principle 1 at 112 & principle 7 at 115

¹³⁵³ Ibid at principle 4 at 113.

¹³⁵⁴ Ibid at principle 3 at 113, principle 5 at 114, principle 16 at 117.

There are also key nuances relating to the disclosure, transparency and accountability of the board of an SOC which are different to those of a board of private or public company.¹³⁵⁵ Some of these nuances have been highlighted to a certain extent under King IV's sector supplement for SOCs.¹³⁵⁶

First, the state is the partial or sole shareholder for SOCs and the executive branch of government comprises a hierarchical accountability structure. This structure which commences with board of the SOC being accountable to the Minister, the Minister being accountable to Cabinet and Cabinet being accountable to Parliament.¹³⁵⁷ However, King IV does not provide guidance on the issues facing the accountability of the board of an SOC when the state becomes complacent or corrupt and fails to discharge its supervisory role and reciprocal duty to hold the board accountable.

Secondly, the state holds various stakeholder capacities in relation to an SOC and not just as the sole shareholder which is concerned with profit-maximization.¹³⁵⁸ As a policymaker, the state should oversee the implementation of certain service delivery functions by the SOC.¹³⁵⁹ As shareholder, the state should be concerned with the financial and operational performance of the SOC which may also affect its ability to perform its service delivery functions.¹³⁶⁰ As a regulator, the state should also monitor the industry practices of SOCs, their pricing structures and the interests of consumers.¹³⁶¹

These different capacities may overlap and conflict and the engagement between the board and the state is key to ensuring the fulfilment of all of the objectives of the SOC in terms of its commercial and non-commercial mandates.¹³⁶² King IV promotes the conclusion of an annual shareholder compact between the state and the board of an SOC to communicate accurate performance indicators.¹³⁶³ However, King IV fails to provide recommendations for the board of an SOC where the state fails to actively engage with it and conclude annual compacts which may hinder the ability of the board to ensure the effective fulfilment of all of the objectives of their dual mandates. It is arguable that where the state fails to actively communicate and engage with the

¹³⁵⁵ Ramalho op cit note 1262 at 175; Mashamaite op cit note 1350 at 126.

¹³⁵⁶ King IV op cit note 19 at part 6.6 at 111.

¹³⁵⁷ Ibid principle 4 at 113 & principle 16 at 117.

¹³⁵⁸ Ibid principle 16 at 117; Mashamaite op cit note 1350 at 132.

¹³⁵⁹ Ibid.

¹³⁶⁰ Ibid; principle 4 at 113.

¹³⁶¹ 117.

¹³⁶² Ibid; Mashamaite op cit note 1350 at 128.

¹³⁶³ Ibid.

board of the SOC on a regular basis, the enforcement of the accountability of the board is diluted.¹³⁶⁴

Thirdly, the board of the SOC is accountable to the public as its ultimate stakeholder due to the utilisation of taxpayer monies and as a result of the public interest mandates which are discharged on behalf of the state.¹³⁶⁵ Many SOCs are reliant on state funding to continue their operations and the state's purse is funded, in large part, through taxpayers' monies.¹³⁶⁶ This causal link results in the taxpayer becoming an 'investor' in the SOC and a stakeholder to which the board of the SOC remains accountable. Therefore, the public is a direct stakeholder of SOCs by virtue of their use of taxpayer monies and may be directly concerned with the failing status of SOCs which begets more state funding through taxpayer monies.¹³⁶⁷

King IV mentions this unique challenge for SOCs in that they are accountable to the public but does not provide any recommendations on how the board is to meaningfully engage with the public, other than by way of publishing their annual integrated reports.¹³⁶⁸ Such reports, as evident by the examination on the SAA Reports do not actually provide an accurate and up to date reflection of the status of an SOC and the public should find alternative avenues to ensure that it holds an SOC accountable for its performance.¹³⁶⁹

Unfortunately, King IV is limited in its ability to address the serious issues facing the board of an SOC where the state, as its sole shareholder and in various other stakeholder capacities, fails in its supervisory role and reciprocal duty to hold the SOC accountable. This accountability issue has been raised as one of the predominant contributing factors to the dismal financial and operational performance of SOCs over the last decade, despite their boards' application of the King Codes.¹³⁷⁰ This issue is unique to SOCs as the shareholders of private and public companies are, arguably, more concerned with losing their personal investments and are, therefore, more actively engaged

¹³⁶⁴ Mashamaite op cit note 1350 at 132.

¹³⁶⁵ King IV op cit note 19 at principle 3 at 113 & principle 5 at 114.

¹³⁶⁶ Mashamaite op cit note 1350 at 128; Makuta op cit note 205 at 67.

¹³⁶⁷ Ibid.

¹³⁶⁸ King IV op cit note 19 at principle 3 at 113 & principle 5 at 114.

¹³⁶⁹ SAA Reports op cit note 20; Kanyane op cit note 10 at 30.

¹³⁷⁰ Kanyane op cit note 10 at 32; Thomas op cit note 9 at 450; Makwethu (AGSA) op cit note 18 at 10.

in holding the board to account for the company's performance.¹³⁷¹ The state is not similarly incentivized, although it should be, to hold the board of an SOC accountable.¹³⁷²

As a result of the unique challenges facing SOCs, which are not adequately addressed by King IV, an appropriate enforcement mechanism needs to be devised which seeks to ensure the accountability of the board of an SOC.

5.5 Enforcement Mechanisms for Accountability

There are two predominant enforcement mechanisms which are generally utilised to ensure the accountability of an SOC: reward-based and retribution-based systems.¹³⁷³ Reward-based mechanisms entail incentivizing enforcement through the provision of rewards.¹³⁷⁴ A director who effectively applies the principle of accountability in his or her decision taking is rewarded.¹³⁷⁵ Retribution-based mechanisms ensure enforcement through the fear of retribution for non-compliance.¹³⁷⁶ A director who does not comply with the respective rules and regulations in his or her decision taking is punished.¹³⁷⁷ A combination of reward and retribution-based systems is often utilized in order to enforce the accountability of directors for their decision taking. The effectiveness of any enforcement mechanism, arguably, lies in its implementation.

For SOCs, their unique nature which is brought about by the state being the sole shareholder may complicate the effectiveness of any enforcement mechanism which is utilised to ensure the accountability of the board and its directors.¹³⁷⁸ A possible reform of the current enforcement mechanism, which comprises both reward and retribution-based systems, for holding directors of SOCs accountable, may be required.

5.5.1 Retribution-Based Mechanism

The effectiveness of a retribution-based enforcement mechanism lies in the fear of the imposition of punishment for non-compliance with a mandatory rule or regulation.¹³⁷⁹ It is proposed that the

¹³⁷¹ Mashmaite op cit note 1424 at 133.

¹³⁷² Ibid.

¹³⁷³ Davies op cit note 709 at 18.

¹³⁷⁴ Ibid at 17.

¹³⁷⁵ Futuregrowth op cit note 10 at 15.

¹³⁷⁶ Davies op cit note 709 at 18.

¹³⁷⁷ Futuregrowth op cit note 10 at 15.

¹³⁷⁸ Ibid at 15; Thabane op cit note 9 at 23.

¹³⁷⁹ Davies op cit note 709 at 21; Shu-Acquaye. Florence 'Corporate Governance Issues: United States and the European Union' (2007) 29 *Houston Journal of International Law* 584 at 586; Schulschenk op cit note 34 at 4.

imposition of a retribution-based system as an enforcement mechanism for accountability should include the codification of a duty to account. Directors would be required to comply with the statutory duty to account in order to avoid punishment for non-compliance. In this respect, the duty to account becomes a rule, the compliance with which is mandatory for all directors regardless of their categorization as an executive or non-executive director.

There are many benefits associated with the use of retribution as an enforcement mechanism for ensuring compliance with rules and regulations. Rules and regulations create certainty and uniformity for directors who are able easily access their statutory duties.¹³⁸⁰ The rules are contained in statutes which are readily available and directors are able to inform themselves of their requisite duties and obligations.¹³⁸¹ From a compliance perspective, adhering to a standard set of rules and regulations is less time consuming and, therefore, more cost-effective.¹³⁸²

However, there are negative aspects associated with a rule-based compliance system of enforcement for directors' duties. Rules and regulations, because of their rigidity and uniformity, are easier to circumvent than a set of principles which require comprehension in order to ensure their effective application.¹³⁸³ The systemic compliance with rules and regulations also tends to stifle innovation and flexibility and is not conducive to fostering an environment of comprehension and understanding.¹³⁸⁴

A regulated set of requirements also espouses a '*one-size-fits-all approach*' as rules are not applied based on individual circumstances but are requirements for all entities, regardless of their nature and size.¹³⁸⁵ Rules and regulations must be complied with regardless of the requirements of each individual entity and set rules may not cater for the unique board and business model of an entity.¹³⁸⁶ There have been numerous corporate governance failures where the regulatory approach was adopted such as the Sarbanes-Oxley Act in the United States.¹³⁸⁷ As a result, there has been a

¹³⁸⁰ Davies op cit note 709 at 27.

¹³⁸¹ Ibid at 28.

¹³⁸² Ibid.

¹³⁸³ Ibid at 25.

¹³⁸⁴ Bronstein & Oliver op cit note 5 at 4.; Schulschenk op cit note 34 at 4; Ramalho op cit note 1262at 178.

¹³⁸⁵ Ibid Schulschenk at 4; Florence op cit note 1379 at 586; King III op cit note 217 at 5; King IV op cit note 19 at 35; Ramalho op cit note 1262at 176.

¹³⁸⁶ Ibid Florence at 586.

¹³⁸⁷ Kirkpatrick op cit note 1275 at 63

global and fundamental shift towards understanding and comprehension as opposed to regulatory compliance.¹³⁸⁸

A plethora of statutory requirements also leads to directors resorting to a ‘tick-box’ mentality of mindless compliance with the rules and regulations without understanding their underlying nature or purpose.¹³⁸⁹ It has been suggested that this mindless compliance has led to many corporate failures where entities have alleged compliance with mandatory requirements yet failed in any event.¹³⁹⁰ Instead of ensuring that the directors actually implement good corporate governance measures, boards simply ‘tick the box’ for each requirement in order to avoid punishment without contemplating the reason behind the rule and the purpose for which it was enacted.¹³⁹¹

The main aspect for enforcement in a retributive system lies in the fear of punishment due to the possible implementation of harsh and severe retributive measures.¹³⁹² For SOC boards, a breach of the statutory duties may result in the imposition of personal or criminal liability in accordance with the provisions of the PFMA and Companies Act.¹³⁹³ The threat of imprisonment and a substantial loss of cashflow should act as deterrents for any future breaches of duties by directors. However, the actual implementation of retributive measures, regardless of their severity, is required in order to ensure their effectiveness as an enforcement mechanism.¹³⁹⁴ Directors may only be deterred from considering a breach of their duties if the imposition of personal and criminal liability is a realistic possibility as opposed to simply being perceived as an idle threat.¹³⁹⁵

Regardless of the breadth of available theoretical retributive measures, they must be consistently and continuously implemented against directors who have breached their duties to ensure their effectiveness. Without actual implementation of the statutory retributive measures against recalcitrant directors, the enforcement of their accountability is diluted. However, a careful balance needs to be achieved and courts should be wary of imposing punishment on directors as continuous

¹³⁸⁸ Sarbanes-Oxley Act, 2002, Pub L 107-204, 116 Stat 745 (2002); Florence op cit note 1379 at 586; Schulschenk op cit note 34 at 4.

¹³⁸⁹ Davies op cit note 709 at 22; Ramalho op cit note 1262at 175.

¹³⁹⁰ Ibid; Davies op cit note 709 at 25; Thomas op cit note 9 at 463.

¹³⁹¹ Ibid Davies at 26.

¹³⁹² Ibid Davies at 19; Andrew Keay et al ‘Business judgement and director accountability: a study of case-law over time’ (2020) 20 *Journal of Corporate Law Studies* 359 – 387 at 386.

¹³⁹³ PFMA op cit note 11 at section 86 (2); Companies Act op cit note 11 at section 77.

¹³⁹⁴ Keay op cit note 1467 at 385.

¹³⁹⁵ Ibid at 386.

litigation initiated against directors may completely deter persons from serving on the boards of SOCs.¹³⁹⁶

5.5.2 Reward-Based Mechanism

It is arguable that, due to its nature as a principle, accountability is predominantly implemented through voluntary application by directors and enforced through the provision of rewards in an incentive-based system. An incentive-based system works through the receipt of a possible reward as a result of the achievement of a certain goal or outcome by a director.¹³⁹⁷ The provision of bonuses and increased remuneration are the most utilized rewards for an incentive-based enforcement mechanism for the performance of executive directors.¹³⁹⁸ Whilst non-executive directors may also be rewarded with increased fees for their services, the provision of increased remuneration and bonuses is more ideally suited and proposed for the incentivisation of executive directors.

The predominant issue with a reward-based system is that it tends to lack a measure of actual implementation due to its optional or voluntary nature.¹³⁹⁹ A director may choose not to apply the principle of accountability, in his or her decision taking, thereby choosing to forgo the provision of a reward. Unlike the fear of punishment, there is no consequence for failing to apply a principle but rather the forgoing of a reward which may be easier for directors to contemplate.¹⁴⁰⁰ In order for reward-based systems to be effective as an enforcement mechanism for the accountability of directors, the incentives utilized need to be too enticing to forgo.¹⁴⁰¹

Another issue pertaining to the implementation of a reward-based enforcement mechanism is the uniform provision of rewards to all directors, regardless of their performance, targets or individual merits.¹⁴⁰² A disconnect between the performance of the director or the SOC and the provision of rewards may dilute the effectiveness of an incentive-based enforcement mechanism.¹⁴⁰³ In

¹³⁹⁶ Ibid at 359; Samet Caliskan ‘Company Liability and Competition Law: Exposure of Company to Risk of Undesirable Behaviour of Directors’ 40 *Liverpool Law Review* 1 – 29 at 25

¹³⁹⁷ Ibid; Davies op cit note 709 at 17.

¹³⁹⁸ Ibid at 20.

¹³⁹⁹ Ibid at 21; Florence op cit note 1379 at 586.

¹⁴⁰⁰ Ibid; Schulschenk op cit note 34 at 4.

¹⁴⁰¹ Viviers, Suzette ‘Executive Remuneration in South Africa: key issues highlighted by shareholder activists’ (2015) 9 *African Journal of Business Ethics* 1.

¹⁴⁰² Ibid at 2.

¹⁴⁰³ Ibid.

essence, without a causal link between the performance and the reward, directors won't be incentivized to perform.

The effectiveness of a reward-based system lies in its incentivization. If the reward is high enough there will be an incentive for the director to ensure achievement of all of his or her duties and obligations.¹⁴⁰⁴ However, as shown from the SAA Reports, if the reward is not enticing or is provided to all directors, and not merit based, there is little incentive to perform duties and fulfil obligations which often come at great personal expense.¹⁴⁰⁵ The effectiveness of a reward-based enforcement mechanism largely depends on the discretion to reward only those directors who have performed and ascertained their targeted indicators. Directors are incentivized to outperform one another and be rewarded accordingly.¹⁴⁰⁶

The common incentives utilised to enforce the performance of executive directors are the provision of increased remuneration and bonus payments.¹⁴⁰⁷ The measurement for performance must be based on a uniform, clear and achievable scorecard to ensure fairness for all directors. There should always be a link between the remuneration and bonuses given to directors and their performance as well as the performance of the entity.¹⁴⁰⁸ In the absence of such a link, the remuneration and bonuses given to executive directors may become a contentious issue between shareholders and directors.¹⁴⁰⁹

Shareholders are concerned with the growth of their investments and require transparent and fair remuneration for directors which is linked to their performance and the performance of the entity.¹⁴¹⁰ The performance of the entity is increasingly thought to include not only financial performance but operational performance and maximizing shareholder wealth in a socially responsible manner.¹⁴¹¹ In the event that the entity performs poorly over a number of years, activist

¹⁴⁰⁴ Ibid.

¹⁴⁰⁵ SAA Reports op cit note 20; 2013 report at 124; 2014 report at 146, 2015 report at 130 & 143, 2016 report at 163, 2017 report at 165.

¹⁴⁰⁶ Ibid at 4; Davies op cit note 709 at 8.

¹⁴⁰⁷ Ibid at 1.

¹⁴⁰⁸ Viviers op cit 1401 at 1; Davies at 20.

¹⁴⁰⁹ Davies at 4; Nirupa Padia & Chris Callaghan 'Executive director remuneration and company performance: panel evidence from South Africa for the years following King III' (2020) *Personnel Review* 1.

¹⁴¹⁰ Viviers op cit note 1401 at 3.

¹⁴¹¹ Elize Kirsten & Elda Du Toit 'The relationship between remuneration and financial performance for companies listed on the Johannesburg Stock Exchange' (2018) 21 *South African Journal of Economic and Management Sciences* 1 at 8.

shareholders may vote against increased remuneration or the provision of bonuses for directors.¹⁴¹² The board of an entity should always ensure that it is accountable for any remuneration or bonus policy involving the directors and should establish a remuneration committee for this purpose.¹⁴¹³

It is further submitted that another issue for the reward-based mechanism is the time consuming and, therefore, costly application of principles.¹⁴¹⁴ The application of a principle requires understanding and comprehension by the director which may be a more burdensome task than simply complying with uniform rules and regulations.¹⁴¹⁵ Many entities do not have adequate resources for directors to spend time comprehending and applying principles. The capacity of directors and their ability to understand and comprehend the purpose of a principle may also be a barrier to their application.¹⁴¹⁶ Hence, the necessity for a minimum set of qualifications for director appointments which are set by a nominations committee.¹⁴¹⁷

It is submitted that the possible solution to these issues is to compile a set of principles which are simple and easy to apply and which do not comprise an overly exhaustive list of recommended practices.¹⁴¹⁸ Directors should undergo training to ensure that they understand the principle which the entity is attempting to achieve without resorting to the application of numerous recommended practices in a ‘tick-box’ fashion.¹⁴¹⁹ A mindless application of principles simply replaces mindless compliance with the rules. The result remains the same in both instances, a failure by directors to comprehend and understand the rule or principle that they are trying to comply with or to apply will dilute their accountability.

5.6 SOC Enforcement Mechanisms

The enforcement mechanism for ensuring the accountability of the board of an SOC and its directors comprises components of reward and retribution-based systems.¹⁴²⁰ Directors of SOCs are held accountable through statutory duties which are contained in the PFMA, the Companies

¹⁴¹² Ibid.

¹⁴¹³ King IV op cit note 18 at 31; Padia op cit note 1409 at 3.

¹⁴¹⁴ Florence op cit note 1379 at 586.

¹⁴¹⁵ Ibid.

¹⁴¹⁶ Davies op cit note 709 at 22.

¹⁴¹⁷ Viviers op cit note 1401 at 6.

¹⁴¹⁸ Gloeck op cit note 33 at 16.

¹⁴¹⁹ Ramalho op cit note 1262 at 174.

