

CHAPTER FIVE

5. CORPORATE GOVERNANCE

“Corporate governance is concerned with the ethical principles, values and practices that facilitate holding the balance between economic and social goals and between the individual and communal goals. The aim is to align as nearly as possible the interests of individuals, corporations and society within a framework of sound governance and common good”.

Objectives, Standards, Criteria and Indicators for the APRM,
6th Summit of the NEPAD HSGIC, 9 March 2003, Abuja, Nigeria

5.1 Overview

411. Corporate governance in South Africa must be situated within the wider macroeconomic framework of the country. Occupying only 3 per cent of the continent’s surface area, the country produces 25 per cent of Africa’s gross domestic product (GDP), which reflects its status as an economic powerhouse in the region. South Africa also accounts for about 40 per cent of all industrial output and over half of all generated electricity. Its mining industry constitutes 45 per cent of all mineral production in Africa, with exports to as many as 87 countries. Gold, platinum, coal and diamonds dominate the export and revenue earnings.
412. Other strengths include an excellent physical and economic infrastructure, growing manufacturing sector and tremendous growth potential in tourism and the service industry. The country is also well positioned technologically to compete in the global market. Its communication system is well developed, with about 5 million installed telephones, 4 million installed exchange lines and 14 million mobile telephone users. The network is entirely digital and the main transmission media are microwave and fibre-optics. Internet access is widely available.
413. Private and state-owned corporations produce the bulk of South Africa’s goods and services, both for export and domestic consumption. They manage most of its capital stock, are central to the allocation of investment and are responsible for virtually all of the country’s savings. Over the last 13 years, corporations have mobilised more than 75 per cent of South Africa’s domestic savings, allocated and planned 85 per cent of all investment, and currently own and manage three-quarters of the capital stock. The corporate sector and corporate governance are inevitably crucial to South Africa’s development, particularly in the light of the political transformation that has been taking place since 1994.





414. Prior to the advent of democracy, the economy was dominated by six mining finance houses.²⁶ By 1994, five of these conglomerates controlled 84 per cent of the then Johannesburg Stock Exchange, with Anglo Gold alone accounting for 43 per cent of its market capitalisation (i.e. the value of all the shares). Currently, the mining finance house no longer exists. Attempts have also been made to unbundle conglomerates, pyramid schemes and other elaborate control structures. South African companies have been warmly welcomed into the international fold, accompanied by increased investment by multinational corporations in South Africa. By 2005, more than 600 American, 450 German and 200 British companies had a corporate presence in South Africa, together with other corporations from all continents.
415. In 2005, the World Federation of Exchanges ranked the JSE Securities Exchange (JSE) the 16th largest financial exchange in the world, with a domestic market capitalisation of about US\$550 billion. The JSE's market capitalisation stands at approximately 1.65 times the GDP (excluding cross-holdings), which is higher than comparable figures for developed countries such as the United Kingdom (UK), France, Germany and even the United States (USA). The JSE is ranked among the top ten performing stock exchanges in the world in local currency terms. It is ranked second globally for single stock futures.
416. South Africa has a highly sophisticated banking system ranking with the best in the world, having been rated tenth globally. Barclays Bank's acquisition in 2005 of ABSA, the country's largest consumer bank, provides good prospects for banking in Africa, as the merger is deemed to have created the leading bank on the continent.
417. South Africa's exports to the rest of Africa have grown exponentially during the past 13 years and currently exceed those of the USA and the European Union. This has been accompanied by the expansion of local companies investing in the region, in areas such as mining, construction, agriculture, tourism, hospitality, manufacturing, telecommunications, transport, oil and gas.
418. In tandem with these developments have been the changes made to legislation, regulations, listing rules and accounting standards to bring them in line with international norms, such that South Africa currently rates among the top performers in corporate governance in emerging markets.
419. Worthy of mention is the development of the King I and II Reports which, though home-grown in South Africa, have received international acclaim for their comprehensiveness and are widely used. The first report, published in 1994, made a significant contribution to corporate governance law reform and was aimed at boosting the competitiveness in South Africa's private sector following the country's reintegration into the global economy. The 2002 King II Report has had great impact in enhancing corporate social responsibility (CSR). It forms the basis of the triple bottom line (TBL) concept, which requires companies to report on such matters as social transformation, ethics, environment and socially responsible investment.

²⁶ Mining finance houses were holding companies characterised by a conglomerate structure with diversified holdings, and entrenched control through pyramid structures.