¹⁴²⁰ Thabane op cit note at 9; Futuregrowth op cit note 10 at 38; Dullah op cit note 190 at 1

Act and their own founding legislation.¹⁴²¹ Any failure to comply with any statutory duty may result in retribution being levied against the director in the form of personal or criminal liability.¹⁴²²

Directors of SOCs are also encouraged to practice sound corporate governance and achieve the principle of accountability through applying the recommended practices in the King IV.¹⁴²³ It is conceivable that application of the principles should result in the improved performance of the SOC for which the executive directors may be rewarded, through the provision of increased remuneration and bonus payments. However, the performance of the SOC should always be reflected in the remuneration of the directors and there should always be a positive correlation between the remuneration of the directors and the performance of the SOC.¹⁴²⁴

The disclosure of remuneration for directors in the annual financial statements of the SOC is a statutory requirement.¹⁴²⁵ The remuneration for SOC directors must also be approved by a special resolution of the shareholder, which will be the state, every two years.¹⁴²⁶ These mechanisms are mandatory in order to prevent the board of an SOC from excessively remunerating the directors without having regard to their performance or the profitability, sustainability, growth and performance of the SOC.¹⁴²⁷ King IV also recommends the implementation by the board of a fair, responsible and transparent remuneration policy which promotes the strategic growth and performance of the SOC.¹⁴²⁸

The enforcement of accountability through the fulfilment of statutory duties, lies in the fear of possible retribution for non-compliant SOC boards.¹⁴²⁹ The enforcement for an application of the principle of accountability by the board of an SOC is incentivization through the provision of rewards.¹⁴³⁰ Despite the presence of both retribution and reward-based enforcement mechanisms, SOCs still exhibit a chronic lack of accountability.¹⁴³¹ It is submitted that the enforcement of the

¹⁴²¹ Ibid at 10; PFMA op cit note 11 at section 50 & 51; Companies Act op cit note 11 at section 76.

¹⁴²² Ibid at section 86 (2); Ibid at section 77.

¹⁴²³ King IV op cit note 19; Thabane op cit note 9 at 10; Futuregrowth op cit note 10 at 16; Dullah op cit note 190 at 1; Thomas op cit note 9 at 450.

¹⁴²⁴ Bezuidenhout op cit note 31.

¹⁴²⁵ Wiese op cit note 63 at 61; Companies Act op cit note 11 at section 30 (4)(a).

¹⁴²⁶ Ibid at section 66 (9).

¹⁴²⁷ Bezuidenhout op cit note 31 at 12.

¹⁴²⁸ King IV op cit note 19 at principle 14 at 116.

¹⁴²⁹ Thabane op cit note 9 at 10.

¹⁴³⁰ Bezuidenhout op cit note 31 at 13; Futuregrowth op cit note 10 at 38.

¹⁴³¹ Thabane op cit note 9 at 14; Dullah op cit note 190 at 3 – 4.

retribution and reward-based systems in the actual levying of punishment and the provision of merit-based rewards is one of the greatest hurdles for the accountability of SOCs.

5.6.1 Retribution-Based Mechanism Failures

Currently, the predominant enforcement mechanism against SOC boards, its individual directors and the Minister seems to be retribution-based in the levying of punishment. The former chairperson of SAA has been declared a delinquent by the court and the board of Eskom have been taken to court on delinquency applications brought by Corruption Watch.¹⁴³² The court has also held two of the directors of SABC personally liable for the costs of an application brought against them for failing to discharge their statutory duties.¹⁴³³ The Eskom board has also been taken to court on allegations of a breach of the fiduciary duties owed to the SOC.¹⁴³⁴ The conduct of the Minister and the Minister of Communications has also been scrutinized by the courts for failing to discharge their constitutional accountability obligation and failing to perform their supervisory role over the boards of Eskom and SABC, respectively.¹⁴³⁵

In the abovementioned cases, the board of the SOC was not the applicant which sought an order against itself, its directors or the Minister. Similarly, the Minister, as the executive authority responsible for ensuring the compliance by the board of an SOC with the provisions of the PFMA, was not the applicant which brought a claim against the board or its directors. Private institutions, OUTA and Corruption Watch and the opposition party, the Democratic Alliance were the interested parties which sought to bring claims against SOC boards and directors for a breach of their duties and the imposition of retribution.¹⁴³⁶ These cases are also very few in number given the underperformance of SOCs over the last couple of years which may be attributed to a lack of resources for private institutions and the opposition party in for instituting court proceedings against SOC boards and their directors.

Precedent has been set by the courts in the ABI and Steinhoff cases that it should be the company itself which institutes proceedings against directors to hold them liable for a breach of their duties which causes the company to suffer a loss.¹⁴³⁷ Following this precedent, the board of an SOC

¹⁴³² *OUTA v Myeni* case supra note 346; Corruption Watch op cit note 1269.

¹⁴³³ *SABC* case supra note 167 para 225.

¹⁴³⁴ *Eskom* case supra note 1191 para 15.

¹⁴³⁵ *Ibid* para 80; *Ibid* para 60.

¹⁴³⁶ *SABC* case supra note 167; *Eskom* case supra note 1191; *OUTA v Myeni* case supra note 346.

¹⁴³⁷ *Hlumisa* case supra note 309 para 1; *De Bruyn* case supra note 353 para 180

should hold its directors liable for a breach of their duties which causes a loss to be suffered by the SOC. In the case against Myeni, the board of SAA should have been the interested party which sought to declare her a delinquent or hold her personally or criminally liable for a breach of her duties to SAA. Failing institution by the board, the Minister should be authorised as the executive authority to pursue a claim against recalcitrant SOC boards and directors.

However, it seems that the boards of SOCs are reluctant to investigate, impose sanctions, institute dismissal proceedings or institute court applications against directors who are alleged to have committed a grossly negligent breach of their duties under the PFMA.¹⁴³⁸ The PFMA also does not authorize the imposition of criminal liability against the board of an SOC by the Minister and only requires that the Minister table findings or sanctions against boards for financial misconduct with the National Assembly.¹⁴³⁹ The Auditor-General should also utilise the extended powers afforded to him under the PAAA to issue certificates of debt so that the Minister is able to recover certain debt amounts from the board of an SOC due to its failure to implement remedial action stipulated by the Auditor-General.¹⁴⁴⁰

It would appear that the statutory retribution mechanisms are not being sufficiently utilised against SOC boards and directors whether by board itself, the Minister, the Auditor-General or through court applications by interested third parties. Given the dismal performance of SOCs and their numerous disclaimed audit findings from the Auditor-General, an argument can be made that retribution should be sought against many more SOC boards and directors on the basis of a breach of their statutory duties.¹⁴⁴¹ As was illustrated by an examination of the SAA Reports, the board has never dismissed any of its directors despite failing to submit annual financial statements for the last two of its year-ends which may constitute a grossly negligent breach of the statutory duties.¹⁴⁴²

Furthermore, none of the SAA directors have been taken to court by the board to hold them liable for breaching their duties which should be evident due to the qualified audit opinion given by the Auditor-General for SAA's 2017 financial year-end.¹⁴⁴³ Unfortunately, the board of SAA could

¹⁴³⁸ PFMA op cit note 11 at section 83 (4) & 84.

¹⁴³⁹ Ibid at section 63 (2) & 65 (1)(b).

¹⁴⁴⁰ PAAA op cit note 647.

¹⁴⁴¹ Makwethu (AGSA) op cit note 18 at 115.

¹⁴⁴² SAA reports op cit note 20.

¹⁴⁴³ SAA 2017 report op cit note 20 at 98 – 105.

not be held liable by the Minister, as directed by the Auditor-General, to recover debt in terms of the PAAA which only came into force on 1 April 2019 with the last published audited financial statements of SAA being for the 2017 year-end and SAA going into business rescue in December 2019.¹⁴⁴⁴

It is possible that as a result of complacency and corruption, the state has failed to ensure the effective implementation of the statutory retribution measures by the board of an SOC against its directors who are alleged to have breached their duties and failed to comply with their statutory obligations.¹⁴⁴⁵ The board of an SOC may also be politically influenced by a corrupt state, as its sole shareholder, to withhold the institution of any sanctions against its directors. Without the actual implementation of these retributive measures, the enforcement of accountability for the fulfilment of statutory duties and obligations for the board of an SOC and its directors is completely negated.¹⁴⁴⁶

5.6.2 Reward-Based Mechanism Failures

Remuneration and bonus payments for executive directors are the predominant forms of rewards and are readily utilised as incentives to enforce the accountability of directors.¹⁴⁴⁷ The issue with the provision of rewards as an incentive-based mechanism is that it may become redundant if the provision of the reward is not based on the performance of the director and the SOC.¹⁴⁴⁸ This issue was evident in the SAA Reports where the executive directors received increased remuneration and bonus payments every year despite the record annual losses sustained by the SOC.¹⁴⁴⁹

Claw-backs of executive director bonus payments have been suggested as a resolution to this issue, however the claw-back system may prove difficult to implement.¹⁴⁵⁰ If the director has already spent the bonus monies then court proceedings will have to be instituted by the company in order to claim repayment which is an expensive and timely process.

¹⁴⁴⁴ PAAA op cit note 647.

¹⁴⁴⁵ Davies op cit note 709 at 21; Dullah op cit note 190 at 38; Kanyane op cit note 10 at 30.

¹⁴⁴⁶ Ibid.

¹⁴⁴⁷ King IV at 14 at 64 – 67; Bezuidenhout op cit note 31 at 13.

¹⁴⁴⁸ Ibid; Makoni op cit note 13 at 16.

¹⁴⁴⁹ SAA Reports op cit note 20; 2013 report at 124; 2014 report at 146, 2015 report at 130 & 143, 2016 report at 163, 2017 report at 165.

¹⁴⁵⁰ Futuregrowth op cit note 10 at 14.

Shareholder activism is possibly the cheaper and less time-consuming method to ensure the presence of a link between the performance the company and the director and the provision of reward.¹⁴⁵¹ Shareholder activists assist in attempting to prevent this possible enforcement issue for private and public companies.¹⁴⁵² Especially for JSE listed companies, activist shareholders who are determined to protect their investments may influence the provision of remuneration and bonus payments for executive directors and the fees for non-executive directors.¹⁴⁵³ Through various methods including: writing letters, engaging with management, voting against resolutions, divesting of shares or enforcing their statutory rights, shareholders are able to voice concerns surrounding rewards which may be provided to directors regardless of their, or the company's, performance.¹⁴⁵⁴

Institutional investors, who have more of an effect than individual investors, are guided in becoming activist shareholders in South Africa through the implementation CRISA.¹⁴⁵⁵ Although not as vocal as they could be, institutional investors in South Africa have a platform for influencing board decision taking in companies in which they are major shareholders.¹⁴⁵⁶ The reputational effects which a divestment of shares by a major institutional shareholder can have on a JSE listed company can be catastrophic.¹⁴⁵⁷ In the premise, the directors of JSE listed companies are encouraged to remain conscious of ensuring their continued performance and to take the concerns of institutional investors seriously, especially when it comes to executive remuneration and bonus payments.¹⁴⁵⁸

However, shareholder apathy is still a huge issue for attempting to utilize shareholder activism to ensure that remuneration, fees and bonus payments act as an effective incentive and reward-based enforcement mechanism for the accountability of directors.¹⁴⁵⁹ Despite the various available methods, shareholders cannot be forced to become active and voice their concerns with the

¹⁴⁵¹ Viviers op cit note 1401 at 4.

¹⁴⁵² Ibid.

¹⁴⁵³ Ibid at 2.

¹⁴⁵⁴ Ibid at 3.

¹⁴⁵⁵ IODSA CRISA op cit note 492.

¹⁴⁵⁶ Viviers op cit note 1401 at 8.

¹⁴⁵⁷ Davies op cit note 709 at 22.

¹⁴⁵⁸ Viviers op cit note 1401 at 8; Davies op cit note 709 at 22.

¹⁴⁵⁹ Thabane op cit note 9 at 25; Bezuidenhout op cit note 31 at 12.

remuneration of directors and the performance of the company. Complacent shareholders are not motivated to hold the board of company accountable for its remuneration policy.

For SOCs, the shareholder apathy issue stems from the fact that the state is the sole shareholder.¹⁴⁶⁰ There is no code for responsible investing for the state and most of the shareholder activist's methods available to private and public shareholders are not available for the state as the sole shareholder of the SOC.¹⁴⁶¹ The state can only divest shares to a willing purchaser once the SOC has become privatized. With the baggage of a non-commercial mandate, many SOCs will not find a willing purchaser.

The state can vote against a resolution by the directors but as the sole shareholder there are no other shareholders to provide a check against excessive remuneration and bonus packages which are authorized by the state, as sole shareholder.¹⁴⁶² If the state has made political appointments to the board of an SOC it is unlikely that it will vote against board resolutions to increase director remuneration and bonus packages.¹⁴⁶³ As is evident from the SAA Reports where former chairperson Myeni was paid excessively high director fees, given her status as a non-executive director and the dire performance of SAA during her tenure on the board.¹⁴⁶⁴ It is arguable that the excessively high fees for the former chairperson may have resulted from her close links to the former president, Jacob Zuma.

The Department of Public Enterprises also published a remuneration guideline for executive and non-executive directors of SOCS in 2007 which was recently revised in 2018 by the National Treasury.¹⁴⁶⁵ The guideline was meant to assist boards of SOCs with their remuneration policies and link the performance of the SOC to the remuneration and fees of the directors.¹⁴⁶⁶ However,

¹⁴⁶⁰ Makoni op cit note 13 at 18.

¹⁴⁶¹ Thabane op cit note 9 at 10; Futuregrowth op cit note 10 at 8.

¹⁴⁶² BusinessTech 'CEO vs Employee salaries at Eskom, SAA and other state companies' 24 August 2017 available at <http://businesstech.co.za/news/wealth/194164/ceo-vs-employee-salaries-at-eskom-saa-and-other-state-companies/>, accessed on 7 September 2020.

¹⁴⁶³ Thabane op cit note 9 at 24.

¹⁴⁶⁴ SAA 2014 report op cit note 20 at 80.

¹⁴⁶⁵ Department of Public Enterprises (DPE) 'State-Owned Enterprises Remuneration Guidelines' (2007) available at http://www.gov.za/sites/default/files/gcis_document/201409/seo-remuneration0.pdf, accessed on 7 September 2020; National Treasury '2018 Adjustment of Remuneration Levels' (2018) available at <http://www.treasury.gov.za/legislation/pfma/renumerative/2018%20Cir%20-%20Rem%20Stat%20&%20Other%20Inst.pdf>, accessed on 7 September 2020.

¹⁴⁶⁶ Ferina Marimuthu & Farai Kwenda 'The Relationship between Executive Remuneration and Financial Performance in South African State-Owned Entities' (2019) 23 *Academy of Accounting and Financial Studies Journal* 1 – 9.

many SOCs such as SAA do not adopt these guidelines and have been the subject of intense public and media scrutiny for allowing the excessive remuneration of their directors which is not linked to the performance of the SOC.¹⁴⁶⁷

King IV states that the recommended practices provided for the remuneration of directors of public and private companies are to be applied for SOCs, without variation.¹⁴⁶⁸ One of the primary recommended practices for fair and reasonable executive director remuneration is the approval of the remuneration policy by the shareholders of the company at an annual general meeting.¹⁴⁶⁹ In the event of 25 per cent or more dissenting votes by those shareholders entitled to exercise voting rights for approving the remuneration policy, the board is required to engage with the dissenting voters.¹⁴⁷⁰ The board is required to ascertain reasons for the dissenting votes and to address the legitimate and reasonable concerns which are raised in connection with the remuneration policy.¹⁴⁷¹

This recommended practice of shareholder approval and engaging with dissenting shareholders is superfluous for SOCs where the state is the sole shareholder. Application of this recommended practice without variation by the board of an SOC whose sole shareholder is the state will not assist in curbing unreasonably high executive director remuneration and fees for non-executive directors. King IV contains no resolutions to this issue where the state is the sole shareholder and fails to effectively supervise the board's remuneration policy which is meant to be linked to the performance of the SOC. Furthermore, King IV does not provide any additional recommended practices to ensure fair, responsible and transparent remuneration policies which are specific to SOCs and which may account for the eventuality of a corrupt and complacent shareholder.

It is submitted that the board of an SOC should adopt the remuneration guidelines provided by the Department of Public Enterprises, however, the guideline requires amendment prior to its implementation. The current guideline uses the size of the SOC to determine the appropriate remuneration and incentive packages for the executive directors.¹⁴⁷² The size of the SOC is determined with reference to the annual revenue generated and the asset base.¹⁴⁷³ The guideline

¹⁴⁶⁷ Ibid at 3; Bezuidenhout op cit note 31 at 13.

¹⁴⁶⁸ King IV op cit note 19 at principle 14 at 64 - 7 & 116.

¹⁴⁶⁹ Ibid.

¹⁴⁷⁰ Ibid.

¹⁴⁷¹ Ibid.

¹⁴⁷² DPE op cit note 1465 at 6.

¹⁴⁷³ Ibid.

also requires that the remuneration policy illustrate a clear link between the remuneration of the directors and the performance of the director and the SOC.¹⁴⁷⁴ Any deviation from the set packages by the board of an SOC must be met with prior approval from the Minister, as the executive authority.¹⁴⁷⁵

It is submitted that the generation of revenue and the size of its asset base are not clear indicators of the SOC's affordability in light of its remuneration policy for directors. The thresholds for director remuneration should be linked to the performance of the SOC, the performance of the director and the cashflow of the SOC.¹⁴⁷⁶ The performance of the SOC should be determined not only from a financial perspective but also with reference to the sustainability, social responsibility, economic, environmental and operational attributes of the SOC.¹⁴⁷⁷ The performance of the director may include: evaluations on the contributions made by the director to the SOC, the accountability, transparency and responsibility exhibited by the director in his or her decision taking, the discharging of his or her duties and his or her overall attendance and input at board meetings.

The remuneration committee of an SOC will devise a performance and remuneration and fee scorecard for directors, based on the aforesaid criteria, which will form part of the remuneration policy. The remuneration and bonus package amounts for the executive directors in the remuneration policy will accord to the maximum thresholds set by the remuneration guideline issued by the Department of Public Enterprises, with the suggested amendments. The remuneration policy of the SOC should adopt the revised guideline issued by the National Treasury in 2018 for the payment of the fees for the non-executive directors. Any deviation from its own remuneration policy by the board of an SOC will require prior approval from the state and the state will be required to justify its approval to Parliament and if necessary, the Auditor-General.

As an avenue of last resort, the taxpayers may become the activist stakeholders of the SOC where the state fails to ensure the implementation of fair and responsible remuneration for executive directors.¹⁴⁷⁸ Evident from various media reports, the public has activated its role in the supervision of executive remuneration and bonus payments for underperforming boards of

¹⁴⁷⁴ Ibid at 8 – 9.

¹⁴⁷⁵ Ibid.

¹⁴⁷⁶ Marimuthu op cit note 1466 at 9; Bezuidenhout op cit note 31 at 2.

¹⁴⁷⁷ Ibid.

¹⁴⁷⁸ BusinessTech op cit note 1462.