420. In all, the regulatory framework for economic activity in South Africa is adequate. Many stakeholders, however, agreed that the Companies Act of 1973 that regulates business is outmoded and in need of major change. A Corporate Law Reform Project was initiated in 2002 and is ongoing. Amendments are also envisioned for bankruptcy and insolvency laws and legislation relating to technical standards and regulations. There are mixed views on the adequacy of labour laws. Some observers argued that they are overprotective and adversely impact on production, productivity and the creation of jobs. The challenge is to balance economic growth with adequate safeguards for workers, given the historical background of the country. The matter remains in public discourse.
421. South Africa has taken steps to reform its laws to ensure full participation in business by historically disadvantaged groups. Most notable of these reforms are the black economic empowerment (BEE) and broad-based black economic empowerment (B-BBEE) strategies, as well as related codes, sectoral charters and various microfinance schemes.
422. Despite efforts to enable the economically marginalised groups to enter the mainstream economy through institutional and legislative reform, South Africa continues to operate two economies – one advanced and sophisticated with first-class infrastructure and competitive industries, and the other informal and characterised by high levels of poverty and unemployment. Poverty among South Africa's disadvantaged populations is exacerbated by high HIV and AIDS rates. The high incidence of crime has been attributed to poverty and inequality and is a cause for concern to both domestic and foreign investors.
423. The fundamental challenge South Africa faces is how to design a corporate governance system that works for its dual economy and, in the long run, will succeed in bridging the gap between the first and second economies and ameliorate the plight of historically disadvantaged groups. The question is how the private sector can assist in tackling the social challenges of enhanced job creation. How can corporations juxtapose the shareholder wealth maximisation model with issues of CSR and investment? How can corporate governance be used as an instrument for wealth creation and redistribution and for addressing ingrained social inequalities? What kind of public-private partnerships (PPP) would be effective for dealing with these challenges?
424. In raising these questions, the progress and transformations South Africa has made in corporate governance are recognised. A great deal of goodwill and support is evident from private sector players such as Business Unity South Africa (BUSA), individual banks and mining companies through initiatives such as the Financial Sector and Mining Charters, the Mzansi Account for the un-banked, skills development measures, and PPPs in the development of infrastructure. While these should continue, they need to be reinforced by all players to be able to confront the fundamental rift between the first and second economies.





5.2 STANDARDS AND CODES

i. Summary of the CSAR

425. The CSAR lists the eight corporate governance standards and codes contained in the APRM's Objectives, Standards, Criteria and Indicators (OSCI). It does not, however, provide specific information on the dates of their adoption or accession, except for the African Charter on Human and People's Rights (ACHPR), which South Africa ratified on 9 July 2006.

ii. Findings of the CRM

426. Due to this omission in the CSAR, the CRM interrogated government officials and other stakeholders on the status of implementation of the country's corporate governance standards and codes. These deliberations confirmed that South Africa has made tremendous progress in their implementation.

Principles of Corporate Governance

427. South Africa has adopted the principles of corporate governance designed by the Organisation for Economic Cooperation and Development (OECD) and Commonwealth associations. The Institute of Directors (IoD) launched an initiative led by Judge Mervyn King, which resulted in the development of the King I and II Reports on corporate governance. These reports recommend principle-based benchmarks, rather than legally binding prescriptions, for a modern code of corporate governance. The King II code has been incorporated into the requirements for companies listed on the JSE, which they have to comply with or provide an explanation for non-compliance. It is, however, voluntary for all companies not listed on the JSE. These codes also apply to the three spheres of government and all public entities, including state-owned enterprises (SOEs). South African companies operating outside of the country are expected to apply the standards of the King II code in their operations.

428. The CRM discussed extensively with several stakeholders – including Judge Mervyn King, the IoD, JSE, the South African Reserve Bank (SARB) and the business community – whether the requirements of the King II Report should be legislated. Caution was expressed about being too stringent in this matter, as it could place a compliance burden on companies without adding much value. Comparisons were made with the Sarbanes-Oxley Act of 2002 that regulates corporate governance, financial disclosure and public accounting in the USA. American companies have had to invest heavily in technology enabling them to comply with the US Securities and Exchange Commission (SEC) rules and regulations under the Act. For example, Open Pages, the leading provider of governance, risk and compliance management solutions for Sarbanes-Oxley Compliance, projected that the average company spent between US\$100 000 and US\$1 million on compliance software in 2005.

429. Stakeholders were also concerned about overburdening small and medium enterprises (SMEs) with compliance costs if the code were to be legislated. For instance, it was observed that the 2006 report by the US Senate Committee on Small Businesses and Entrepreneurship found that compliance costs for the Sarbanes-Oxley measures were disproportionately higher for small businesses than for larger companies. Another reason given was that legislation may not necessarily forestall abuse and, in fact, runs the danger of taking a tick-box approach to compliance.
430. The CRM noted the reasons advanced for non-legislation of the King II Report, in particular the regulatory and compliance burden for SMEs. The CRM holds the view that, given the arguments against codifying corporate governance standards, it may be imprudent to legislate these codes wholesale. Nonetheless, the CRM is convinced that modalities should be found through existing and other legal frameworks to enhance corporate governance practices at enterprise level. For example, poor corporate governance in insurance companies has been blamed on the lack of supportive legislation. The CRM encourages dialogue and discourse among stakeholders so that consensus can emerge on the optimum level for legislation of the King Reports and other codes on corporate governance.
431. The CRM noted the concern raised in the CSAR that some South African companies operating elsewhere in Africa were not adhering to the King II code. Both the government and the business community were aware of certain instances where this has occurred, but do not condone this conduct. Modalities for managing the issue are being explored. This would entail, for example, ensuring that South African multinational companies (MNCs) comply with the new framework for corporate reporting under the Global Reporting Initiative (GRI), which fosters transparency and accountability of corporate activities beyond financial matters.