SOCs.¹⁴⁷⁹ Public outrage followed announcements of continued bonus payments being provided to the boards of SAA and Eskom.¹⁴⁸⁰ These SOC's are financially underperforming and the provision of rewards for their board of directors is counterintuitive.¹⁴⁸¹

The primary factor for the remuneration policy of an SOC is to align the remuneration, fees and bonus packages for directors with the performance of the director and the SOC.¹⁴⁸² This alignment will attempt to ensure that the remuneration policy contains incentives for directors in achieving strategic objectives and performance indicators which promotes the long-term sustainability of the SOC.¹⁴⁸³ As a criterion for the assessment of the directors performance, a director will be incentivized to achieve accountability in his or her decision taking in order to receive the highest possible remuneration or fee package. Without the presence of a link between a director's remuneration or fee and the performance of the SOC, this reward-based enforcement mechanism for ensuring the accountability of the board and its directors will prove ineffective.¹⁴⁸⁴

5.7 Paving the way to Enforceable Accountability

The theoretical retributive measures which are meant to enforce the accountability of directors of SOC's are underutilized, thereby drastically impeding their effectiveness.¹⁴⁸⁵ In addition, the absence of a link between the performance of the director and the SOC and the remuneration, fees and bonus payments dilutes the effectiveness of this reward-based enforcement mechanism for accountability.¹⁴⁸⁶ Therefore, despite the combination of retribution and reward-based measures the enforcement of accountability for the board of an SOC and its directors is still considered a governance mirage.¹⁴⁸⁷

The effectiveness of the recommended practices provided by King IV are debatable in their ability to achieve the actual accountability of the board of an SOC and its directors.¹⁴⁸⁸ Given the dismal

¹⁴⁷⁹ Ibid.

¹⁴⁸⁰ Mzilikazi Wa Afrika 'SAA executive salaries slammed as airline struggles with financial woes' IOL 17 November 2019 available at <http://www.iol.co.za/sundayindependent/news/saa-executive-salaries-slammed-as-airline-struggles-with-financial-woes-37360595>, accessed on 7 September 2020.

¹⁴⁸¹ Makoni op cit note 13 at 18.

¹⁴⁸² Bezuidenhout op cit note 31 at 12; Marimuthu op cit note 1466 at 9; King IV op cit note 19 at principle 14 at 66.

¹⁴⁸³ Ibid.

¹⁴⁸⁴ Ibid; Makoni op cit note 13 at 18.

¹⁴⁸⁵ Dullah op cit note 190 at 38.

¹⁴⁸⁶ Bezuidenhout op cit note 31 at 12.

¹⁴⁸⁷ Fourie op cit note 167 at 39; Futuregrowth op cit note 10 at 39; Kanyane op cit note 10 at 8; Thabane op cit note 9 at 24; Thomas op cit note 9 at 454; Makoni op cit note 13 at 23; Moloji op cit note 905 at 3.

¹⁴⁸⁸ Gloeck op cit note 33.

performance of many SOCs over the last decade it is arguable that an application of the recommended practices may not necessarily result in the achievement of meaningful accountability.

In its last published annual report for its 2017 financial year-end, the board of SAA confirmed its consistent and continued application of the King III recommended practices.¹⁴⁸⁹ Notwithstanding the application of these practices, SAA announced its voluntary entry into business rescue proceedings in 2019.¹⁴⁹⁰ It is argued that the link between the accountability of directors of SOCs and the application of the King Codes has deteriorated, as illustrated by the examination of the SAA Reports. However, it has yet to be uncovered whether the King Codes were actually ever applied by the board of SAA despite its statements to the contrary.

In the premise, a new enforcement framework, which is still based on elements of the retribution and reward-based mechanisms with slight variations, is proposed to ensure the accountability of the directors of SOCs. Under this framework, the reward-based mechanism will be altered to ensure the adoption of a remuneration policy by the board of an SOC which links the provision of remuneration, fee and bonus packages to the performance of the director and the SOC. The current, theoretical retributive measures for punishing recalcitrant SOC directors may also need to undergo reform in order to improve their effectiveness under this novel enforcement framework. Concurrently with the revised retribution measures, the outcome of the Zondo Commission should result in criminal and personal liability being levied against many more SOC directors who are found guilty of committing criminal acts or breaching their duties.¹⁴⁹¹

The details of this framework are set out in the next chapter which include the variations proposed to the current retribution and reward-based mechanisms for holding SOCs accountable. In addition, the framework will suggest innovative proposals with regards to the enactment of certain legislation and corporate governance reform to ensure not just the accountability but the enforceable accountability of SOCs.

¹⁴⁸⁹ SAA report 2017 op cit note 20 at 2.

¹⁴⁹⁰ SAA op cit note 18.

¹⁴⁹¹ Dirk Brand 'The Seven Things New Leaders Need to do to fix South Africa' ENCA 27 May 2019 available at <http://www.enca.com/analysis/seven-things-new-leaders-need-do-fix-south-africa>, accessed on 7 September 2020.

5.8 Conclusion

Currently, the principle of accountability is predominantly achieved through the implementation of corporate governance structures by the board of an SOC. In order to enforce accountability of the board, various retribution and reward-based mechanisms are available for implementation. However, these current mechanisms have proven ineffective in actually enforcing the accountability of the board of an SOC, as was illustrated through an examination of the SAA Reports in the preceding chapter.

It is submitted that this lack of enforceable accountability may have contributed to the poor performance of an SOC, such as SAA, over the last decade. It is proposed that accountability may be achieved through the implementation of corporate governance structures or as a standalone principle, depending on the nature, structure and business model of the specific SOC. It is further proposed that the enforcement of accountability should be implemented with a framework comprising elements of the current retribution and reward-based mechanisms, however, with some suggested material variations.

CHAPTER SIX: ENFORCEABLE ACCOUNTABILITY FOR SOCS

6 Introduction

The proposed framework for the implementation of enforceable accountability for SOCs is twofold. First, the statutory reform for SOCs which entails the enactment of an overarching SOE Legislation, as previously proposed by the Presidential Review Committee on State-Owned Entities and a proposed Rating Agency Act. The overarching SOE Legislation will govern all aspects relating to SOEs, including SOCs. The Rating Agency Act will establish an independent state institution to annually rate the accountability of SOEs, including SOCs. The Rating Agency Act will stipulate that the rating of the SOC must be carried out annually based on a scorecard with uniform categories and the outcome of the rating will be linked to the provision of state funding to the SOC.

Secondly, the board of an SOC will have the discretion to implement any method or mechanism, of which corporate governance is just one, to achieve the principle of accountability. Therefore, accountability will remain a voluntary application for the board of an SOC. The failure of an SOC, such as SAA, to achieve accountability, despite alleged compliance by the board with its statutory duties coupled with the ineffectiveness of the implementation of retribution, in the event of non-compliance, was a primary factor for the proposal that accountability remain a voluntary principle which the board of an SOC is incentivised to achieve through the implementation of a mainly reward-based mechanism. The board will be incentivized to achieve accountability as the provision of state funding to the SOC will be determined based on the outcome of the rating.

6.1 The Solution: Enforceable Accountability

The degree to which the board of an SOC is held accountable is dependent on the enforcement mechanism utilised to ensure the achievement of accountability. The lack of an effective enforcement mechanism will dilute the need for the board of an SOC to account for its performance to the Minister. Enforcement mechanisms are generally found in the form of a retributive or reward-based approach.¹⁴⁹² Despite a plethora of regulatory compliance obligations for the boards of SOCs, accountability is a principle which is mainly constructed on an approach based on voluntary application.¹⁴⁹³

¹⁴⁹² Davies op cit note 709 at 18.

¹⁴⁹³ King IV op cit note 19 at principle 6 at 114.

The current accountability measures in place for the board of an SOC depict a hybrid approach straddling elements of both a regulatory and voluntary nature. The board and the directors of an SOC are currently required to comply with their statutory duties and voluntarily apply the recommended practices of corporate governance under King IV.¹⁴⁹⁴ Compliance by the board and the directors with the statutory duties combined with the voluntary application of corporate governance practices are meant to ensure the accountability of an SOC.¹⁴⁹⁵

As illustrated through an examination of the SAA Reports, the actual accountability of SAA is virtually non-existent despite the alleged implementation of King IV and compliance with the statutory duties and obligations by the board and its directors.¹⁴⁹⁶ Attributable to a multitude of failures, SOCs continue to underperform on a financial and operational level which puts the economy at risk, given the important role played by SOCs as custodians of national assets and potential facilitators of national growth and development.¹⁴⁹⁷

The issue of theoretical accountability, without substantial and real accountability, may be resolved through the implementation of an appropriate enforcement mechanism. Distinguishing between accountability and enforceable accountability may result in the improved performance of SOCs by virtue of the implementation of an effective governance mechanism, practice or structure.

6.2 Rating Agencies for Corporate Governance

Corporate Governance rating agencies have become a popular method for enforcing the accountability of directors, in response to numerous, worldwide corporate governance failures.¹⁴⁹⁸ In the private sector, companies which are listed on stock exchanges make use of rating agencies in order to calculate the effectiveness of their corporate governance structures.¹⁴⁹⁹ The link between a company's good corporate governance and its performance is a hotly debated topic.¹⁵⁰⁰

¹⁴⁹⁴ Ibid; PFMA op cit note 11; Companies Act op cit note 11.

¹⁴⁹⁵ Makuta op cit note 205 at 61.

¹⁴⁹⁶ SAA reports op cit note 20.

¹⁴⁹⁷ Makwethu (AGSA) op cit note 18 at 10; National Treasury op cit note 1 at 90; Makoni op cit note 13 at 21. Futuregrowth op cit note 10 at 4; Kanyane.op cit note 10 at 5; Thomas op cit note 9 at 448.

¹⁴⁹⁸ Madan Bhasin 'Corporate Governance Rating Systems: A Powerful Tool of Accountability' (2008) 1 *Indian Journal of Corporate Governance* 1; Han Donker & Saif al Zahir 'Towards and Impartial and Effective Corporate Governance Rating System' (2008) 8 *Corporate Governance International Journal of Business in Society* 83-93 at 83; Mine Ertugrul & Shantaram Hedge 'Corporate Governance Ratings and Firm Performance' (2009) 38 *Wiley Financial Management Association International* 139 at 139.

¹⁴⁹⁹ Ibid Bhasin at 1.

¹⁵⁰⁰ Ibid; Gloeck op cit note 33; Makoni op cit note 13 at 23; Donker op cit note 1498 at 86.

The ongoing debate revolves around the fact that a company's practicing of effective corporate governance does not always necessarily result in its improved performance or that it is difficult to establish a clear causal link between the two.¹⁵⁰¹ However, it is submitted that a correlation should exist between good corporate governance, including accountability and the performance of a company based on the agency theory.¹⁵⁰² Each company must balance the costs associated with effective corporate governance structures with its perceived benefits in order to decide on its implementation.

Notwithstanding the ongoing debate on the link between good corporate governance and company performance, the accountability of directors is always of paramount consideration.¹⁵⁰³ The more accountable the directors, the more confidence that existing and future investors will have in the performance of the company.¹⁵⁰⁴ Companies therefore utilize the outcome of the corporate governance rating, if favourable for accountability, as a way of attracting potential future investors and providing security and comfort to existing investors.¹⁵⁰⁵ The publicity of the ratings outcome remains at the discretion of the company and in most jurisdictions an annual governance rating is not a regulatory requirement for companies.¹⁵⁰⁶

There are various methodologies and rankings which are used by the different rating agencies, the majority of which are largely based on the overarching principles of corporate governance. These principles are akin to those set out in King Codes: transparency, accountability, responsibility and fairness.¹⁵⁰⁷ The four most globally recognized firms which conduct governance ratings are: The Institutional Shareholder, Standard & Poor's, Governance Metric International and the Corporate Library.¹⁵⁰⁸

¹⁵⁰¹ Ibid Donker at 87; Ruth Epps & Sandra Cereola 'Do Institutional Shareholder Services (ISS) corporate governance ratings reflect a company's operating performance?' (2008) 19 *Critical Perspectives on Accounting* 1135-1148 at 1135; Robert Daines et al 'Rating the ratings: How good are commercial governance ratings?' (2010) 98 *Journal of Financial Economics* 439 – 461 at 440; Ertugrul op cit note 1498 at 139.

¹⁵⁰² Annelies Renders et al 'Corporate-Governance Ratings and Company Performance: A Cross European Study' (2010) 18 *Corporate Governance, An International Review* 2 at 100; Amir Louizi & Radhouane Kammoun, 'Evaluation of Corporate Governance Systems by Credit Rating Agencies' (2016) 20 *Journal of Management Governance* 363; Epps op cit note 1501 at 1137.

¹⁵⁰³ Gloeck op cit note 33; Makoni op cit note 13 at 23; Futuregrowth op cit note 10 at 29; Epps op cit note 1501 at 1137; Thomas op cit note 9 at 450.

¹⁵⁰⁴ Ibid.

¹⁵⁰⁵ Bhasin op cit note 1498 at 1; Epps op cit note 1501 at 1137.

¹⁵⁰⁶ Ibid at 2.

¹⁵⁰⁷ King III op cit note 217 at 7; King IV op cit note 19 at principle 1 at 43 – 44; Bronstein & Oliver op cit note 5 at 43; Daines op cit note 1501 at 461.

¹⁵⁰⁸ Bhasin op cit note 1498 at 2; Donker op cit note 1498 at 88.

It is submitted that the best rating methodology which should be utilised by all of these rating agencies is twofold. First, a rating should be done on a particular country's approach to corporate governance.¹⁵⁰⁹ Secondly, the specific company's corporate governance must then be rated with reference to country in which it operates.¹⁵¹⁰ Investors gain a much more accurate assessment of a company by analysing its corporate governance rating in the context of the country in which the company operates its business.¹⁵¹¹

The most common categories of assessment by the ratings agencies include: board composition, accountability of the directors, director remuneration, audit processes, internal controls, ownership structures, anti-takeover devices, financial disclosures and shareholder rights.¹⁵¹² The most common procedure amongst rating agencies is to conduct their rating of a company using publicly available documents, media articles and company websites.¹⁵¹³ The rating scorecard may then be made available to the rated company, institutional investors or interested parties for a certain fee.¹⁵¹⁴ The cost of the scorecard is determined by the specific rating agency and may be based on an annual subscription fee or a once-off review cost.¹⁵¹⁵ The rating agencies are often chosen based on their costs and the criteria which they use in their ranking assessments.¹⁵¹⁶

In conjunction with the corporate governance rating agencies are the global credit rating agencies which are an essential component of capital markets.¹⁵¹⁷ These agencies are fast becoming an indispensable source of credible information for investors who are assessing in which company and country to make their investment.¹⁵¹⁸ The three global credit rating giants are: Moody's Investor Services ('Moody's'), Fitch Ratings ('Fitch') and Standard & Poor.¹⁵¹⁹ These agencies ascribe domestic and external ratings, at the request of the borrower, using different methodologies and assessment criteria which are continually revised to keep up with international corporate trends.¹⁵²⁰ Increasingly, these agencies are incorporating an assessment of effective corporate

¹⁵⁰⁹ Ibid.

¹⁵¹⁰ Ibid.

¹⁵¹¹ Ibid.

¹⁵¹² Bhasin op cit note 1498 at 3; Donker op cit note 1498 at 84.

¹⁵¹³ Ibid; Donker at 89.

¹⁵¹⁴ Ibid; Louizi op cit note 1502 at 365.

¹⁵¹⁵ Ibid at 3.

¹⁵¹⁶ Ibid at 4.

¹⁵¹⁷ Ibid at 5.

¹⁵¹⁸ Ibid.

¹⁵¹⁹ Ibid; Louizi op cit note 1502 at 365.

¹⁵²⁰ Ibid at 383.

governance structures into their various rating methodologies.¹⁵²¹ All of the information regarding the rating and decisions taken by the agency are made publicly available for easy and cost-effective analysis by all investors on a global spectrum.¹⁵²²

The reputation of the credit and governance rating agencies is of the utmost importance to instil confidence for investors who consider their ratings to be credible and accurate.¹⁵²³ Millions of investors worldwide take investment decisions based on the outcomes given by credit and governance rating agencies of various companies and the countries in which they operate.¹⁵²⁴ In order for a rating outcome to be an effective enforcement mechanism for the accountability of directors, an incentive has to be created.

Investors who invest in companies with good ratings on their corporate governance, which includes an assessment on accountability, are rewarded with better equity performance which in turn creates an incentive in two respects. First, other companies are incentivized to implement good corporate governance structures and achieve higher ratings in order to attract more investors.¹⁵²⁵ Secondly, more investors may regard good governance ratings as one of their predominant informants when taking their investment decisions.¹⁵²⁶

6.2.1 Disadvantages of Rating Agencies

Opponents of the use of corporate governance rating agencies, as an incentive for companies and investors, emphasize several disadvantages of these systems. First, there is no definitively proven link between good corporate governance and company performance.¹⁵²⁷ There is, therefore, little incentive for a company to implement effective corporate governance structures and then to have them rated by any agency.¹⁵²⁸ Investors are also cautioned when analysing a company's corporate governance rating as it does not necessarily imply good performance.¹⁵²⁹ Secondly, rating agencies use different methodologies and assessment criteria for their governance rankings which dilutes uniformity thereby making comparisons between rated companies very difficult.¹⁵³⁰ Thirdly,

¹⁵²¹ Ibid at 365.

¹⁵²² Bhasin op cit note 1498 at 5.

¹⁵²³ Ibid; Louizi op cit note 1502 at 383.

¹⁵²⁴ Ibid; Renders op cit note 1502 at 101; Epps op cit note 1501 at 1137.

¹⁵²⁵ Bhasin op cit note 1498 at 6.

¹⁵²⁶ Ibid; Daines op cit note 1501 at 440.

¹⁵²⁷ Ibid; Donker op cit note 1498 at 91; Epps op cit note 1501 at 1135 & 1143.

¹⁵²⁸ Ibid.

¹⁵²⁹ Epps op cit note 1501 at 1143.

¹⁵³⁰ Donker op cit note 1498 at 91; Bhasin op cit note 1498 at 7; Daines op cit note 1501 at 461.

rating agencies which assess governance criteria separately may produce misleading results as many criteria are inter-related and interdependent and should be examined on a holistic basis.¹⁵³¹

Fourthly, many rating agencies rely primarily on published annual integrated reports of a company, media reports and company websites as the sources of information on which to conduct their ratings.¹⁵³² These sources are secondary and may not depict an accurate reflection of the company which may lead to unreliable ratings.¹⁵³³ Fifthly, the country in which the rated company operates may have legislation which affects its governance methods and which are not taken into account in the assessment, thereby compromising comparability between various companies.¹⁵³⁴

Sixthly, the independence of the rating agencies becomes questionable when the rated company pays for assessment to be conducted.¹⁵³⁵ This may lead investors to assume that the company may have influenced the agency in order to receive a preferable outcome which dilutes the integrity of the rating. Finally, the resources expended by companies, from a time and cost perspective, on ascertaining a rating may prove an insurmountable hurdle for smaller enterprises which are attempting to enter into competitive markets.¹⁵³⁶

6.2.2 Advantages of Rating Agencies

Proponents for the use of corporate governance rating agencies also make very convincing arguments. First, governance ratings agencies are utilized as an accountability enforcement mechanism for directors as achieving accountability will likely result in good ratings.¹⁵³⁷ Secondly, a rated company may track its own accountability and corporate governance if the ratings are done annually and directors are able to gauge and understand the effectiveness of their own governance structures.¹⁵³⁸ Thirdly, rated companies with high ratings are able to use them as marketing tools to attract future investors.¹⁵³⁹ Fourthly, a company with a good governance rating is able to provide comfort and security to its existing investors which may lower the risk of dissenting shareholders and their claims against the company.¹⁵⁴⁰

¹⁵³¹ Ibid Donker at 90.

¹⁵³² Ibid at 86; Bhasin op cit note 1498 at 2.

¹⁵³³ Ibid at 91.

¹⁵³⁴ Ibid.

¹⁵³⁵ Ibid; Bhasin op cit note 1498 at 7.

¹⁵³⁶ Ibid at 7.

¹⁵³⁷ Renders op cit note 1502 at 87; Louizi op cit note 1502 at 383.

¹⁵³⁸ Bhasin op cit note 1498 at 7.

¹⁵³⁹ Ibid; Louizi op cit note 1502 at 383; Epps op cit note 1501 at 1137.

¹⁵⁴⁰ Ibid at 384.

Fifthly, where corporate governance measures are legislated, such as the Sarbanes-Oxley Act in the United States and for JSE Listed Companies in South Africa, rating agencies may promote compliance with the law.¹⁵⁴¹ Companies which comply with the law will receive good ratings and this, in turn, may incentivize other companies to follow suit.¹⁵⁴² Sixthly, it may be insinuated that companies exhibiting a good rating are illustrative of accountable directors which lowers the risk profile for the company as directors are accountable to their stakeholders for their decisions which may reduce the possibility of a perpetration of fraud.¹⁵⁴³ The low risk profile of the company may lead to lower costs of capital and improve the company's value which may attract future investors.¹⁵⁴⁴

Lastly, as a result of recent corporate failures and global recessions investors are seeking credible sources of information on which to base, in whole or in part, their investment decisions.¹⁵⁴⁵ Rating agencies with good reputations are fast becoming indispensable investment tools for institutional investors.¹⁵⁴⁶ Possibly as an unintended consequence and due to the recent failure of many huge corporations, rating agencies have become increasingly popular as a source of credible information for institutional and individual investors.¹⁵⁴⁷

In an ever-evolving environment with challenging economic circumstances, peace of mind for investors has become an irreplaceable commodity.¹⁵⁴⁸ For the majority of investors, companies with good corporate governance ratings are considered less risky and, therefore, good investments.¹⁵⁴⁹ The presence of rating agencies which assess the governance of multiple companies and the countries in which they operate provide an essential source of comfort and security for investors.¹⁵⁵⁰

¹⁵⁴¹ Bhasin op cit note 1498 at 7; Sarbanes-Oxley Act op cit note 1388; JSE Limited op cit note 1298; Renders op cit note 1502 at 101.

¹⁵⁴² Ibid at 102.

¹⁵⁴³ Donker op cit note 1498 at 86 – 87.

¹⁵⁴⁴ Ibid; Renders op cit note 1502 at 88; Louizi op cit note 1502 at 383; Epps op cit note 1501 at 1137.

¹⁵⁴⁵ Ibid; Bhasin op cit note 1498 at 7; Daines op cit note 1501 at 439.

¹⁵⁴⁶ Bhasin op cit note 1498 at 7.

¹⁵⁴⁷ Ibid; Donker op cit note 1498 at 86; Louizi op cit note 1502 at 364.

¹⁵⁴⁸ Renders op cit note 1502 at 101; Daines op cit note 1501 at 439; Ertugrul at op cit note 1498 at 141.

¹⁵⁴⁹ Ibid at 100; Louizi op cit note 1502 at 365; Bhasin op cit note 1498 at 7.

¹⁵⁵⁰ Ibid.

6.3 Corporate Governance Ratings for SOCs

SOCs play an integral part in providing public service mandates on behalf of the government and have the ability to accelerate national growth and development.¹⁵⁵¹ SOCs which are underperforming, from a financial and operational perspective, due to poor governance and a lack of accountability may be hugely detrimental to the economy of the country in which they operate.¹⁵⁵²

The rating of the corporate governance structures and the accountability of an SOC may not be beneficial, from a protentional investor perspective as is the case in the private sector, as the state is the sole shareholder of an SOC. However, the outcome of a rated SOC may prove a useful indicator of the governance and possible future performance of the economy in which the SOC operates.¹⁵⁵³ This indicator would be beneficial to potential investors in ascertaining whether to invest in certain companies in the economy in which the rated SOC operates.¹⁵⁵⁴ The performance of SOCs is meant to be monitored and supervised by the state as the sole shareholder. The rating of SOCs may, therefore, be an indicative representation of the effectiveness of the governance and accountability measures which are enforced by the state in its supervision of SOCs.¹⁵⁵⁵

In addition, the results from an SOC's rating may provide a credible and accurate source of information pertaining to the actual governance and accountability of the SOC instead of relying solely on an interpretation of its annual integrated reports.¹⁵⁵⁶ This information would be beneficial for the board of an SOC in its attempts to improve governance and accountability measures.¹⁵⁵⁷ The state and the public should also be interested parties in examining the results of the rating of an SOC, as the primary stakeholders.¹⁵⁵⁸

Currently, in many jurisdictions the corporate governance of SOCs is rated as one of the assessment criteria of the major credit rating agencies: Standard & Poor's, Moody's and Fitch.¹⁵⁵⁹ Moody's is the only credit rating agency which incorporates corporate governance as one of its

¹⁵⁵¹ Thomas op cit note 9 at 450; Wendy Dobson 'China's State-Owned Enterprises and Canada's Foreign Direct Investment Policy' (2017) 43 *Canadian Public Policy* 29 at 30.

¹⁵⁵² Ibid at 452; Kanyane op cit note 10 at 29.

¹⁵⁵³ Louizi op cit note 1502 at 382.

¹⁵⁵⁴ Ibid.

¹⁵⁵⁵ Bhasin op cit note 1498 at 7.

¹⁵⁵⁶ Thomas op cit note 9 at 463.

¹⁵⁵⁷ Kanyane op cit note 10 at 30.

¹⁵⁵⁸ Ibid.

¹⁵⁵⁹ Louizi op cit note 1502 at 369.

pivotal assessment criteria.¹⁵⁶⁰ Instead of utilising corporate governance rating agencies, as would be the case within the private sector, some jurisdictions have set up institutions which are solely responsible for monitoring and supervising their SOCs.¹⁵⁶¹ Arguably, due to the costs associated with setting up such institutions, South Africa still solely relies on the assessments provided by the credit rating agencies in order to get information surrounding the governance and accountability of its SOCs.¹⁵⁶²

Other countries including: China, Singapore, France and New Zealand have established a government branch, agency or state-owned institution which is solely responsible for monitoring and supervising their SOCs.¹⁵⁶³ This supervision ordinarily includes an assessment of the governance and accountability structures practiced by such SOCs.¹⁵⁶⁴ New Zealand is the only country which has established an institution, that is partially independent from government, to monitor the performance of its various SOCs.¹⁵⁶⁵ For these countries, the corporate governance and accountability of their SOEs remains a top priority as their governments are willing to allocate time and resources to ensure that they are efficiently monitored and supervised.¹⁵⁶⁶

The numerous corruption allegations levied against the South African government indicate that only an institution which is completely independent would be able to effectively monitor the corporate governance and accountability of its SOCs.¹⁵⁶⁷ Political interference, motivations and conflicts of interest would detract from a government institution's ability to effectively monitor the performance of its own SOCs, in an independent, objective and impartial manner.¹⁵⁶⁸ Therefore, independence is the paramount criterion in the establishment of any government institution which has a duty to rate the accountability of South African SOCs without fear, favour or prejudice.

¹⁵⁶⁰ Ibid at 367.

¹⁵⁶¹ Futuregrowth op cit note 10 at 42.

¹⁵⁶² Banele Ginindza 'Moody Slashes SA State Owned Land Bank's Credit Rating to Junk' *IOL* 22 January 2020 available at <http://www.iol.co.za/business-report/economy/watch-moodys-slashes-sa-state-owned-land-banks-credit-rating-to-junk-41059782>; accessed on 8 September 2020.

¹⁵⁶³ Kanyane op cit note 10 at 39; Futuregrowth op cit note 10 at 42; Dobson op cit note 1551 at 31.

¹⁵⁶⁴ Ibid.

¹⁵⁶⁵ Futuregrowth op cit note 10 at 42.

¹⁵⁶⁶ Dobson op cit note 1551 at 34.

¹⁵⁶⁷ Kanyane at op cit note 10 at 32; Thabane op cit note 9 at 12; Thomas op cit note 9 at 448; McGregor op cit note 831 at 5; Futuregrowth op cit note 10 at 4.

¹⁵⁶⁸ Ibid.

6.4 Accountability Rating Agency for South African SOCs

There is an ongoing debate as to the evidence of a positive correlation between the good corporate governance rating of a company and its performance.¹⁵⁶⁹ However, the abovementioned numerous advantages make a case for the use of a rating agency as an enforcement mechanism to incentivize directors to achieve accountability which may be a solution for underperforming South African SOCs.

Slight variations are proposed to the existing approach of corporate governance rating agencies and government monitoring institutions which are used in other jurisdictions around the world.¹⁵⁷⁰ These variations address the disadvantages associated with the use of ratings agencies and focus on the achievement of accountability as a core principle, either under corporate governance structures or on a standalone basis, given the specific requirements of the SOC. This novel accountability framework will include the rating of SOCs as a reward-based enforcement mechanism coupled with a reform of current retributive measures.

The inevitable downgrade of South Africa's credit rating occurred in early 2020 when Moody's announced its rating of the economy, following the suit of Standard & Poor and Fitch who downgraded South Africa to junk status in 2017.¹⁵⁷¹ A large contributor to this downgrade resulted from the chronic lack of accountability displayed by the continuously underperforming SOCs, such as Eskom and SAA.¹⁵⁷² As major public entities, a lack of accountability from these SOCs is hugely detrimental to the economy and is indicative of a complacent state in its supervisory role as sole shareholder.¹⁵⁷³ An integral component for the reform of these distressed SOCs is the establishment of an independent institution which is tasked with conducting annual ratings of the accountability, governance and performance of SOCs.

¹⁵⁶⁹ Bhasin op cit note 1498 at 1; Gloeck op cit note 33; Makoni op cit note 13 at 23; Donker op cit note 1498 at 86.

¹⁵⁷⁰ Futuregrowth op cit note 10 at 42; Dobson op cit note 1551 at 34.

¹⁵⁷¹ Alexander Winning 'Moody's downgrades South Africa to 'junk' status' *IOL* 28 March 2020 available at <http://www.iol.co.za/business-report/economy/moodys-downgrades-south-africa-to-junk-status-45700334>, accessed on 8 September 2020.

¹⁵⁷² Lameez Omarjee 'Weak state entities a risk to SA's credit rating – Moody's' *Mail & Guardian* 16 October 2018 available at <http://mg.co.za/article/2018-10-16-weak-state-entities-a-risk-to-sas-credit-rating-moodys/>, accessed on 9 September 2020; Thomas op cit note 9 at 450.

¹⁵⁷³ Thomas op cit note 9 at 450; Kanyane op cit note 10 at 32; Thabane op cit note 9 at 2; Futuregrowth op cit note 10 at 4.

6.4.1 The Rating Scorecard

There are various scorecards which are utilized by corporate governance and credit rating agencies, of which accountability is one of the criteria.¹⁵⁷⁴ SOCs should be rated with accountability as one of the primary criteria due to the chronic lack of accountability which has been highlighted one of the predominant contributing factors to the dismal performance of South African SOCs, over the last decade.¹⁵⁷⁵ The scorecard may also be applied by a private rating agency to private and public companies, with slight variations to certain criteria which are specific to SOCs. The concept of this proposed rating scorecard for SOCs may also be extended to cover primary corporate governance principles including: fairness, responsibility and transparency. However, the focus on achieving the principle of accountability is paramount for SOCs in South Africa and the proposed scorecard will be constructed with this principle at the forefront.

Unlike the approach to corporate governance provided by the King Codes, an accountability rating scorecard for SOCs will focus on achievement of the principle by the board of directors as opposed to application of numerous recommended practices.¹⁵⁷⁶ The objective of the accountability scorecard is for directors of SOCs to comprehensively apply their minds to meaningful achievement of the principle as opposed to mindless application of recommended practices.¹⁵⁷⁷

The rating scorecard should be simple and clear whilst simultaneously being broad and flexible in order to foster comprehension and understanding of accountability for the SOC directors. The board of an SOC should be allowed the flexibility to effectively apply the principle of accountability in the context of the unique nature of the SOC given its size and the industry in which it operates.¹⁵⁷⁸ The ability of the board of an SOC to effectively account for its decisions, giving reasons and justifications is compromised by a one-size fits all methodology.¹⁵⁷⁹

¹⁵⁷⁴ Bhasin op cit note 1498 at 2; Donker op cit note 1498 at 87.

¹⁵⁷⁵ Thomas op cit note 9 at 450; Kanyane op cit note 10 at 32; Thabane op cit note 9 at 2; Futuregrowth op cit note 10 at 4.

¹⁵⁷⁶ King IV op cit note 19 at part 6.6 at 111; Gloeck op cit note 33.

¹⁵⁷⁷ Ibid.

¹⁵⁷⁸ Morten Huse 'Accountability and Creating Accountability: A Framework for Exploring Behavioural Perspectives of Corporate Governance' (2005) 16 *British Journal of Management* 65 at 69.

¹⁵⁷⁹ D Northcott & Smith, J. 2011. 'Managing Performance at the Top: A Balanced Scorecard Approach for Boards of Directors' (2011) 7 *Journal of Accounting and Organizational Change* 33-56 at 34.

The accountability scorecard will be measured in terms of select categories which will contain some of the assessment criteria utilized by existing governance and credit rating agencies.¹⁵⁸⁰ Prior to the first rating, the agency should equip itself with the knowledge, information and understanding of the unique nature of the SOC, its business, the common state ownership structure (with differing ministers as the state's representative), board composition and the specific industry in which it operates. Whilst the rating agency may analyse the business of each unique SOC to understand the way in which it operates, which may differ from case to case, the rating agency will apply a uniform scorecard for accountability. The five uniform categories and their assessment criteria for the rating scorecard are proposed under the next heading of this chapter.

The uniform categories and sub-categories of the scorecard must be applied to each SOC, having due regard to the circumstances and the industry in which it operates. This uniform scorecard will eliminate inconsistencies which may occur due to the utilization of differing methodologies which is currently the case with the existing corporate governance rating agencies.¹⁵⁸¹ The scorecard, and its various categories, will also be legislated in the proposed Rating Agency Act which will ensure its uniformity and clarity. The assessment criteria within each category will be published from time to time under the regulations to the proposed Rating Agency Act and will be capable of change to avoid stagnation and to ensure their alignment with the current socio-economic climate in South Africa.

The rating agency, in addition to utilizing media sources, integrated reports and SOC websites will engage in active interviews and circulate questionnaires' or surveys to the directors. This will provide a source of accurate information in order to effectively rate the SOC. Any interactive engagement with the directors by the rating agency should be limited and time sensitive to avoid any unnecessary burden on the SOC directors and a possible waste of resources. Any interviews, surveys or questionnaires that are to be conducted with various directors will entail questions which are open-ended in an attempt to ensure comprehension and understanding and avoid

¹⁵⁸⁰ MSCI Inc 'ESG Research' (2020) available at <http://www.msci.com/esg-ratings>, accessed on 9 September 2020; Linda-Eiling Lee et al '2020 ESG Trends to Watch' (2020) MSCI Inc available at <http://www.msci.com/documents/10199/02f6473f-6fd8-aa8f-be72-443196478ec3>, accessed on 9 September 2020 at 25; Moodys Investor Services 'Moody's Publishes Framework for Assessing Corporate Governance at Publicly Traded Non-Financial Corporates' (2019) available at http://www.moodys.com/research/Moodys-publishes-framework-for-assessing-corporate-governance-at-publicly-traded--PBC_1185911, accessed on 9 September 2020.

¹⁵⁸¹ Donker op cit note 1498 at 91; Bhasin op cit note 1498 at 7; Daines op cit note 1501 at 461

mindless application or compliance which may be brought about by leading or closed-ended questioning methods.¹⁵⁸²

The categories of the rating scorecard are also based on the existing internal and external accountability mechanisms of SOCs but with slight variations in an attempt to address the issues associated with the current mechanisms. The internal accountability mechanisms include: the directors, the board and its committees, the state as shareholder, the internal audit and the role of the company secretary. The external accountability mechanisms include: the external audit, the office of the Auditor-General and Public Protector, the judiciary and legislature and the public. Founded on these accountability mechanisms, the proposed scorecard depicts five distinct categories which contain select assessment criteria. Although the categories of the scorecard are distinct, the assessment criteria may be inter-linked and inter-related to one another and the rating agency should take care to avoid unnecessary duplications of the criteria whilst assessing the SOC under the various categories.

Under this scorecard, the directors and the board will owe their duties to the SOC and not just the board as stipulated under the PFMA. The scorecard will conceptualize the concurrent application of the Companies Act and the PFMA by requiring that the board, as a collective body and the directors, as individuals, owe their duties and obligations to the SOC. The board and the directors will be utilised interchangeably throughout the scorecard categories and any reference to the board or the directors will imply that the duty or obligation pertains to both.

The total accountability score for the SOC will be provided by the rating agency in respect of the five major categories and their assessment criteria. A simple numerical scorecard of accountability will suffice on an ascending scale from the numbers zero to ten. The lowest level of accountability being rated with a score of zero and the highest level with a score of ten. The rating agency will provide reasons and justifications for its accountability rating of the SOC. The reasons will not be so convoluted and detailed so as to be utilised in a mindless ‘tick-box’ fashion by the board of the SOC in an attempt to improve its future rating.¹⁵⁸³

¹⁵⁸² Ramalho op cit note 1262 at 175.

¹⁵⁸³ Davies op cit note 709 at 22.

(a) *Category One: The Board and Ownership Structures*

The first category will comprise the board and ownership structures of the SOC. In this category directors will be questioned as to their understanding of the structure of the board of the SOC, the business of the SOC and its shareholder which is the state as sole shareholder. Although the state's sole ownership of SOCs is a common feature, understanding the tiers of government is essential for directors who need to understand what it an SOCs is and what it means to owe their duties to the SOC (i.e the ownership structure of the SOC being the state and how the executive branch of government works).

It is proposed that initial assessment criteria for this category may include an examination on: the directors understanding of the state's ownership and accountability structure, the SOC's board composition, any minimum qualification criteria for directors for their appointment, the process of appointment and removal of directors, the staggered rotation of directors, the succession planning, the various committees, the remuneration policy, any codes of conduct, the training programmes for directors, the role and duties of directors, the categories of directors, the number of board meetings, the attendance at those meetings, the topics and agendas of the meetings and the transparency of the minutes of the meetings and the records kept.¹⁵⁸⁴

Within this initial category, certain accountability issues for SOCs may become evident which should be addressed by the rating agency in its ratings outcome. The SOC should have training programmes to ensure that directors understand their positions as independent or executive directors and the duties that they owe to the SOC. The differing roles of the independent chairman and CEO should be expressly detailed and publicly disclosed.¹⁵⁸⁵ The independence of independent, non-executive directors should be continually analysed by the SOC and results of this analysis made publicly available.¹⁵⁸⁶ The appointment of directors should entail a list of minimum qualifications and experience to prevent capacity issues.¹⁵⁸⁷ Any removal of directors should be accompanied by an explanation and a disclosure of any exit packages which were offered to a director.