International Accounting Standards

432. Accounting standards were discussed at a meeting with the South African Institute of Chartered Accountants (SAICA). The CRM learnt that South Africa has adopted the International Accounting Standards (IAS) and that South African companies have been required to comply with the International Financial Reporting Standards (IFRS) since 1 January 2005. At the time of writing this Report, these standards did not yet have legal backing. However, the proposed Companies Amendment Bill will give legal backing to the IAS.
433. The CRM noted the concern expressed in the CSAR about the absence of effective mechanisms for regulatory enforcement. According to the 2003 Report on the Observance of Standards and Codes (ROSC) of the International Monetary Fund (IMF), this situation facilitated uncontrolled manipulation of accounting policies. According to the ROSC, many companies have highly skilled accountants and auditors available to them who use sophisticated accounting manipulations that may not be evident from a reading of financial





statements. As a result, non-compliance with established accounting standards takes place, even while giving the appearance of full compliance.

434. The CRM was informed that this shortfall necessitated the creation of the Monitoring Panel of Generally Accepted Accounting Principles (GAAP) by the JSE and SAICA as a private sector body to enforce accounting standards for listed companies. This body will be replaced by a Financial Reporting Council (FRC) that will give guidance on reporting standards once the new Companies Act is in place. Overall, the CRM is of the impression that current reforms to laws impacting on accounting, such as the proposed Companies Act and Auditing Profession Act (APA) of 2005, would improve disclosure and safeguard the integrity of the accounting and auditing professions.
435. The difficulty SMEs experienced in applying accounting standards at the same level as larger companies was raised in the discussions. The CRM learnt that, due to capacity constraints, there are challenges in implementing the Public Finance Management Act (PFMA) of 1999 and the Municipal Finance Management Act (MFMA) of 2003. Collaborative efforts are being made by the government, SAICA and other players to address the issue. The new Companies Act groups companies into public interest and limited public interest companies. SMEs would fall in the latter group and hence could be allowed to use simplified accounting standards.

International Standards on Auditing

436. The CRM was informed that South Africa has adopted international standards on auditing and developed a number of standards to complement these. The King II Report also recommends that interim financial statements be audited.
437. Worthy of note is the new APA signed into legislation by President Mbeki in January 2006. The Act is to be implemented in phases, the first of which came into effect on 1 April 2006. Its purpose is “to provide for the establishment of the Independent Regulatory Board for Auditors (IRBA); to provide for the education, training and professional development of registered auditors; to provide for the accreditation of professional bodies; to provide for the registration of auditors; to regulate the conduct of registered auditors ...”
438. The Act seeks to improve the integrity of South Africa’s financial sector and financial reporting by introducing a more comprehensive, modern legislative framework for overseeing and regulating the auditing profession. As noted earlier, there are also provisions in the proposed Companies Amendment Bill that entrench and safeguard the independence of auditors within the corporate environment, inter alia, by providing for the rotation of audit partners.

Core Principles of Effective Banking Supervision

439. Due to the global operations of the South African banking sector, the best international standards of banking regulation and supervision are employed. Corporate governance in

South African banks is also sound, as evidenced by the report of the Myburgh Commission in 2003. The study by Judge Myburgh covered five of the country's largest banks (the Standard Bank Group; ABSA; the FirstRand Group, which includes First National Bank Limited; Investec; and the Nedbank Group) and found that these banks were committed to the highest standards of corporate governance. As a result, South African banks operate easily outside the country and, similarly, foreign banks are attracted to South Africa because of the good supervisory environment.

440. South Africa's commitment to maintaining high standards of governance in the banking sector also extends to cooperation with, and assistance to other bank supervisors in the Southern African Development Community (SADC). Matters of common interest include the harmonisation of supervisory and accounting practices, training of supervisors, development of technology-based systems and measures to combat money laundering.
441. The CRM met with the SARB about the progress being made with regard to South Africa's declared position to adopt the "International Convergence on Capital Measurements and Capital Standards: A Revised Framework", or Basel II, which was issued by the Basel Committee in June 2004. The CRM learnt that the announced implementation date for the country's banks was 1 January 2008. As regulator, the SARB will evaluate the impact of the new framework on capital requirements and risk management processes during a parallel run to be conducted for a year prior to implementation (commencing on 1 January 2007). Indications are that the country's main banks will be ready for implementation of the Basel II Accord by the due date. It was also acknowledged that aligning all banks to the Basel II framework would require significant investment, both in time and resources.

Core Principles of Securities Supervision and Regulations

442. The CRM met with the Financial Services Board (FSB), which is responsible for supervising financial services except banks. The CRM learnt that South Africa has adopted the 30 Core Principles of Securities Regulations of the International Organisation of Securities Commissions (IOSCO). These form the basis of the regulations designed by the FSB.
443. South Africa has adopted the Insurance Core Principles of the International Association of Insurance Supervisors (IAIS). The CRM was informed that the FSB undertook a self-assessment in February 2005 and found that the country "observed" or "largely observed" all but Principle 9 (which deals with corporate governance) and Principle 28 (which is concerned with anti-money laundering and combating financing of terrorism). These latter two principles were rated as "partly observed".
444. Partial observance of the corporate governance principles was ascribed to the lack of supporting legislation via the Companies Act of 1973, leading to reliance on administrative requirements alone. Although adherence to the King II Report is required by the Registrar of Insurance in terms of Directive No. 38 as a registration condition, this would only be





monitored through on-site visits. It is neither legislation nor a regulation and is therefore not enforceable.

445. The FSB deals with anti-money laundering by requiring that information on the policies, procedures and records for the Financial Intelligence Centre Act (FICA) of 2001 be submitted in insurers' returns. However, the supportive Act passed in 2003 is still relatively new and the Financial Intelligence Centre charged with oversight of the implementation of legislation was established only in 2004. Furthermore, there is no dedicated staff at the FSB responsible for anti-money laundering legislation.
446. The Financial Intelligence Centre was established by the FICA of 2001. The Act states that the purpose of the Centre, together with the Money Laundering Advisory Council also established under the Act, is "to combat money laundering activities; to impose certain duties on institutions and other persons who might be used for money-laundering purposes; to amend the Prevention of Organised Crime Act of 1998 and the Promotion of Access to Information Act of 2000; and to provide for matters connected therewith."
447. The CRM learnt that Banks are doing well in implementing the "Know Your Customer" obligations in the fight against money laundering. The FSB felt there was room for improvement in the execution of anti-money laundering requirements in insurance companies, based on results of the aforementioned self-assessment on Principle 28 of the Insurance Core Principles.
448. South Africa is recognised as a strategic country in international finance. In 2003 it was welcomed as the first African country and the 30th member of the Financial Action Task Force (FATF), a group that deals with anti-money laundering and combating terrorist financing.

Labour Codes

449. The backdrop to South Africa's accession to a number of conventions of the International Labour Organisation (ILO) is the political history of the country, which is dotted with discrimination and abuse of certain categories of workers under the apartheid regime. Political unrest in the 1950s led to the amendment of the Conciliation Act of 1956 to have more control over the activities of, and the role played by black workers in the national economy. The establishment of the Wiehahn Commission in 1979 totally changed the outlook of the labour relations and labour laws of South Africa. One of the most profound recommendations made by the Commission was the extension of freedom of association to cover all persons, irrespective of race or gender. Thus, for the first time, trade unions representing black workers were able to make full use of the Labour Relations Act of 1956.
450. South Africa has signed all the fundamental conventions of the ILO and therefore recognises the following principles and rights of workers: freedom of association; the right to collective

bargaining; elimination of all forms of forced or compulsory labour; the effective abolition of the worst forms of child labour; implementation of minimum ages of employment, as stipulated in ILO Conventions 182 and 138; and the elimination of discrimination in respect of employment and occupation.

451. South Africa has also signed the priority conventions of the ILO relating to such issues as: labour inspection in all workplaces; a labour inspection system in agriculture; tripartite consultation (member countries commit to operating procedures that promote effective consultations between representatives of the government, employers and workers on ILO-related matters); and Convention 122 of 1964, referred to as the Employment Policy Convention. The aims of the Convention are to stimulate economic development, raise the standards of living and overcome problems of unemployment and underemployment.
452. Following the advent of democracy in South Africa and the adoption of the Interim Constitution in 1994, it became evident that the Labour Relations Act of 1956 was in conflict with key clauses of the Interim Constitution. A Ministerial Legal Task Team was appointed to draw up new labour legislation, which resulted in the Labour Relations Act of 1995, later amended in 2002. Other legislation impacting on labour law includes: the Basic Conditions of Employment Act of 1997; Skills Development Act of 1998; Unemployment Insurance Act of 2001; Occupational Health and Safety Act of 1993; and the Compensation for Occupational Injuries and Diseases Act of 1993. The country has also instituted policies aiming at promoting equality and harmony on the labour front, such as the Employment Equity Act (EEA) of 1998, the Growth, Employment and Redistribution (GEAR) Strategy, and BEE models.