¹⁵⁸⁴ King IV op cit note 19; Companies Act op cit note 11; PFMA op cit note 11; Thomas op cit note 9 at 448; Kanyane op cit note 10 at 2; Futuregrowth op cit note 10 at 4; Ramalho op cit note 1262 at 173.

¹⁵⁸⁵ King IV op cit note 19 at principle 10 at 116.

¹⁵⁸⁶ Ibid at principle 7 at 115.

¹⁵⁸⁷ Ibid; Viviers op cit note 1401 at 6; Thabane op cit note 9 at 5.

The state should employ accountability mechanisms to engage with the board of directors of the SOC on a continual basis. Monthly or quarterly reports should be ascertained from the SOC by the state as opposed to once-off annual shareholder compacts. The scorecard is different, in this respect, to that of the recommendations provided by King IV which pertain to the board who owes its duties to the SOC. Due the issues associated with the state being the sole shareholder of SOCs, additional accountability measures need to be enforced to ensure that the state fulfils its reciprocal constitutional duty to hold the board accountable.¹⁵⁸⁸

These additional measures will be interspersed under the assessment criteria of the scorecard as the accountability obligation of the state is an underlying principle which permeates various categories of the scorecard to ensure the achievement of actual accountability by the board of an SOC.

(b) Category Two: The Accountability of the Board

The second category will comprise the accountability of the board and its directors for the performance of the SOC. In this category the directors will be made to account for the performance of the SOC with primary reference to the fulfilment of its commercial and non-commercial mandates. The economic, social responsibility, sustainability, operational and environmental performance of the SOC will also be considered under this category.¹⁵⁸⁹ Any overlaps or duplications of the assessment criteria under this category and category one of the scorecard should be identified and minimized to avoid possible repetitions. The accountability mechanisms utilised should be ones of continual application and not only an annual summary provided in the integrated reports of the SOC.

Suggested methods of continual accountability mechanisms include: self, board and stakeholder evaluations, key-performance scorecards and measurements, peer reviews, the imposition of a balanced scorecard and the implementation of accountability measures to improve historical ratings.¹⁵⁹⁰ The reward of remuneration, fees and bonus payments for directors to incentivize good performance also needs to be closely monitored.¹⁵⁹¹ There should always be link between the

¹⁵⁸⁸ Constitution op cit note 11 at section 92 (2) & 195 (1)(f).

¹⁵⁸⁹ Marimuthu op cit note 1466 at 9; Bezuidenhout op cit note 31 at 2.

¹⁵⁹⁰ Northcott op cit note 1579 at 36 – 8; Huse op cit note 1578 at 68 – 70; King IV op cit note 19 at principle 9 at 40.

¹⁵⁹¹ Marimuthu op cit note 1466 at 9.

performance of the SOC and the directors and the provision of reward to the directors and such link needs to be disclosed and published.¹⁵⁹²

The reciprocal duty on the state, as sole shareholder, to hold the board of the SOC accountable will also be analysed in this category. The methods available to the state to ensure the accountability of the board may include: evaluations of the board, the achievement of key-performance targets, the imposition of rewards or retributions on directors based on performance and compliance and the frequency and effectiveness of the communication mediums between the board and the state.¹⁵⁹³

An analysis of the historical ratings of the SOC will be undertaken by the board in an attempt to resolve any accountability issues and obtain an improved future score. Subsequent ratings of the accountability of the SOC will comprise an analysis of the measures implemented by the SOC in order to improve its rating score from the previous year. The rating agency should be able to ascertain from its engagements with the board whether a mindless ‘tick-box’ method of application of accountability has been implemented which is devoid of any actual comprehension and understanding of the concept of accountability.¹⁵⁹⁴ It will be evident, whether the board of an SOC has failed to mindfully apply the principle of accountability to their decision taking as if the board attempts to mindlessly apply the recommendations given by the rating agency in its previous assessment, then the rating for this category will again produce a very low score.

(c) *Category Three: Compliance*

The third category is compliance by the board and the Minister with internal and external regulatory requirements, from a legal and industry specific perspective. The specific focus of this category will entail an examination of the financial accountability mechanisms, including: the audit committee, the internal audit control, the frequency of the audits as a form of continual assessment and the improvements in any measures to be implemented, compliance with legislation, the risk management policy, financial reporting and disclosure mechanisms, the external audit and the external auditors.¹⁵⁹⁵

¹⁵⁹² Bezuidenhout op cit note 31 at 13.

¹⁵⁹³ Ibid; Davies op cit note 709 at 22.

¹⁵⁹⁴ Ibid.

¹⁵⁹⁵ King IV op cit note 19 at principle 7 at 115; Gloeck op cit note 33.

The agency will specifically ascertain whether the board of the SOC has been held accountable by the state, and to what extent, for any failure to perform any of the mandated financial controls. An inability of the state to effectively hold the board accountable for any non-compliance will negatively affect the rating of the SOC under this category. This is again different to the approach under King IV where the focus is on the board of the SOC as the primary body to ensure the sound corporate governance and accountability of the SOC.¹⁵⁹⁶ Under this category the accountability of the board and the reciprocal duty on the state to hold the board accountable will be of combined importance.

Annual integrated reports should be simplified and only contain information which is specific to that financial year-end and should not comprise a repetition of the previous year's report. The external auditors will be carefully analysed to ensure their independence from the SOC and their report on the audit of the SOC's annual, financial statements will also be examined.¹⁵⁹⁷ Methods for ensuring the absolute independence of the external auditors should be implemented by the board of the SOC, including: mandatory rotation, continual independence assessments and the submission of any potential conflicts of interests.¹⁵⁹⁸

The directors should be held accountable for compliance with relevant regulations and legislation by the SOC and in respect of the fulfilment of their own duties and obligations as directors.¹⁵⁹⁹ The directors should be held personally accountable and an explanation required for any possible litigation instituted against them for a breach of their duties and the imposition of personal or criminal liability.¹⁶⁰⁰ Under this category it is the directors and the board who will be examined for the fulfilment of their duties, as a collective body and as individuals who owe their duties to the SOC.¹⁶⁰¹ Any breach by the board or the directors may result in the imposition of liability either jointly and severally against the entire board or against individual directors.¹⁶⁰² Liability should be imposed by the board of the SOC against individual directors, alternatively and secondly by the state against the board or the individual directors of the SOC.

¹⁵⁹⁶ Ibid at principle 6 at 114.

¹⁵⁹⁷ Ibid at principle 8 at 115.

¹⁵⁹⁸ Companies Act op cit note 11 at section 90 – 2.

¹⁵⁹⁹ King IV op cit note 19 at principle 7.

¹⁶⁰⁰ Companies Act op cit note 11 at section 76.

¹⁶⁰¹ PFMA op cit note 11 at section 50 & 51 concurrently applied with the Companies Act op cit note 11 at section 76.

¹⁶⁰² Ibid at section 86 (2) concurrently applied with the Companies Act op cit note 11 at section 77.

Any adverse findings or investigations made against the SOC by independent institutions such as the Auditor-General or Public Protector need to be explained and justified by the board.¹⁶⁰³ The board needs to prove its compliance with any remedy which is stipulated by such institutions.¹⁶⁰⁴ The ability of the state to ensure the compliance by the board with its statutory obligations and the taking of any stipulated remedial action will be of specific focus under this category. The state may withhold the increased remuneration, fees or bonus packages to the directors of the SOC as a result of non-compliance or failing to fulfil their duties.¹⁶⁰⁵ This method of withholding rewards may be preferable as an enforcement mechanism for the state as opposed to the imposition of punishment.

(d) *Category Four: Stakeholder Relations*

The fourth category pertains to the relationship that the board of the SOC maintains with its numerous stakeholders. The board of the SOC should be held accountable for maintaining constant and effective communication with its stakeholders, including: employees, creditors, regulators, the state and the public.¹⁶⁰⁶ The board should disclose such communication methods publicly and investigate any stakeholder complaints. A code of conduct for director engagement with stakeholders should also be published on the SOC's website. Under this category, the supervisory role of the state, as sole shareholder, will again be brought into consideration.¹⁶⁰⁷

(e) *Category Five: Support Mechanisms*

The last category comprises an analysis of the support mechanisms which the board employs in order to meet its accountability requirements. The board should be assisted by various committees as well as the company secretary.¹⁶⁰⁸ The mandatory committees should include, depending on the size and nature of the SOC: an audit and finance committee, a governance and accountability committee, a nominations and removal committee and a compliance committee.

The position of the company secretary should be continually analysed. A minimum set of qualifications should be stipulated in the founding legislation of the SOC for the appointment of

¹⁶⁰³ PAAA op cit note 647; PPA op cit note 682.

¹⁶⁰⁴ Makwethu (AGSA) op cit note 18 at 10.

¹⁶⁰⁵ Bezuidenhout op cit note 31 at 13.

¹⁶⁰⁶ McGregor op cit note 831 at 13.

¹⁶⁰⁷ Ibid at 17.

¹⁶⁰⁸ Companies Act op cit note section 84 (1)(b) & 88 (2)(a).

the company secretary.¹⁶⁰⁹ A mandatory rotation of the company secretary after a set period should also be stipulated. The role of the company secretary will also be examined, including: independence, capacity, availability, number of director interactions, training programmes provided to directors, compliance with legislation, communication methods and access for directors.

6.5 The Rating Agency

The state institutions which were established for the purpose of strengthening democracy, under chapter nine of the Constitution, have been utilized effectively as a powerful accountability tool for flailing SOCs.¹⁶¹⁰ The track record of the Public Protector and the Auditor-General are nearly impeccable, notwithstanding their operation in the context of a torrential socio-economic climate.¹⁶¹¹ These institutions have had to overcome continuous threats to their impartiality largely due to political interference from the executive. However, the integrity and independence of these institutions has remained intact and they have effectively fulfilled their duties and performed their functions, without fear, favour or prejudice.¹⁶¹²

Despite the effectiveness of these state institutions, SOCs still exhibit a lack of accountability which contributes to their continuing poor performance.¹⁶¹³ Therefore, a need arises for the establishment of an independent rating agency for SOCs as a state institution under chapter nine of the Constitution. This independent state institution will be mandated to annually rate the accountability of SOCs. The rating agency is required to be an independent institution due to the numerous allegations of corruption against the state which is the sole shareholder of many SOCs. These allegations have brought into question the ability of the state to effectively fulfil its constitutional obligation to hold the board of SOCs accountable.¹⁶¹⁴ As an independent state institution, the rating agency should be able to perform its functions without fear, favour or prejudice, akin to the offices of the Public Protector and Auditor-General.

¹⁶⁰⁹ King IV op cit note 19 at principle 10 at 116.

¹⁶¹⁰ Constitution op cit note 11 at ch 9 & section 181.

¹⁶¹¹ *SABC* case supra note 167 para 24 – 9; *Mail & Guardian* case supra note 701 para 19 and 22; *New National Party* case supra note 701 para 98 and 99.

¹⁶¹² Constitution op cit note 11 at section 181 (2); *SABC* case supra note 167 para 29 & 53; *EFF* case supra note 677 para 54.

¹⁶¹³ Thabane op cit note 9 at 24; Thomas op cit note 9 at 451; Kanyane op cit note 10 at 30.

¹⁶¹⁴ Constitution op cit note 11 at section 92 (2); Kanayane op cit note 10 at 30; Thabane op cit note 9 at 24; Thomas op cit note 9 at 451; Futuregrowth op cit note 10 at 2.

The additional powers and functions of the rating agency will be set out in national legislation which is to be enacted and is proposed as the Rating Agency Act.¹⁶¹⁵ The primary function of the rating agency will be to carry out annual ratings of SOCs, on an individual basis, according to the proposed accountability scorecard and to publish those ratings and deliver them to the National Assembly.¹⁶¹⁶ It is submitted that the proposed Rating Agency Act may incorporate provisions relating to: the appointment and removal of its members, the rating process of SOCs, the accountability scorecard and the proposed categories, the link between the provision of state funding and the rated SOCs; maximum thresholds for state funding to SOCs based on their ratings, the reporting and publishing process, its code of conduct, its annual report, its funding requirements, the use of its funds and its own disclosure and accountability requirements.¹⁶¹⁷

The rating agency remains accountable to the National Assembly at all times as is the case with the chapter nine state institutions.¹⁶¹⁸ It is proposed that Parliament should establish a standing committee to deal with and actively engage with the ratings agency whilst at the same time respecting and maintaining its independence. As is the case with the SCOPA which deals with the Public Protector.¹⁶¹⁹ The proposed standing committee may advise the state on matters including: the appointment and remuneration of members of the rating agency, the additional powers of the agency and any complaints referred to the committee, in respect of the agency.¹⁶²⁰ The supervisory role over SOCs provided by the current committees, SCOPA and the Standing Committee on Finance, may be subsumed under the role of the proposed standing committee dealing with the rating agency.

The President, on recommendation of the National Assembly and the proposed rating agency standing committee, must appoint the head and the members of the ratings agency.¹⁶²¹ However, the proposed Rating Agency Act must stipulate a list of minimum qualifications and experience, which members of the agency are required to fulfil in order to be appointed by the President. The Constitution must specify that the head of the office of the rating agency may only be held by a fit

¹⁶¹⁵ This national legislation will be similar to the PPA and the PAA which were enacted in support of the Public Protector and Auditor-General when they were established as a chapter nine state institutions under the Constitution op cit note 11 at section 181 (2), 182 (1) & 188 (2).

¹⁶¹⁶ Ibid at section 181 (5).

¹⁶¹⁷ These provisions are largely drawn from the provisions contained in the PPA and the PAA.

¹⁶¹⁸ Constitution op cit note 11 at section 181 (5).

¹⁶¹⁹ PPA op cit note 682 at section 2 (1).

¹⁶²⁰ Ibid.

¹⁶²¹ Constitution op cit note 11 at section 193 (4).

and proper South African who has specialized knowledge and experience in the area of corporate governance and accountability.¹⁶²²

The tenure of the head of the office of the rating agency should be for a period of seven years in order to avoid the issues associated with constant turnover of the position. The head of the office may only be removed, prior to the expiry of his or her tenure, in limited circumstances by the President or the National Assembly.¹⁶²³

6.6 Enforcement of the Rating Agency

There are potential enforceability issues in respect of the remedial action prescribed by the state institutions to SOCs as previously discussed in terms of the remedial action stipulated by the Public Protector.¹⁶²⁴ In order to combat this issue, an enforcement mechanism needs to be established which compels the board of an SOC to resolve any issues raised by the rating agency. A rated SOC which achieves a low score will be required to address its accountability issues in order to improve its future scoring. A mechanism needs to be implemented to ensure that the SOC takes steps to improve its accountability and achieve a better future score. This enforcement mechanism can be in the form of a reward which incentivizes action or in the form of punishment which deters non-compliance.¹⁶²⁵

Currently, the state's provision of funding to failing SOCs is prolific and there is a lack of accountability when it comes to the continued poor performance of the SOC despite numerous bailouts provided by the state.¹⁶²⁶ It is argued that there may be room for an enforcement mechanism which links the state funding to SOCs with the outcome of their scoring from the rating agency. It is submitted that SOCs with lower ratings are provided with less funding or funding on less favourable terms and SOCs with higher ratings are provided with more funding or funding on preferential terms. This link between state funding and the rating of the SOC provides an enforcement mechanism for accountability which is incentive-based as SOCs with higher ratings

¹⁶²² Similar to the requirements for the appointment of the Auditor-General and Public Protector under the Constitution at section 193 (1) & (3).

¹⁶²³ *Ibid* at section 194.

¹⁶²⁴ *SABC* case supra note 167 para 60; De Vos op cit note 714.

¹⁶²⁵ Davies op cit note 709 at 22.

¹⁶²⁶ Futuregrowth op cit note 10 at 42; Kanyane op cit note 10 at 30; Thabane op cit note 9 at 24; National Treasury op cit note 1 at 90 – 95; Thomas op cit note 9 at 451.

are rewarded with more or preferential state funding. Therefore, the board of an SOC is incentivized to achieve actual accountability and receive a high rating from the rating agency.

The annual rating of an SOC by the rating agency and the link between the rating and the state funding to SOCs should be mandated and included in legislation. These rules may be contained in the overarching SOE Legislation or the Rating Agency Act or in both statutes. Any state funding provided to SOCs must be regulated and maximum thresholds should be set which are linked to the annual ratings provided by the agency. Any state funding must be declared by an SOC and the use of those funds must be tracked in its annual financial statements. An inability of the board to effectively account, every year, for the utilization of state funds will impact negatively on the SOC's scoring in terms of the third category of the scorecard in an assessment on its internal financial controls.

The link created between the provision of state funds or preferential funding and the outcome of the rating will incentivize the board of the SOC to improve its accountability measures and obtain a higher rating. An increase in the provision of state funding, or preferential funding, should assist in improving the financial and operational performance of the SOC. An SOC which out performs its competitors will be able to increase remuneration and director fees and make bonus payments. Directors are, therefore, incentivized to ensure that they remain accountable in order to obtain a high rating and the benefit of more, or preferential, state funding.

Incentivized directors should, in turn, reduce the necessity for the continual monitoring and supervision by the state, through the Minister, as sole shareholder. The directors will want to be accountable and achieve high scores to receive the needed state funding and should not require much prompting from the Minister. The reciprocal duty on the state to hold the board of the SOC accountable remains an assessment criterion under the scorecard which may also incentivize the board to constantly and effectively engage and communicate with the state.

One of the main components of this enforcement mechanism is the strict implementation of transparency and disclosure methods by the SOC. These methods should be legislated and be encompassed under the proposed provisions of the overarching SOE Legislation. These proposed statutory provisions may be drawn from the existing minimum mandatory requirements and

voluntary recommended practices for the accountability, transparency and disclosure of SOCs which are contained in the PFMA, the Companies Acts and King IV.¹⁶²⁷

The mandatory annual rating of an SOC by the rating agency together with the statutory creation of a link between the rating score of the SOC and the provision of state funding to that SOC establishes a proposed incentive-based enforcement mechanism to ensure the actual accountability of the board of an SOC.

6.7 Implementation of SOC Reform

The proposed framework for the accountability reform of South African SOCs comprises two primary components. In the first instance, two pieces of national legislation would have to be enacted. A proposed Rating Agency Act would be implemented which depicts the rules and regulations for the establishment of a rating agency which will rate the accountability of SOCs. In order to include this rating agency as a state institution, chapter nine of the Constitution would have to be amended.¹⁶²⁸ An overarching SOE Legislation would also have to actually be enacted to govern all aspects relating to SOEs, including SOCs.¹⁶²⁹

In the second instance, the corporate governance approach currently undertaken by SOCs may have to be reformed to include the effects brought about by the rating agency and its accountability scorecard. The application of accountability would remain voluntary as a principle to be achieved by the board of an SOC by whatever structures or measures it chooses to implement whether under the auspices of corporate governance or as a standalone principle. However, it is proposed that two components of the accountability of SOCs be regulated under the reformed approach. First, a duty to account for the directors of SOCs must be made mandatory as a statutory duty embodied under the proposed overarching SOE Legislation. Secondly, the annual rating of an SOC by the rating agency and the link between the SOC's rating and the provision of state funding to that SOC must be mandated.