Codes on Industrial and Environmental Safety and Hygiene

453. From documents that are publicly available, the CRM learnt that South Africa is a signatory to several industrial and environmental safety and hygiene treaties. It has also promulgated domestic laws, such as the Mine Health and Safety Act of 1996 and National Environmental Management Act (NEMA) of 1998 to promote safety and hygiene, especially in the workplace.

Monitoring and Enforcement of Compliance of Codes and Standards

454. Implementation of codes and standards in South Africa is supported by a wide variety of oversight and regulatory institutions. These include the Ministry of Finance for financial regulation, the FSB in the non-banking financial sector and the SARB in the financial sector. Others are the Accounting Standards Board (ASB), the Registrar of Companies located at the Department of Trade and Industry (DTI), the JSE and the Securities Regulation Panel (SRP). There are also sector-specific regulators (for competition, gambling, etc.) whose oversight functions are targeted and serve a specific purpose. In addition, there is a good number of self-regulatory and professional bodies, most of which adhere to high standards. As a result of the National Credit Act of 2005, the National Credit Regulator was established in June 2006 to oversee and regulate entities





giving credit to more than 100 people per annum and charging interest on the credit extended.

455. Some stakeholders voiced their concern about overregulation, noting that the plethora of oversight institutions, particularly in financial services supervision, often led to compliance and enforcement pitfalls due to multiple reporting obligations. They observed that there may be a need to consolidate some of these obligations.
456. When the CRM raised the issue of a multi-sector regulator for South Africa, it was informed of discussions around the establishment of a single regulator for the financial services sector, encompassing the SARB's Banking Supervision Department and the FSB, but that the country had not yet decided to move in this direction. Some of the considerations herein relate to capacity constraints.

iii. Recommendations

457. The APR Panel recommends that South Africa:
- Take steps to oversee and enforce adherence to the King II Report and the GRI by South African companies operating elsewhere on the continent in all aspects of their operations. [Government; Oversight Institutions; BUSA; Companies Operating in Africa]
 - Enhance capacity at the provincial and municipal levels to comply with the requirements of the IAS, PFMA and MFMA. [SAICA; IRBA; Professional Accounting Bodies; Government]
 - Assist smaller banks in aligning with the Basel II framework. South Africa is also encouraged to continue the supportive role it is playing in southern Africa to inform and build capacity on Basel II issues. [Government; SARB; Banks]
 - Enhance enforcement of the ILO codes through inspection and site visits, in particular in labour-intensive factories and on rural farms where these laws are often wantonly abused. [Department of Labour; Trade Unions; Civil Society; Employers]
 - Step up surveillance, monitoring and enforcement roles in each of the mandates of oversight institutions. Greater coordination is needed among these institutions. [Government; Ministry of Finance; SARB; Oversight Institutions]
 - Continue discussions on the multi-sector regulator, in particular between the FSB and the SARB, to find modalities for further strengthening and streamlining supervision of the financial services sector. [Ministry of Finance; Treasury; SARB]

5.3 Assessment of the Performance on APRM Objectives

Objective 1: To Promote an Enabling Environment and Effective Regulatory Framework for Economic Activities

i. Summary of the CSAR

Commercial Enterprises and the Economy

458. South Africa's well-developed economy includes large and well-established enterprises and conglomerates, a number of SMEs and a large number of micro-enterprises, the majority of which are survivalist. The CSAR notes that over 75 per cent of South Africa's production is generated by private business. SOEs account for approximately 25 per cent of capital stock in South Africa and generate a disproportionate 33 per cent of all savings.

Regulatory Framework

459. Key laws governing corporate affairs in South Africa are the Companies Act of 1973, Close Corporations Act of 1984 and Cooperatives Act of 2005. Other government legislation with a direct impact on corporate governance includes: the Labour Relations Act of 1995; Basic Conditions of Employment Act of 1997; National Environment Management Act of 1998; Insider Trading Act of 1998; Promotion of Access to Information Act of 2000; EEA of 1998; and Securities Services Act (SSA) of 2004.

460. In the public sector the PFMA of 1999, MFMA of 2003, Treasury Regulations and Companies Act of 1973 govern public sector reporting and accountability. The CSAR recognises that there is lack of clarity on the accountability mechanism for public bodies, particularly with regard to the parliament's oversight role.

461. The Broad-Based Black Economic Empowerment (B-BBEE) Act of 2003 aims at creating an enabling framework within which the government and business can contribute to BEE by, for example, publishing codes of good practice and entering into sectoral transformation charters.

462. The FICA is in place to counter money laundering and international crime. Laws for regulating specific sectors of the financial industry include: the South African Banks Act of 1990; Long-Term Insurance Act of 1998; Short-Term Insurance Act of 1998; and Collective Investment Schemes Act of 2002. The Auditing Industry is regulated by the APA of 2005.