6.8 Statutory Reform

The statutory reform for the implementation of a rating agency as a chapter nine state institution under the Constitution requires two primary actions. First, the Constitution would have to be

¹⁶²⁷ PFMA op cit note 11; Companies Act op cit note 11; King IV op cit note 19.

¹⁶²⁸ Constitution op cit note 11 at ch 9.

¹⁶²⁹ Kanyane op cit note 10 at 30; PRC op cit note 3 at 9.

amended in order to include the rating agency as a chapter nine state institution.¹⁶³⁰ Secondly, national legislation would have to be enacted in terms of the overarching SOE Legislation and the Rating Agency Act.

6.8.1 Amendment of the Constitution

The Constitution would need to be amended to include the rating agency as a chapter nine state institution. Chapter nine of the Constitution would need to be amended by a Bill supported by two thirds of the members of the National Assembly.¹⁶³¹ Approval of the Bill by the NCOP would not be required as the amendment to the Constitution pertains to the establishment of a chapter nine institution for the rating of SOCs which is not considered a provincial matter.¹⁶³² The process detailing an amendment of the Constitution is lengthy and depicted under section 74 of the Constitution.¹⁶³³ This process would have to be initiated efficiently if the rating agency is to be utilized to enforce the accountability of SOCs in the near future.

6.8.2 Enactment of National Legislation

There are two legislative enactments which are proposed in order to implement the enforceable accountability framework for SOCs. The proposed Rating Agency Act would have to be implemented as national legislation to govern all of the powers and processes of the rating agency as a chapter nine state institution under the Constitution. The overarching SOE Legislation would also have to be enacted as national legislation to govern all aspects relating to SOEs, including SOCs.

The national legislative authority vests in Parliament which confers on the National Assembly the power to pass legislation.¹⁶³⁴ The National Assembly would, by a majority vote of its members, pass a Bill governing all aspects relating to the Rating Agency Act.¹⁶³⁵ The Bill would then be referred to the NCOP where the Bill will be passed, with or without amendment, or rejected.¹⁶³⁶ A

¹⁶³⁰ Constitution op cit note 11 at ch 9.

¹⁶³¹ Ibid at section 74 (3)(a).

¹⁶³² Ibid at section 74 (3)(b).

¹⁶³³ Ibid at section 74.

¹⁶³⁴ Ibid at section 44 (a)(ii).

¹⁶³⁵ Ibid at section 53 (1)(a).

¹⁶³⁶ Ibid at section 75 (1)(a).

Bill passed by the NCOP without any proposed amendments will be submitted for assent by the President.¹⁶³⁷

A rejected Bill, or one passed with amendments, will be referred back to the National Assembly for consideration.¹⁶³⁸ The National Assembly may then pass the Bill as national legislation, with or without the proposed amendments or decide not to proceed with the Bill.¹⁶³⁹ A Bill passed by the National Assembly must be submitted to the President for assent.¹⁶⁴⁰ Once the Bill has been assented to and signed by the President, it becomes national legislation and must be published in the government gazette.¹⁶⁴¹ The effective date of the statute is the date upon which it comes into operation which is the date that the government gazette is published or a date set out in the statute itself.¹⁶⁴²

(a) *The Rating Agency Act*

The Constitution requires that the office of the Public Protector and the Auditor-General, which are established as chapter nine institutions, refer to national legislation to govern their additional powers and processes.¹⁶⁴³ Akin to these institutions, a rating agency which is established as a chapter nine institution would require national legislation to govern all aspects related to its implementation, powers and processes.

This proposed Rating Agency Act will contain two predominant aspects. First, to enact the mandated link between the outcome of the SOC rating and the provision of state funding to that SOC. Secondly, to regulate the accountability scorecard containing the five categories for the rating of SOCs which is to be utilised by the rating agency. The assessment criteria, which fall under each category, will be published from time to time under the regulations of the proposed Rating Agency Act. The regulated scorecard categories and the published assessment criteria, which may be subject to change from time to time, are meant to achieve a sense of uniformity and clarity for SOC directors whilst at the same time promoting flexibility to ensure proper application, comprehension and understanding of the principle of accountability.

¹⁶³⁷ Ibid at section 75 (1)(b).

¹⁶³⁸ Ibid at section 75 (1)(c).

¹⁶³⁹ Ibid at section 75 (1)(c)(i) & (ii) & 55 (1)(a).

¹⁶⁴⁰ Ibid at section 75 (1)(d).

¹⁶⁴¹ Ibid at section 79 & 81.

¹⁶⁴² Ibid at section 81.

¹⁶⁴³ Ibid at section 182 (2) & 188 (4).

The Rating Agency Act must mandate the link between the provision of state funding and the rating of the SOC with set maximum thresholds of funding or preferential funding based on the rating scores, on an ascending scale from zero to ten. As an example, an SOC achieving a level one rating will receive state funding or funding on the designated terms which is within the parameters set for a level one score and for which there will be maximum thresholds. The state will be bound by the provisions of the Rating Agency Act and will not be able to deviate from the maximum funding thresholds or designated funding terms.

In the premise, the directors of SOCs will be incentivized to achieve actual accountability and a high rating score as the state will not be able to provide funding to the SOC unless in accordance with the provisions of the proposed Rating Agency Act.

(b) SOE Legislation

The second aspect of the statutory reform for SOCs is the implementation of the overarching SOE Legislation.¹⁶⁴⁴ The SOE Legislation will include provisions specifically relating to the identification and governance of all SOCs which are proposed under next heading of this chapter. The SOE Legislation may repeal the PFMA, in its entirety, as well as the provisions of the Companies Act and the JSE listing requirements which pertain to SOCs.¹⁶⁴⁵ All of the current rules and regulations in under these statutes which pertain to SOCs will be subsumed, with or without amendment, under the SOE Legislation. SOCs will be given a transition period, similar to that which was given to companies under the Companies Act, to amend their founding legislation to ensure alignment with the SOE Legislation. In a conflict between the founding legislation of an SOC and the SOE Legislation, the SOE Legislation will prevail.

The SOE Legislation may resolve the initial hurdle caused by the complicated definitions ascribed to SOEs and SOCs under the PFMA and the Companies Act.¹⁶⁴⁶ The SOE Legislation may address this issue by amalgamating the differing definitions provided by the PFMA and the Companies Act and providing clear definitions thereby eliminating unnecessary duplications and contradictions. It is proposed that simplifying and amending the various qualifying criteria for SOCs and providing for continual assessment and possible reclassification methods, if circumstances dictate, would assist in clearly identifying and categorizing SOEs and SOCs. This

¹⁶⁴⁴ Kanyane op cit note 10 at 30; Futuregrowth op cit note 10 at 42.

¹⁶⁴⁵ PFMA op cit note 11; Companies Act op cit note 11; JSE Limited op cit note 1298.

¹⁶⁴⁶ Ibid at section 1.

improved and accurate classification of all SOEs will assist in identifying and clarifying their unique mandates and may avoid conflicts of interest which arise in their fulfilment.

The enactment of one overarching SOE Legislation may also assist in overcoming some of the compliance issues currently facing SOCs. SOCs are required to comply with multiple rules and regulations contained in numerous statutes which are often contradictory, convoluted and complex.¹⁶⁴⁷ This creates an overly burdensome task for directors of SOCs who have to refer to multiple statutes to ensure compliance. The costs of compliance may be reduced with adherence to only statute as opposed to multiple.¹⁶⁴⁸

There may already be processes in place to enact an overarching piece of national legislation which will cover all governance aspects relating to the state's management of SOEs, as the partial or sole shareholder. The Shareholder Management Bill is expected to be presented by the executive to Parliament for consideration in 2021¹⁶⁴⁹. Arguably, the Bill should resolve many of the issues pertaining to the lack of accountability for SOCs with various amendments proposed to the existing legislation. The Bill will also aim to establish a framework to ensure that all the boards of all SOEs and SOCs are held accountable to the executive.¹⁶⁵⁰ However, this Bill has been in the process of being implemented since at least 2014 and it is possible that it may never actually be enacted as national legislation.¹⁶⁵¹

6.8.3 Proposed Provisions for the SOE Legislation

The overarching SOE legislation may amend some of the current rules and regulations pertaining to SOCs with the objective of addressing their numerous accountability issues. It is submitted that there are seven predominant solutions to be proposed in the provisions of the overarching SOE Legislation.

¹⁶⁴⁷ Kanyane op cit note 10 at 32.

¹⁶⁴⁸ Ibid.

¹⁶⁴⁹ Parliamentary Monitoring Group 'Report of the Portfolio Committee on Public Enterprises on Budget Vote 9: Public Enterprises and the Annual Performance Plan for the 2019/2020 of the Department of Public Enterprises' (2019) available at <http://pmg.org.za/taled-committee-report/3867>, accessed on 10 September 2020.

¹⁶⁵⁰ Ana Reporter 'Public enterprises wants to fast-track oversight bill on SOEs' IOL 3 July 2019 available at <http://www.iol.co.za/news/politics/public-enterprises-wants-to-fast-track-oversight-bill-on-soes-28568547>, accessed on 10 September 2020.

¹⁶⁵¹ Leandi Kolver 'Processing of Government Shareholder Management Bill has to be sped up' Polity 20 August 2014 available at <http://www.polity.org.za/article/processing-of-government-shareholder-management-bill-has-to-be-spiced-up-portfolio-committee-2014-08-20>, accessed on 10 September 2020.

(a) *Directors*

The accountability issues facing directors of SOCs will be addressed by the overarching SOE Legislation through an amendment of the current rules and regulations. There are, arguably, three major challenges which currently impede the accountability of SOC directors and which may be resolved through the SOE Legislation.

In the first instance the SOE Legislation may address the capacity issue facing the directors of many SOCs by implementing three requirements. First, a minimum set of qualification criteria for the appointment of SOC directors should be legislated.¹⁶⁵² Directors of SOCs may not be appointed by the state if they do not satisfy the minimum statutory requirements set out in the SOE Legislation. These criteria will be specific to the category of director, whether executive or non-executive and the criteria for independent, non-executive directors will centre around their independence from the SOC in order to avoid any potential conflicts of interest. The founding legislation of the SOC may also set out additional qualification criteria for the appointment of its directors.

Secondly, a nominations committee should also become compulsory for SOCs and the state must only be allowed to appoint directors by a majority agreement of the nominations committee. This nominations committee will also have to be consulted by the state prior to the removal of any directors from the board of an SOC. In the premise, the Minister will no longer be allowed to appoint or remove directors to, or from, the board of SOCs at his or her sole discretion.¹⁶⁵³

Thirdly, mandatory training for directors of SOCs will also be regulated and directors will be required to comply, failing which, they will be removed from their office. The mandatory training afforded to directors will assist in educating them on their respective positions, and differing roles, as independent, non-executive or executive directors and the duties which they are required to fulfil. The training will also centre around compliance with relevant legislation which will beget education surrounding the implementation of governance mechanisms to improve the SOC's accountability ratings. This training may dilute an argument for future directors claiming ignorance

¹⁶⁵² Viviers op cit note 1401 at 6.

¹⁶⁵³ Lukas Muntingh 'Appointing Directors to the Boards of State-Owned Enterprises' (2020) Dullah Omar Institute available at <http://dullahomarinate.org.za/women-and-democracy/board-members-of-state-owned-enterprises-towards-transparent-appointments/reports/appointment-of-soe-directors-assessment-pdf-version-12-feb-2020-final.pdf>, accessed on 11 September 2020 at 5.

in the event of tyrant chairpersons taking decisions which are not in the best interests of the SOC, as was the case with Myeni and the board of SAA.¹⁶⁵⁴

The continuous evaluation of directors of SOCs by the nominations committee, the minimum qualification criteria and the implementation of mandatory training should reduce capacity constraints experienced by SOC boards and assist in reducing the turnover of predominant executive directors.¹⁶⁵⁵ The frequent turnovers cause disruption in the board's operations and are largely as a result of incapacity from the initial appointment or due to a lack of training after the appointment has been made.¹⁶⁵⁶ This risk may be mitigated with the proper screening of directors prior to their appointment by the nominations committee and mandatory training on their positions and the duties with which they have to comply in order to retain their positions on the board.

In the second instance, the numerous statutory duties for SOC directors, which make compliance a burdensome and time-consuming task, may be resolved by the SOE Legislation.¹⁶⁵⁷ Amalgamation of all of the statutory duties stemming from the PFMA and Companies Act would assist SOC directors from a compliance perspective.¹⁶⁵⁸ Any duplications of the statutory duties may also be amended to avoid unnecessary contradictions and interpretation issues. Directors need only source one piece of legislation instead of numerous in order to ascertain which duties they owe to the SOC. A duty to account may also be included in the statutory fiduciary duties with which the directors of SOCs are required to comply.

In the third instance, the provisions regarding the liability to be imposed on recalcitrant directors may be reformed through the SOE Legislation. Although there are currently statutory measures for holding directors personally and criminally liable, they are outdated and ineffectively implemented as retributive-based enforcement mechanisms. With the exception of the court orders for declaring delinquent directors, the liability provisions set out under the PFMA and Companies Act are underutilized.¹⁶⁵⁹ This underutilization may occur, in part, due to the application of the numerous safeguards afforded to directors who are alleged to have breached their duties. The SOE Legislation should allow for liability to be imposed by the state on the board, jointly and severally,

¹⁶⁵⁴ *OUTA v Myeni* case supra note 346.

¹⁶⁵⁵ Muntingh op cit note 1653 at 6.

¹⁶⁵⁶ Makoni op cit note 13 at 22 – 3; Thabane op cit note 9 at 5.

¹⁶⁵⁷ Kanyane op cit note 10 at 30.

¹⁶⁵⁸ Ibid at 32.

¹⁶⁵⁹ PFMA op cit note 11 at section 86 (2); Companies Act op cit note 11 at section 77 & 162.

as well as on the individual directors, by the state or the board, for a breach of their duties to the SOC.

An abuse of the safeguards dilutes the enforceability which the liability provisions are meant to provide. In addition, the criminal liability imposed under the PFMA in the event of a breach of duties for SOC directors is archaic and should be amended if not removed entirely. The provisions pertaining to the liability and safeguards for SOC directors should be complementary and reinforce one another in order to be effective as retributive-based enforcement mechanisms for accountability.

SOE Legislation which comprehensively deals with the liabilities, safeguards and duties for SOC directors may negate any contradictions and duplications, thereby improving their clarity and effectiveness as enforcement mechanisms for accountability.

(b) The Board and Committees

The composition of the board for SOCs is currently not mandated and should remain as such with a few exceptions and additions. The composition of the board of directors is specific and unique for each SOC, depending on the nature of its business, its size and the industry within which it operates.¹⁶⁶⁰ Regulating board composition would place uniform requirements on all SOCs which would stifle flexibility and the ability to determine the best composition for each specific SOC. A one-size fits all, regulatory approach may not be beneficial in ascertaining the best board composition for SOCs in terms of the diversity, skills, knowledge and experience of its directors.

The addition of a compulsory nominations committee, minimum qualification criteria and mandatory training for directors, in lieu of uniform rules and regulation for board composition, will assist in removing deficiencies in the board composition of SOCs.¹⁶⁶¹ Based on statutory minimum qualification criteria, only select individuals are screened and appointed as directors of SOCs based on their individual merits and in the context of the SOC given its nature, mandates and specific requirements. The mandatory establishment of the nominations committee, coupled with the requirement of its prior approval for appointments, will mean that the board's opinion will be considered in the appointment of directors and the composition of the board.

¹⁶⁶⁰ King IV op cit note 19 at principle 7 at 115.

¹⁶⁶¹ McGregor op cit note 831 at 13.

The composition of the board of an SOC will form part of the accountability scorecard utilized by the rating agency. Category one of the scorecard pertains to the board structure of the SOC and includes the board's composition and the appointment and removal of its directors. The board's governance systems, the attendance of directors at, and the number of, annual board meetings will also form part of category one of the scorecard and remain voluntary for the SOC. A uniform and regulated approach to the frequency and attendance of board meetings is not conducive to the governance of an SOC. The board of an SOC should be allowed the flexibility to determine the frequency and attendance of board meetings taking into account its own unique governance requirements which may vary based on the nature and size of every SOC.

The governance processes for directors' meetings such as: notices, resolutions, proxies, quorums and recorded minutes under the Companies Act are clear and comprehensive and should be incorporated into the SOE Legislation.¹⁶⁶² The attendance and contribution of directors at board meetings should be linked to their remuneration or fees and bonus payments.¹⁶⁶³ These rewards should act as an incentive mechanism to enforce attendance and meaningful contributions as opposed to punishing directors for non-attendance.

Whilst the composition of the board remains voluntary for the SOC, certain restrictions should be legislated. There should be statutory disqualification criteria for the appointment of independent, non-executive directors to the board. It is submitted that there should be rules stating that no person who has a personal or financial interest, whether director or indirect, in the state should be appointed to serve as an independent, non-executive director for an SOC. Similarly, a person cannot be appointed as an independent, non-executive director if that person has previously served as an executive director for that SOC. The regulation of both of these requirements would have prevented the appointment of former chairperson Myeni to the board of SAA which had drastic consequences.¹⁶⁶⁴

The continual analysis of the independence of independent non-executive directors will be a function for the nominations committee.¹⁶⁶⁵ Every year the nominations committee must confirm that the independent non-executive directors are truly independent and that the minimum

¹⁶⁶² Companies Act op cit note 11 at ch 2 part F.

¹⁶⁶³ Bezuidenhout op cit note 31 at 13.

¹⁶⁶⁴ *OUTA v Myeni* case supra note 346.

¹⁶⁶⁵ King IV op cit note 19 at principle 7 at 115.

qualification criteria, and none of the disqualification criteria, have been satisfied. The supervisory role of the independent non-executive directors on the board of an SOC is imperative to its composition.¹⁶⁶⁶ The committee should also ensure that mandatory training is imposed, as and when required, for all directors to continuously educate them on their respective roles and duties.

There should be a regulated limitation on the number of years for which an independent non-executive director can serve on the board of an SOC.¹⁶⁶⁷ After a certain period, for example seven years, a director is no longer considered to be independent from the SOC, having been a witness to its operations through the board meetings for a number of years. These directors may continue, after seven years, to serve on the board as non-executive directors however, they will not be classified as independent non-executive directors for the rating purposes of board composition. A director may be reappointed to the board of an SOC as independent non-executive director after a period of five consecutive years of not serving as any director on the board of that SOC.

There should also be a mandated limit on the number of boards on which a person may serve as an independent non-executive director in any given year.¹⁶⁶⁸ In the appointment of the director, the nominations committee will screen the individual and if that individual is already a director, regardless of categorization, of four other entities he or she cannot be appointed as a director of that SOC. This measure is regulated to avoid capacity constraints for independent non-executive directors due to their serving on the boards of too many entities at any one time.

The compulsory committees which SOCs are required to establish must be legislated as is currently the case but with some amendments. The compulsory committees should be: the nominations and removal committee, the audit and finance committee, the governance and accountability committee and the compliance committee. The board of the SOC will have the discretion to compile the contents of the written mandate for each committee.¹⁶⁶⁹ However, the mandates must be written and reviewed every quarter by the board to ensure that the committee fulfils its delegated responsibilities. The screening of directors by the nominations committee, and their prior approval for appointment, should assist in decreasing the frequent turnover of the committee members which causes instability and may detract from their ability to complete their responsibilities.

¹⁶⁶⁶ Ibid at principle 8 at 115; Wiese op cit note 63 at 32; Bhagat op cit note 440 at 235; Olson op cit note 399 at 237.

¹⁶⁶⁷ Ibid at principle 7 at 52.

¹⁶⁶⁸ Ibid at principle 35 at 53.

¹⁶⁶⁹ Ibid at principle 8 at 53; Cassim op cit note 63 at 457.

Whilst the four committees and their written mandates are compulsory, the composition of the committees and their governance will form part of category five of the accountability scorecard and remain voluntary for the SOC. The composition of the committees must be determined in line with the composition of the board and the nature, size and mandates of the SOC. A regulated approach to the composition of the committees may stifle innovation and not cater to the specific needs of each SOC. As is evident from the SAA Reports, the regulation of the composition of the audit committee did not necessarily result in the efficient performance of its mandate especially with regards to the internal audit function.¹⁶⁷⁰

The SOC may also establish committees in addition to the compulsory ones however, the number of committees should be established with due regard to the nature, size and business of the particular SOC. Too many or too few a number of committees may be counterproductive for the execution of their delegated responsibilities on behalf of the board of the SOC.

The SOC board may set requirements for the frequency and attendance of committee meetings. However, as was illustrated from the SAA Reports, there is no proven link between fulfilment of the minimum number of compulsory meetings and the effective fulfilment of the committee's responsibilities.¹⁶⁷¹ The number of meetings held per year is not as important as the attendance at those meetings and the effective fulfilment of the committee's mandates. Therefore, the number of meetings may be left to the discretion of the board of the SOC and form part of the rating scorecard instead of being legislated.

(c) *The Shareholder*

The SOE Legislation will primarily deal with the governance aspects pertaining to the SOC, and particularly, the accountability of the board. The reciprocal duty of the state, as sole shareholder, to hold the board of an SOC to account for its performance will remain a constitutional obligation.¹⁶⁷² The implementation of the Shareholder Management Bill may also deal primarily with the supervisory role which the state is required to discharge over SOCs and, therefore, inclusion of the state's obligations in the SOE Legislation may be unnecessary.¹⁶⁷³ However, the

¹⁶⁷⁰ SAA Reports op cit note 20; 2013 report at 37; 2014 report at 9; 2015 report at 13; 2016 report at 63; 2017 report at 86; Makwethu (AGSA) op cit note 902 at 119; Makwethu (AGSA) op cit note 18 at 125.

¹⁶⁷¹ SAA Reports op cit note 20; 2013 report at 10; 2014 report at 46; 2015 report at 32; 2016 report at 64; 2017 report at 28.

¹⁶⁷² Constitution op cit note 11 at section 92 (2) & 195 (1)(f).

¹⁶⁷³ PMG op cit note 1649.

addition of the proposed provisions in the SOE Legislation, set out in this chapter, may assist in curbing possible abuses of power which are wielded by the state over the SOC as its sole shareholder.

The abovementioned statutory reform to the appointment, removal and assessment of directors of the board of an SOC may assist in preventing the state from abusing its power as the sole shareholder. The state is alleged to have made appointments to the boards of SOC due to political motivations or as a result of conflicts of interest which meant that the appointments were not made with the best interests of the SOC in mind and to better the composition of the board.¹⁶⁷⁴ The proposed statutory minimum qualification and disqualification criteria for directors coupled with the prior approval of the compulsory nominations committee are improved safeguards in preventing political appointments to the boards of SOCs by the state.

The statutory reward-based enforcement mechanism, in the form of the link between the rating of an SOC and the provision of state funding, is another measure which serves to dilute the power of the state. The state will be unable to continuously bail out poorly rated SOCs without being subject to the provisions of the proposed Rating Agency Act and the maximum funding thresholds. The implementation of this reward-based mechanism will also improve the enforceability of the retribution-based mechanism which entails holding directors of SOCs liable in the event of breach of their duties. The state may be more pro-active in instituting proceedings against recalcitrant directors of SOCs in order to improve their accountability ratings and allow for the provision of more state funding.

The state's duty to hold the board of an SOC to account, whether by reward or retribution is measured under various categories of the scorecard and therefore remains paramount. The addition of a compulsory compliance committee for an SOC will also assist in ensuring compliance by the board with its statutory duties and obligations which shifts the supervisory role to the board and averts the detrimental effects of a complacent state.

Furthermore, the implementation of the rating agency as an independent state institution may also assist in overcoming failures by the state to hold the board of an SOC to account. The establishment of the rating agency will act as an additional accountability check on the SOC, notwithstanding the degree to which the state, as sole shareholder, holds the board of an SOC to account. Therefore,

¹⁶⁷⁴ *OUTA v Myeni* case supra note 346; Muntingh op cit note 1653 at 6.

in the event of a disengaged state shareholder, the rating agency may act as a primary accountability check on the board of the SOC.

The state's ability to abuse its power as the sole shareholder of an SOC may be restricted due to the imposition of the proposed provisions for the SOE Legislation. The state should be incentivized to hold the board of an SOC to account in order to improve its ratings and allow for the provision of more or preferential state funding. The provision of meagre state funding to an SOC as a result of its poor rating may hinder its ability to perform public policy and service delivery mandates on behalf of the state. This should incentivise the state to hold the board accountable to improve the SOC's ratings. If the state is not so incentivized, the rating agency may subsume the role of the state as the primary mechanism for holding the board of an SOC to account through the implementation of the rating system.

(d) *Internal Audit and Company Secretary*

The current statutory provisions pertaining to the internal accountability mechanisms provided by the internal audit and the company secretary for SOCs will largely remain unamended. The SOE Legislation will contain the amalgamated provisions from the Companies Act and the PFMA with regards to the compulsory, internal audit and the appointment of a company secretary for SOCs.¹⁶⁷⁵ These amalgamated regulations in the SOE Legislation will assist with the board's compliance therewith, as any conflicting regulations will be removed and only one piece of legislation will have to be referenced as opposed to multiple.

The current statutory provisions pertaining to the conducting of an internal audit by the audit committee of an SOC are substantial.¹⁶⁷⁶ Arguably, the issue with the internal audit as an accountability mechanism for SOCs lies in its enforceability. Despite being mandated, the Auditor-General alleges in his consolidated report that many SOCs fail to conduct internal audits throughout the year.¹⁶⁷⁷ Retributive measures are seldom levied against the members of the audit committee for failing to conduct the statutory internal audits of the SOC.¹⁶⁷⁸ The implementation of a reward-based mechanism, linking the rating of the SOC to its funding, may incentivize the audit committee members to ensure that the internal audits are conducted in a timely fashion.

¹⁶⁷⁵ PFMA op cit note 11 at section 76 (4); Treasury op cit note 306 reg 27.2.2. & 27.1.10; Companies Act op cit note 11 at section 92 (7)(f)(iii) & 86(1) and (3).

¹⁶⁷⁶ Ibid.

¹⁶⁷⁷ Makwethu (AGSA) op cit note 18 at 114.

¹⁶⁷⁸ Ibid.

The incentivization of the audit members may be a better enforcement mechanism than the current retributive measures for the implementation of the internal audit as an accountability measure.

The addition of a mandatory time period, for which the company secretary may serve the SOC, must be included in the SOE legislation. This will attempt to ensure that the independence of the company secretary is maintained and avoid any potential conflicts of interest which may comprise the ability of the company secretary in the performance of his or her duties. A minimum set of qualification criteria for appointment and mandatory training of the company secretary must be included in the SOE Legislation in order to avoid capacity constraints.¹⁶⁷⁹ Additional qualification criteria may be provided in the founding legislation of an SOC, if required.

The company secretary must also be a mandatory member of the nominations committee to provide guidance on the screening and appointment of directors to the board of an SOC. The company secretary must also attend all nomination committee meetings. The prior approval of the nominations committee must be a statutory requirement in the board's appointment and removal of the company secretary for the SOC.

The board of the SOC will be able to voluntarily implement its own governance structures to further bolster the accountability mechanisms provided by the internal audit and the company secretary. The role of the internal audit of the SOC will be examined by the rating agency under category three of the scorecard. The role of the company secretary will be examined by the rating agency under category five of the scorecard.

(e) *The External Audit*

The mandatory rules regarding the annual external audit of SOCs are comprehensively governed by the PAA, as amended by the PAAA, the APA and the Companies Act.¹⁶⁸⁰ These statutory provisions relating to the appointment of auditors for SOCs will be amalgamated and subsumed under the SOE Legislation, with minor amendments to include the involvement of the nominations committee in the appointment and assessment of the external auditors.

The nominations committee must provide a recommended list to the board of the SOC, comprising its preferred external auditors prior to their appointment every financial year.¹⁶⁸¹ The independence

¹⁶⁷⁹ Companies Act op cit note 11 at section 86 (2)(a).

¹⁶⁸⁰ Companies Act op cit note 11 at section 90 -3; APA op cit note 591; PAA op cit note 595; PAAA op cit note 647.

¹⁶⁸¹ PAA op cit note 595 at section 25(1)(b).

and capacity of the external auditor will be the primary considerations for the nominations committee in its recommendations to the board.¹⁶⁸² The board must select an external auditor from the list provided by the nominations committee which is subject to approval by the Auditor-General.¹⁶⁸³ There must be minimum qualification and disqualification criteria for the appointment of the external auditors under the SOE Legislation. The reasons for the appointment of the auditor by the board, on recommendation by the nominations committee, must be set out in the SOC's annual integrated report.

The maximum period for which an external auditor can be appointed to audit an SOC must be set under the SOE Legislation at a consecutive period of five years which is currently the period stipulated under the Companies Act.¹⁶⁸⁴ Auditors may only apply for the role of external auditor of an SOC after the term of the preceding auditors has expired or upon request by the board of the SOC, in the event of the existing auditors being removed prior to the conclusion of their term. The mandatory rotation of the external auditors of an SOC, every five years, will assist in maintaining their independence. The independence of the external auditors, over their five-year term, will be continuously assessed by the nominations committee in order to avoid any conflicts of interest.

The external auditors may only be removed by the board of the SOC on the expiration of their term or with the consent of the Minister and the Auditor-General, as already prescribed.¹⁶⁸⁵ The reason for the removal of the external auditor must be set out in the SOC's annual integrated report.

A predominant issue, in terms of the external audit function, stemmed from a lack of accountability by the boards of SOC's in failing to: submit annual financial statements, remedy issues identified in disclaimed auditors' opinions or comply with legislation.¹⁶⁸⁶ The available retributive measures were never imposed against directors of SOC's who had failed to comply with their statutory obligations which undoubtedly amounted to a breach of their duties.¹⁶⁸⁷ It is submitted that the fear of punishment is not an effective enforcement mechanism for the accountability of the board of an SOC. The implementation of the proposed reward-based mechanism may improve compliance by directors of SOC's with the financial requirements, including the external audit

¹⁶⁸² King IV op cit note 19 at principle 8 at 115.

¹⁶⁸³ Ibid.

¹⁶⁸⁴ Companies Act op cit note 11 at section 92 (1).

¹⁶⁸⁵ PAA op cit note 595 at section 26.

¹⁶⁸⁶ Makwethu (AGSA) op cit note 18 at 4.

¹⁶⁸⁷ PFMA op cit note 11 at section 63 (2) & 86 (2).

function. The quality of the of the external audit, as well as the external auditors and their independence, will form part of the assessment criteria under category three of the accountability scorecard.

(f) *External Role Players*

There are currently three predominant external institutions which provide effective accountability checks on SOCs. The Auditor-General, the Public Protector and the judiciary currently play an indispensable role in improving the accountability of SOCs. The effectiveness of these institutions largely stems from their ability to retain their independence from the state, despite numerous allegations of state corruption.¹⁶⁸⁸ These institutions have maintained their independence and their ability to function without fear, favour or prejudice, and to take action against SOCs and the state has remained relatively unscathed. However, the mechanisms available to these institutions to enforce the accountability of SOCs and the state needs to be bolstered.

The office of the Auditor-General was recently given extensive statutory powers to curb and prevent fruitless and wasteful expenditure by SOCs.¹⁶⁸⁹ The effect of these newly enforced retributive measures has yet to be fully tested; however, they are expected to assist in the accountability of SOCs and prevent the squandering of state funds.

The office of the Public Protector has proven extremely efficient and capable of investigating the actions and conduct of SOCs and ferreting out those suspected of engaging in corrupt practices.¹⁶⁹⁰ However, the current enforcement mechanism available to the Public Protector in her ability to take appropriate remedial action requires revitalization. The remedies of the Public Protector appear to be ineffectual enforcement accountability mechanisms for SOCs which are seemingly able to circumvent their binding nature.¹⁶⁹¹ Although the Public Protector is able to refer persons suspected of committing a crime during the course of her investigation to the NPA, this is rarely done.¹⁶⁹²

Unless the Pubic Protector avails her office of the retributive enforcement mechanism at her disposal, compliance with her binding remedies will appear to be voluntary. It is submitted that

¹⁶⁸⁸ *Reserve Bank* case supra note 714 para 2.

¹⁶⁸⁹ PAAA op cit note 647 at part 5.

¹⁶⁹⁰ Madonsela op cit note 16; Madonsela op cit note 695.

¹⁶⁹¹ *SABC* case supra note 167 para 60.

¹⁶⁹² PPA op cit note 682 at section 6.

the Public Protector should also be granted extensive statutory powers to hold directors of SOCs personally liable for failing to implement her binding remedies. These powers would be legislated in an amendment of the PPA, in a similar fashion to those given to the Auditor-General in the PAAA.¹⁶⁹³

The three spheres of government: the executive, legislature and judiciary act as accountability checks over one another.¹⁶⁹⁴ The executive has proven itself to be an ineffective accountability check over the performance of its own SOCs.¹⁶⁹⁵ The legislature has, to some extent, executed its role satisfactorily through passing legislation and establishing committees to control and supervise the functioning of SOCs.¹⁶⁹⁶ The functions of the Portfolio Committee, the SCOPA and the Standing Committee on Finance, in supervising the performance and conduct of SOCs, may be amalgamated and subsumed under the role of the committee to be established for the rating agency.

The legislature will be required to pass the legislation in terms of the proposed Rating Agency Act and the SOE Legislation, in fulfilment of its accountability role over the executive in respect of the conduct of its SOCs.

The judiciary remains an effective accountability enforcement mechanism, as its independence has withheld political interference and influence.¹⁶⁹⁷ The judiciary has, over the last decade, been called upon to adjudicate allegations of corruption against the state as well as its numerous SOCs.¹⁶⁹⁸ Unwavering in its integrity, the court system is still the most effective branch of government in the country in terms of maintaining its independence from the other branches of government. Without fear, favour or prejudice, the judiciary has impartially adjudicated upon and granted orders against the state, or the directors of SOCs, when found guilty of corrupt practices.¹⁶⁹⁹

The only proposed improvement to the adjudication function of the judiciary would be the levying of harsher, and more frequent, punishment against recalcitrant SOC directors as an effective deterrent for similar future behaviour. The reward-based mechanism, in the link between the rating of the SOC and the provision of state funding, may also serve as a better enforcement mechanism

¹⁶⁹³ Ibid; PAAA op cit note 647 at part 5.

¹⁶⁹⁴ *Certification* case supra note 726 para 108.

¹⁶⁹⁵ Masuku op cit note 184 at 119; Makwethu (AGSA) op cit note 18 at 38 – 39.

¹⁶⁹⁶ Constitution op cit note 11 at section 43 (1) & 55 (2).

¹⁶⁹⁷ *SABC* case supra note 167; *Eskom* case supra note 1191; *OUTA v Myeni* case supra note 346.

¹⁶⁹⁸ Ibid.

¹⁶⁹⁹ Ibid.

for accountability than the current retributive mechanisms. In addition, the reward-based mechanism may prove more effective for holding SOC directors to account than the outcome of the investigation provided by the Zondo Commission. The investigation and outcome of the Zondo Commission is lengthy, costly and a once-off exercise whereas the SOC ratings will be conducted annually and will form part of the annual national budget.

It is further submitted that as a result of the implementation of the reward-based enforcement mechanism, the public's role as an accountability check on SOCs will dwindle. This will be a welcome reprieve for the state which is currently inundated with various claims emanating from civil rights institutions.¹⁷⁰⁰ Furthermore, civil unrest should decrease as fewer public protests and demonstrations will have to be staged against failing SOCs whose performance is likely to improve as a result of the implementation of the reward-based enforcement mechanism. The role of the public, as an external accountability measure for SOCs, will be restored to an avenue of last resort.

(g) *The SOE Ombuds*

As a result of their limited ability to establish a cause of action and obtain court orders against SOCs and recalcitrant directors, the public should be given a direct avenue to lodge complaints against SOEs, including SOCs. It is proposed that an SOE Ombuds be established for this purpose, as a non-profit company, in terms of the regulations of the SOE Legislation. The primary role of the SOE ombudsman will be the resolution of disputes borne out of complaints lodged against various SOEs by private citizens.

The establishment of the SOE Ombuds will open up an alternative avenue for the public, as opposed to protests and demonstrations against the state. The SOE Ombuds will be established in similar fashion, and with a similar purpose, to the Consumer Goods and Services Ombuds which was established due to enactment of the Consumer Protection Act 68 of 2008.¹⁷⁰¹

6.9 Reform of SOC Corporate Governance

The current corporate governance regime implemented by most SOCs in South Africa entails the application of the recommended practices contained in King IV.¹⁷⁰² King IV contains a sector specific supplement for the application of sound corporate governance practices for SOCs.¹⁷⁰³

¹⁷⁰⁰ *OUTA v Myeni* case supra note 346; Corruption Watch op cit note 1267; Masuku op cit note 184 at 123.

¹⁷⁰¹ Consumer Protection Act 68 of 2008 at section 86 (2)

¹⁷⁰² King IV op cit note 19; Matsiliza op cit note 939 at 42; PWC op cit note 70 at 7.

¹⁷⁰³ Ibid at part 6.6 at 111.