463. The Competition Act of 1998 provides mechanisms for creating and regulating a fair business environment. Generally, consumers are protected under the Credit Agreements Act of 1980. South Africa has also updated its regulatory framework for technical and standards regulations and trade administration, especially for anti-dumping and tariff administration.
464. Overall, the regulatory framework is noted as being adequate, although a few problematic areas are currently under review. One of these is the Companies Act of 1973, which is seen as highly formalistic and imposes unnecessary compliance burdens on the investor. The CSAR also points out that the time it takes to register a company can be shortened. Other laws proposed for amendment include bankruptcy and insolvency laws and legislation relating to technical standards and regulation.
465. Another issue flagged in the CSAR concerning the regulatory framework relates to commercial dispute resolution. It is noted that the judicial system is highly burdened with criminal matters and consequently pays insufficient attention to civil matters.
466. The CSAR outlines the supervisory authorities responsible for oversight of the business environment in South Africa. It is further noted that the government and banking, insurance and financial sector regulators are generally considered effective. However, the CSAR observes that some self-regulatory bodies are primarily seen as mechanisms for lobbying for the government.

Banking System and Access to Finance

467. The banking sector is described in the CSAR as stable and sophisticated, with four large banks and smaller niche institutions supporting medium and large business with debt and equity financing options.

South Africa's Exchanges

468. The CSAR notes that the JSE is a large and very liquid stock market, ranked 16th in the world. A secondary board, the Alternative Exchange (AltX), lists smaller businesses, while a Socially Responsible Investment (SRI) Index highlights JSE-listed companies operating in the areas of socio-economic and sustainable development. The Report highlights the significant technological and cost-effective measures developed in the last ten years at the JSE, which can be described as a best practice in Africa. It notes that under JSE rules, companies are obligated to: disclose price-sensitive information in advisory and cautionary public trading statements; declare director interests; disclose related party transactions; and publish interim reports, quarterly results and annual financial statements.
469. No information is contained in the CSAR on the Bond Exchange of South Africa (BESA) or the South African Futures Exchange (SAFEX).

Infrastructure

470. The CSAR refers to international benchmarks indicating that the economic infrastructure in South Africa is “of reasonable quality”. It notes that a total 271 712 gigawatt hours of electricity were generated in the country in 2002, produced almost entirely from coal, and that South African electricity is low cost. The country has 20 796 km of rail track, 63 177 km of paved roads, three international airports, 4.844 million fixed telephone lines and 13.9 million mobile telephone users. Access to water is good in urban areas but lags behind in rural areas.

Small, Medium and Micro-Enterprises

471. The CSAR states that the national strategy for small, medium and micro-enterprises (SMMEs) has two objectives, namely to promote the growth of SMMEs so as to generate employment and promote income redistribution, and to redress the discrimination experienced by historically disadvantaged groups in accessing finance.
472. In this regard, the government introduced the Small and Medium Enterprise Development Programme to facilitate the entry of women in business. A National Strategy for the Development and Promotion of Small Business in South Africa has also been created to foster an enabling environment for small business. Key institutions for funding SMMEs are the Small Enterprise Development Agency (SEDA), Khula Enterprise Finance, the National Small Business Council and provincial SMME desks. The government has embarked on two funding initiatives: the South African Micro-Finance APEX Fund and Land Bank, both of which promote the agricultural sector and seek to ensure the equalisation of benefits to disadvantaged groups such as women and people with disabilities.

Investment Promotion

473. The CSAR notes the presence of several state-owned entities and development finance institutions (DFIs) that promote private sector growth, such as the Development Bank of Southern Africa (DBSA), Industrial Development Corporation (IDC), National Empowerment Fund (NEF) and Export Credit Insurance Corporation. It also refers to the National Industrial Participation Programme, which aims to raise investment levels and increase the export of South African goods and services. Sector-specific government investment programmes also exist.

State-Owned Enterprises

474. The CSAR refers generally to the government’s two-pronged approach to SOEs. It notes that, in some instances, the government has partially privatised SOEs, while in others the “corporatisation” of SOEs has been pursued. The goals of the government are to improve service delivery, accountability and efficiency in SOEs.





Women's Entrepreneurial Development

475. The government pursues its goals of supporting women in business through various strategies, including the National Research and Development Strategy. This strategy supports access to, and participation of women and historically disadvantaged communities in the science, engineering and technology fields. There is also government participation in the National Economic Development and Labour Council (NEDLAC), a forum for dialogue on socio-economic policy.

Constraints to Growth

476. The CSAR identifies factors that constrain growth: access to infrastructure in rural areas, including water and sanitation; bureaucratic red tape; policies for trade liberalisation; skills shortages; HIV and AIDS; corruption; and high costs of certain inputs, such as telecommunications and logistics. However, no analysis or contextualisation of these constraints is made in the CSAR.

ii. Findings of the CRM

Commercial Enterprises and the Economy

477. Enterprises in South Africa cover a wide variety of activities that can be clustered as follows: agriculture and agro-processing; construction; electrical, gas, steam and water; finance, insurance and business services; manufacturing; mining; catering and accommodation; communications; transport; storage; trade, and so on. Agriculture and mining are regarded as primary sectors. The finance, real estate and business services sector constitutes the largest portion of the economy (19.5 per cent), followed by manufacturing (16.4 per cent). The trade sector, including wholesale and retail trade, hotels and restaurants, provided the most employment opportunities, with over 3.02 million South Africans working in this industry in September 2005.²⁷
478. South Africa is a self-sufficient in food production and the agricultural sector has become a major exporter. International agro-processing industries with a recognised presence in the country include, for example, Cadbury, Schweppes Coca-Cola, Danone, HJ Heinz, Kellogg, McCain Foods, Minute Maid, Nestle, Parmalat, Pillsbury, Unilever and Virgin Cola.

Regulatory Framework

479. The legislative framework for commercial activity is largely adequate. The CRM confirmed that problematic areas noted in the CSAR (e.g. the revision of the Companies Act of 1973) are being addressed. In this context, a project to reform company laws was initiated in 2002 and is being implemented in two phases. The first phase relates to the amendment of corporate laws to be completed in 2006, while the second concerns the overhaul of the Close Corporations Act of 1984 to be passed in 2007. In short, the reforms aim

²⁷ Source: Statistics South Africa (StatsSA). Statistical Release P0441, Third Quarter 2005, Table A; and Statistical Release P0210, Labour Force Survey, September 2005.

to simplify the process of starting and maintaining a company, while at the same time providing for enhanced corporate governance. The CRM was informed that the first phase is at an advanced stage and relevant stakeholder groups, such as business and the IoD, have commented on the proposed amendments.

480. Both the background paper and the CSAR point to problems with the highly formalistic legislation for registering companies, which imposes unnecessary compliance burdens and lengthens the time it takes to register a business. The CSAR notes that the turnaround time is one week, while the background paper states that it can take up to six weeks. According to the 2006 edition of the World Bank's Doing Business survey, entrepreneurs can expect to go through nine steps to launch a business over 35 days on average, at a cost equal to 6.9 per cent of the gross national income (GNI) per capita in South Africa. This compares less favourably with an average 6.2 steps to launch a business over 16.6 days, at a cost of 5.3 per cent of GNI per capita in the OECD countries.
481. The Companies and Intellectual Property Registration Office (CIPRO), the agency under the DTI responsible for business registration, was of the view that its turnaround time in company registration has improved significantly. CIPRO maintained that it takes one day for close corporations and three days for public companies to register. This claim was disputed by stakeholders who cited delays in registration. The CRM was informed of "shelf registration" wherein an intermediary or third party registers a number of companies with the principal goal of selling them off to third parties. This practice had come about due to previous inordinate delays in registering a company. It is hoped that the new Companies Act will address these concerns.
482. The CRM interrogated the effectiveness of CIPRO's regulatory and oversight mandate. Information provided by the Office indicated that it is governed by the Acts under its administration, the most important being the Companies Act of 1973, Close Corporations Act of 1984, Cooperatives Act of 2005 and Intellectual Property Laws Rationalisation Act of 1996 for trademarks, patents, copyright and designs. CIPRO noted that the practice has been to accept all filing of documents in good faith, or the bona fides of the persons filing the documents. However, CIPRO has realised it should be more proactive in combating fraudulent filings and now plays a more active regulatory function in this regard. For example, the Compliance and Regulation Division has been set up to handle all fraudulent filings and actively investigate all transgressions of these Acts as per their mandate. Electronic interventions are used to tighten up on filing requirements and checks.
483. Stakeholders expressed mixed views on the adequacy of labour legislation. Those mostly from the private sector stated that labour laws are restrictive in some areas and have a broader impact on production, productivity, growth and job creation. Representatives of trade unions, however, were of the view that the current labour framework is ideal, especially when measured against the historical backdrop of South Africa. Also impacting on labour laws are the BEE and B-BBEE strategies. All parties consulted supported these strategies but noted that they should be properly implemented to avoid abuse.





484. Several foreign companies complained that South Africa's immigration laws make it difficult for them to obtain work permits for their foreign employees. This called into question potential investors' ability to staff their operations with skills at a given time.
485. Stakeholders confirmed the concern expressed in the CSAR that the process of commercial dispute resolution is too long and costly. A number of alternative mechanisms for dispute resolution have been championed and instituted by business, and more recently the IoD. More work is still needed in this area to reduce backlogs and ensure justice.
486. Problems with the judicial system also extend to the prosecution of economic and white-collar crime, which is noted as ineffective due to inordinate delays. This has necessitated the establishment of self-help mechanisms by entities. For example, the JSE has a name-and-shame strategy for those found to engage in insider trading and other unethical practices. The FSB has also put in place an Appeals Tribunal to address matters within its jurisdiction.
487. Stakeholders pointed to the need to reform the bankruptcy and insolvency laws to allow for bankruptcy reorganisation.