Given the many recent domestic and global corporate failures, many SOCs have taken to adopting the recommended practices from King IV in, arguably, a ‘tick box’ fashion in an effort to assure investors and instil confidence in the public.¹⁷⁰⁴ However, the argument over the causal link between sound corporate governance practices and the performance of the entity is still a hotly debated topic.¹⁷⁰⁵

Notwithstanding this debate, the accountability of the board of an SOC should always be considered of primary importance.¹⁷⁰⁶ Regardless of good or bad performance, the board of an SOC must always account for its decisions which are to be taken in the best interests of the SOC at all times. It is evident from an examination of the SAA Reports that a lack of accountability from the board of an SOC may negatively impact its financial performance .¹⁷⁰⁷ The board and directors of an SOC should focus on the achievement of accountability, regardless of the mechanism utilized of which corporate governance is just one.¹⁷⁰⁸

Accountability is the predominant principle which is lacking in almost all South African SOCs.¹⁷⁰⁹ The accountability scorecard, utilized by the rating agency, contains five categories with various assessment criteria which also comprise elements of fairness, disclosure and responsibility. Therefore, with accountability as the primary principle all of the other principles are inter-related and are also accounted for under the scorecard although they are of a secondary nature. The achievement of accountability may result in the achievement of the other important principles of good corporate governance due to their inter-relatedness.¹⁷¹⁰

King IV has been criticized for failing ensure the actual achievement of the principle of accountability through the implementation of its numerous recommended practices.¹⁷¹¹ It is also submitted that King IV failed to provide adequate recommendations for the specific nature of SOCs and the unique consequences facing them as a result of the state being their sole shareholder.

¹⁷⁰⁴ Davies op cit note 709 at 26; Makuta op cit note 205 at 58; Thabane op cit note 9 at 5; Deniz op cit note 1285 at 220.

¹⁷⁰⁵ Gubert op cit note 1266 at 212; Gloeck op cit note 33.

¹⁷⁰⁶ Corrigan op cit note 1342; Thabane op cit note 9 at 10; Kanyane op cit note 14 at 32; Thomas op cit note 9 at 460; Futuregrowth op cit note 10 at 4.

¹⁷⁰⁷ Ibid; SAA Reports op cit note 20; Masuku op cit note 184 at 123; Makwethu (AGSA) op cit note 18 at 18.

¹⁷⁰⁸ Gloeck op cit note 33.

¹⁷⁰⁹ Futuregrowth op cit note 10 at 4; Kanyane op cit note 10 at 32.

¹⁷¹⁰ King IV op cit note 19 at 5.

¹⁷¹¹ Gloeck op cit note 33; Dullah op cit note 190 at 31; Masuku op cit note 184 at 123.

As illustrated by the SAA Reports, it is evident that an application of the King Codes does not necessarily result in the achievement of accountability of the board of an SOC.¹⁷¹²

Therefore, it is submitted that instead of mindlessly applying the numerous recommended practices contained in King IV, the board of an SOC should comprehensively debate the best mechanism for achieving accountability. The adoption of King IV may not be the best approach for SOCs in the achievement of accountability and it may not even be the adoption of corporate governance practices at all.

The proposed accountability scorecard to be utilized by the rating agency will be legislated while the assessment criteria in each category of the scorecard will be published in the regulations of the proposed Rating Agency Act and may be subject to amendment from time to time. The assessment criteria must always align to corporate trends and the prevailing economic circumstances of South Africa. This will avoid stagnation of the statute as is currently the case with the identification and categorization of various SOEs and SOCs under the PFMA.

It is only the assessment criteria which will be published and not any recommended practices for the achievement of the criteria for SOC directors. This method will attempt to prevent a ‘tick-box’ mentality in mindlessly applying the recommended practices for good corporate governance.¹⁷¹³ The board of an SOC will have the discretion to implement any mechanism it deems sufficient in order to effectively achieve the principle of accountability. The rating agency will then rate the accountability by the SOC, through the scorecard which comprises the five statutory categories and their various assessment criteria.

The outcome of the rating will be presented to the SOC so that the board can improve on the rating score for the following year. The SOC will then also receive state funding, if required, in accordance with its specific rating and the maximum thresholds which are set in accordance with the provisions of the proposed Rating Agency Act.

The establishment of a mandatory governance and accountability committee for the SOC in terms of the SOE Legislation will also assist with the achievement of accountability. This committee will be mandated to ensure that the principle of accountability is achieved by the board of the SOC

¹⁷¹² SAA Reports op cit note 20; 2013 report at 10; 2014 report at 46; 2015 report at 32; 2016 report at 64; 2017 report at 28.

¹⁷¹³ Gloeck op cit note 33.

through the implementation of any mechanisms, practices or structures. The strategic planning of this committee will entail an examination of the various categories and assessment criteria under the proposed Rating Agency Act and its regulations. The committee will be required to ensure that the principle of accountability is actually achieved by the board of the SOC, given its unique nature, size and business operations. The committee will also act as the medium between the rating agency and the SOC by providing information and setting up requisite interviews, thereby prompting an efficient and accurate rating process.

Currently, one of the predominant issues pertaining to the voluntary application of King IV by the board of an SOC, is the lack of an appropriate enforcement mechanism.¹⁷¹⁴ This voluntary application is subjective and discretionary and, as depicted by the SAA Reports, the board of an SOC may claim to have implemented all of the recommended practices in King IV without any evidence of their actual implementation.¹⁷¹⁵ The establishment of an independent, third party rating agency will attempt to resolve this issue of the perceived accountability of an SOC. The rating provided by the rating agency may be a better indication of the mechanisms actually implemented by the board of an SOC in its attempts to achieve accountability, in comparison to the blanket statements which are made in the annual integrated reports.

Furthermore, the link between the rating of the SOC and the provision of state funding will act as a reward-based enforcement mechanism for the achievement of accountability. The more effective the mechanisms which are implemented by the SOC and the greater the level of accountability, the higher the rating from the rating agency. A high rating will attract more funding or funding on preferential terms from the state. Therefore, the directors of an SOC, through its governance and accountability committee, are incentivized to implement effective structures to achieve actual accountability as the provision of state funds to the SOC will have a direct impact on their remuneration or fees and bonus payments.

In the premise, the board of an SOC still has the discretion to employ any method at its disposal, including corporate governance, in order to achieve accountability. The proposed framework for the enforceable accountability of SOCs comprises elements of both retribution-based and reward-based systems. Directors of SOCs who fail to fulfil their duties and obligations may be held

¹⁷¹⁴ Thabane op cit note 9 at 14; Dullah at op cit note 190 at 231.

¹⁷¹⁵ SAA Reports op cit note 20; 2013 report at 10; 2014 report at 46; 2015 report at 32; 2016 report at 64; 2017 report at 28.

personally liable or declared delinquents, in accordance with the statutory retributive measures contained in the SOE Legislation. Directors of SOCs are incentivized, with the possibility of greater remuneration or fees and bonus payments, to obtain high accountability ratings which will result in more, or preferential, state funding in accordance with the proposed Rating Agency Act.

6.10 Conclusion

The proposed framework to resolve the accountability issues facing SOCs involves statutory and corporate governance reform. Accountability will be enforced for SOCs by establishing an independent rating agency act, as a chapter nine state institution, which will annually rate an SOC in terms of an accountability scorecard. The accountability scorecard will contain five uniform categories with numerous assessment criteria. The rating of the SOC will be linked to the provisions of its state funding, on an ascending scale with set maximum funding thresholds. This reward-based enforcement mechanism serves to incentivise the board of an SOC in actually achieving the principle of accountability.

The rating agency will be subject to the provisions of a proposed Rating Agency Act and established through an amendment to chapter nine of the Constitution. An overarching SOE Legislation will govern all aspects relating to SOEs, including SOCs and the proposed statutory provisions will attempt to overcome some of the accountability issues currently facing SOCs. The corporate governance of SOCs will be reformed in that the board of an SOC may achieve accountability under the umbrella of its corporate governance structures or as a standalone principle. The proposed framework for the enforceable accountability of SOCs serves to improve the accountability of an SOC which may, in turn, improve its future performance.

CHAPTER SEVEN: CONCLUSION AND RECOMMENDATIONS

7. Introduction

The accountability and performance of South African SOCs has deteriorated over the last decade. From an examination of the SAA Reports, it is evident that SAA has suffered largescale accountability issues which may have negatively impacted its financial performance. One of the main issues contributing to this lack of accountability for SAA stemmed from the absence of an appropriate enforcement mechanism. Without being enforced, the accountability of the board of SAA has been virtually non-existent. The proposed framework for the concept of enforceable accountability entails a statutory and corporate governance reform for SOCs which may serve to improve their accountability and future performance.

7.1 Recommendations

The current accountability framework for SOCs in South Africa comprises compliance with statutory requirements and the voluntary application of the recommended practices for good corporate governance encompassed under King IV. Despite a plethora of internal and external accountability mechanisms, SOCs still display a chronic lack of accountability. The state's failure to hold the boards of SOCs accountable has significantly contributed to their poor historical track record of performance.

A complacent state has failed to ensure the accountability of the boards of SOCs due to an underutilization of the statutory retributive measures at its disposal. In addition to underutilised retributive measures, the absence of a correlation between the performance of the directors and the SOC and the provision of rewards, in the form of remuneration or fees and bonus packages, has further diluted the enforcement of holding SOC boards accountable. Without the implementation of an appropriate enforcement mechanism, whether in the form of retribution or reward, the board of an SOC is not held accountable for its decision taking which is meant to be in the best interests of the SOC at all times. This failure to account means that decisions may be taken which are not in the best interests of the SOC and, if left unchecked, this may negatively impact the performance of the SOC.

The proposed framework for enforceable accountability attempts to resolve the lack of accountability exhibited by SOCs with the objective of improving their future performance. Well performing SOCs will be less reliant on state funding and the strain placed on the state's limited

resources will be alleviated, to a certain extent. The framework recommends the enforcement of the accountability of the board of an SOC and directors in three main respects. The first two aspects of the recommendations set out the statutory reform and the last one the corporate governance reform for SOCs.

7.1.1 SOE Legislation Proposed Provisions

Firstly, the enactment of an overarching SOE Legislation which will govern all aspects relating to SOEs and SOCs is re-iterated. The proposal of an overarching legislation for SOEs was first made by the Presidential Review Committee on State-Owned Entities in 2012 but has yet to be actually enacted. Therefore, this thesis sets out the basis for a proposal to efficiently enact an overarching SOE Legislation to govern all aspects relating to SOCs which will serve to reduce compliance costs and remove existing contradictions and complexities in the current statutes which govern SOCs.

The amalgamation of the current statutory provisions pertaining to the identification and categorisation of SOCs, with reference to the PFMA and Companies Act (as well as their own founding legislation) in the SOE Legislation will also assist in removing any inconsistencies and clarify the definition of SOEs and SOCs in South Africa.

The proposed statutory provisions in the SOE Legislation may also overcome accountability issues currently facing SOCs such as SAA. The proposed provisions of the SOE Legislation are set out under the subsequent sub-headings.

(a) Directors, Boards and their Committees

For directors, the recommended statutory provisions include: the insertion of a mandatory nominations and removal committee, mandatory training for all directors, regulated minimum qualification criteria for the appointment of directors, the amalgamation of the current statutory director's duties, the insertion of a duty to account and an updating of the current statutory liability provisions in the event of a breach of the duties.

The recommended statutory provisions to assist the board, as a collective body, include: disqualification criteria for independent non-executive directors, constant board evaluations, a mandatory annual assessment and disclosure of the independence of independent non-executive directors, compulsory committees (nominations and removals committee, audit and finance

committee, governance and accountability committee and compliance committee) and a limited number of boards on which an independent non-executive director may serve in any given year.

It is recommended that board and committee composition as well as the governance of board and committee meetings, in terms of frequency and attendance (but excluding notices, quorums, adjournments, minutes and resolutions which should remain regulated) should be at the discretion of the SOC and not be regulated which may result in a restrictive one-size fits all approach. Board and committee composition and governance, limited to the attendance of meetings and the frequency of such meetings, should be set by the SOC with reference to its nature, size and business.

(b) The State

The state's reciprocal duty, as sole shareholder, to hold the board of an SOC accountable will also be addressed through the proposed statutory provisions. The state will no longer be able to solely appoint and remove directors as it will require the prior approval of the mandatory nominations committee of the SOC. Furthermore, the addition of mandatory minimum qualification criteria for director appointment may serve to curtail the number of political appointments to the boards of SOCs. The extension of the independence of independent non-executive directors to prevent the appointment of persons related (or interested parties) to the state may also reduce the number of political appointments.

The addition of a compulsory compliance committee for an SOC may also assist the state in holding the board accountable for its compliance with relevant legislation. The imposition of set maximum funding thresholds which are linked to the rating outcome of the SOC will also dilute the power of the state by curtailing the state's ability to provide funding to an SOC, without limitation.

(c) Company Secretary and Audits

The role of the company secretary in the accountability of SOCs will also be bolstered through the statutory provisions which include: minimum qualification criteria for the appointment of the company secretary, the imposition of a maximum tenure, mandatory inclusion as a member of the nominations committee and mandatory training for directors.

The proposed statutory provisions will also cover some of the issues associated with the internal and external audit of the SOC. The internal and external audit process will remain largely the same

as currently contained in relevant statutes. However, the addition of the statutory reward-based mechanism, in linking the funding of the SOC to its rating, may serve as a better enforcement mechanism to incentivise the directors to actually conduct internal audits and to ensure that a proper independent, external audit is conducted every year. The external auditors will only be appointed on recommendation by the nominations committee, subject to the satisfaction of the minimum qualification criteria (with a strict focus on independence) and for a maximum period of five years.

(d) SOE Ombuds

It is lastly recommended that the statutory provisions propose the establishment of an SOE Ombuds to resolve disputes from complaints lodged with it by the public against SOEs, including SOCs.

7.1.2 The Rating Agency Act

Secondly, it is recommended that a Rating Agency Act be enacted which will establish a rating agency as an independent, state institution under chapter nine of the Constitution. The statutory reform of this proposal will include the enactment of national legislation as the Rating Agency Act to govern all aspects relating to the rating agency and rating process and an amendment to chapter nine of the Constitution to establish the rating agency as an independent, state institution.

The proposed Rating Agency Act will implement a statutory scorecard with five uniform categories containing various assessment criteria against which the accountability of SOCs will be rated. The five uniform categories will be: understanding the ownership and board structures, the accountability of the board, compliance, stakeholder relations and support mechanisms. The assessment criteria are contained in the regulations to the proposed Rating Agency Act and are subject to amendment, from time to time, to ensure their alignment with the prevailing socio-economic circumstances in South Africa and global corporate trends.

The proposed Rating Agency Act will also set out a mandatory link between the rating of the SOC and the provision of state funding to the SOC, with maximum set thresholds based on the level of rating achieved, on an ascending scale. This mandated link will serve to incentivize the board of the SOC to achieve actual accountability and a high rating in order to receive more or preferential state funding. The implementation of the link between the rating of the SOC and the provision of

state funding is to act as a reward-based enforcement mechanism for the accountability of the board of an SOC.

This enforcement mechanism will also serve to incentivise the state, as sole shareholder, to hold the board accountable as it will no longer be able to provide state funding at its sole discretion to SOCS (many of which discharge public policy functions on behalf of the state).

7.1.3 Corporate Governance Reform

Thirdly, it is proposed that the focus by the board of the SOC is the achievement of accountability as a standalone principle or under the umbrella of the corporate governance recommended practices under King IV. This approach deviates from the current approach in that SOCs predominantly utilise only corporate governance methods to attempt to achieve accountability. Whilst corporate governance structures may also be implemented by the board of an SOC, its priority should be the achievement of accountability through the implementation of any mechanisms, structures or practices. The achievement of accountability remains at the discretion of the board of the SOC and is not regulated through legislation.

The addition of the reward-based enforcement mechanism also shifts the focus from punishing the directors in the event of a breach of their duties to rewarding them for fulfilling their duties. The enforceable accountability framework includes a combination of the current retributive measures, with slight variations to the statutory liability provisions and the proposed reward measures, largely in the form of linking the rating of the SOC to its state funding, on an ascending scale.

The achievement of accountability by the board of an SOC will be one of the categories of the mandated, uniform scorecard of the rating agency and is an underlying principle throughout the other categories and assessment criteria of the scorecard. This proposed enforceable accountability framework is designed to ensure the actual achievement of accountability which may serve to improve the future performance of SOCs.

7.2 Possible Issues

The implementation of the proposed framework for the enforceable accountability for SOCs may encounter its own issues. The initial set up costs of the rating agency, through the implementation of the proposed Rating Agency Act, may deplete valuable state resources. The logistics in administering the rating agency may initially prove overwhelming for the strained capacity of the executive. The implementation of legislation and the ability of the rating agency to conduct its first

rating may involve lengthy processes and procedures over which period many SOCs may further deteriorate. Many more SOCs may go into business rescue or possibly liquidation proceedings.¹⁷¹⁶ The costs associated in waiting for the implementation of the requisite legislation may be too high and result in irrevocable consequences for many SOCs.

However, the long-term benefits of accountable and well performing SOCs should outweigh the initial set up and administration costs. The government should call upon available resources and the assistance of governance experts in order to effectively establish the rating agency, enact the SOE Legislation and the proposed Rating Agency Act and assist in the agency's first rating. The assistance of governance experts, such as the Institute of Directors South Africa, may also serve to reduce the timeframe for the implementation of this reform which will prove invaluable for many rapidly deteriorating SOCs. The executive and legislature should make the implementation of this reformed framework a priority to foster the long-term sustainability of financially underperforming SOCs and reverse the drain which these SOCS have on the state's limited resources.

Another issue for the proposed framework may stem from the rigidity of the statutory provision of state funding to SOCs based on their accountability ratings. There are no proposed exceptions to the maximum thresholds, or preferential terms, for the provision of state funding to SOCs which is linked to their ratings. This omission of exceptions means that the state is afforded no discretion and is not able to deviate from the provisions of the proposed Rating Agency Act. The state is only able to provide funding to the SOC in accordance with the maximum thresholds contained in the proposed Rating Agency Act.

The availability of exceptions for the state may ultimately result in an abuse of power in terms of the provision of funding to SOCs. The implementation of the rating agency and the link between the rating of the SOC and the provision of state funding is meant to prevent possible abuses of power by the state. However, the rigidity of these statutory provisions may result in many more SOCs facing possible business rescue or liquidation proceedings in the event of consistently poor ratings for which they receive limited state funding. It is therefore submitted that the only way to remedy this issue would be to implement the proposed framework for the enforceable

¹⁷¹⁶ SAA op cit note 18.

accountability of SOCs and to adjudicate it on a trial and error basis before any possible amendments are initiated to the reform after conscientious deliberation.

7.3 Concluding Remarks

The accountability and performance of SOCs has been a hugely detrimental issue for the South African economy over the last decade. Arguably contributing to the inevitable downgrade to junk status, these financially underperforming SOCs have placed a huge strain on the state's limited resources. Many SOCs have become fully reliant on state funding, despite their categorisation as '*Enterprises*' which means that they should be capable of financial independence due to the successful discharging of their commercial mandates.

As a developing economy with many SOEs to support, who aren't capable of being financially independent from the state, these SOCs are in need of a reform to improve their financial performance and alleviate their drain on the state's resources.

Not without its own possible issues, the proposed enforceable accountability framework provides a stepping stone to improving the accountability and performance of SOCs. With the implementation of the proposed statutory and corporate governance reform set out in this thesis, underperforming SOCs may once again become financially independent from the state. The enforceable accountability of SOCs serves to improve their accountability and future performance which will, in turn, alleviate their reliance on state funding thereby assisting in the growth and development of the South African economy.

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