Banking System

488. South Africa has a highly sophisticated banking sector, ranked among the best in the world. The Banking Supervision Department of the SARB supervises 34 locally controlled and eight foreign-controlled banks, 15 local branches of foreign banks, 61 representative offices of foreign banks and two registered mutual banks.
489. The CRM discussed access to banks in rural areas, high bank charges and the large percentage of the under-banked black population. These issues are further elaborated on in Objective 2.

South Africa's Exchanges

490. The JSE is licensed as an exchange under the SSA and provides a market for trading in equities, equity derivatives, agricultural products and interest rate products. Its main lines of business are listings, trading, clearing and settlement, technology and related services.
491. The JSE has a unitary board of 15 members, consisting of a majority of non-executive directors. In the interests of transparency, representatives from the FSB attend board meetings as observers. The JSE supports the principles of corporate governance enshrined in the King I and II Reports. In 2005, the JSE took the decision to adopt a corporate structure, although it has been operating in most respects as a de-facto corporate since its restructuring in 2000. In June 2006, the JSE listed on its own exchange.

492. The JSE ranks 16th in the world with a domestic market capitalisation of about US\$550 billion at the end of 2005. Commendably, the JSE has a parallel market for small, medium and growing companies, the AltX, which came into being in October 2003. Companies can join the AltX to issue new shares, raise funds, widen their investor base and have their shares traded on a regulated market. The AltX is designed to appeal to a diverse range of companies in all sectors, including young and fast-growing businesses, start-ups, management buy-outs and buy-ins, family-owned businesses, BEE companies and junior mining companies. In 2005 the JSE launched Yield-X, an entirely new market that provides a one-stop shop for a wide range of interest rate products. Table 5.1 compares the JSE main board and the AltX.

Table 5.1: Comparison between the JSE Main Board and the AltX

Listing Requirements	Main Board	AltX
Share capital	R25 million	R2 million
Profit history	3 years	None
Pre-tax profit	R8 million	n/a
Shareholder spread	20 per cent	10 per cent
Number of shareholders	500	100
Sponsor/designated adviser	Sponsor	Designated adviser
Publication in the press	Compulsory	Voluntary
Number of transactions	3	n/a
Special requirements	n/a	Appointment of financial directors
Annual listing fee	0.04 per cent of average market capitalisation with a minimum of R26 334 and a maximum of R121 700 (incl. VAT)	R20 000 maximum
Education requirements	n/a	All directors to attend the Directors' Induction Programme

Source: JSE Annual Report 2005. (n/a indicates "not applicable".)

493. To help focus the debate on CSR, as espoused by the King II Report, the JSE developed criteria for measuring the TBL performance of volunteering listed companies.





494. Consequently, in 2004, the JSE launched the SRI Index inspired by the Dow Jones Sustainable Group Index and the FTSE4Good Index in the UK. The SRI not only encourages social responsibility but also allows investors to assess the behaviours of companies in which they invest. It may well lead to a premium rating for companies included in the Index.
495. In June 2006, the JSE launched the South African Social Investment Exchange (SASIX), which allows companies to assess the performance of their corporate and social investments with a social return. A first in Africa, SASIX builds on the experience of a similar initiative launched by the Brazilian Stock Exchange in 2003, as well as the growing global practice of performance-based social investment. SASIX will help investors understand exactly where their money is going and how it is making a difference, and will help instil a culture of accountability among beneficiary organisations.

Best Practice 8: JSE Securities Exchange

The JSE is a world-class exchange with simultaneous listing and trading through the London Stock Exchange. All settlements of JSE trades are guaranteed and take place electronically through STRATE (Share Transactions Totally Electronic). STRATE is a central securities depository that provides the means for the electronic settlement of all financial instruments in South Africa. The JSE has been able to maintain a zero-failed trade status (i.e. a 100 per cent success rate since the inception of STRATE in the main order book). The JSE has real-time market surveillance systems used to combat insider trading. All listed companies are required to comply with the IFRS and the King II Report requirements, which help boost investor confidence. The Alternative Exchange provides a platform for listing for smaller companies. Yield X provides a one-stop shop for interest rate products. The SRI and SASIX help companies assess their TBL activities.

Source: Compiled by the APRM CRM from the 2005 JSE Annual Report and stakeholder interactions, July 2006.

496. Despite its remarkable capitalisation and rankings, the JSE lags behind globally in terms of the number of listed companies. In Africa, for example, it trails behind the Cairo and Alexandria Exchanges. The number of companies listed on the main board has continued to decline – from a peak of 668 companies in 1998 to 426 in January 2004, and only 343 indicated in the 2005 Annual Report. The JSE has tried to attract more listings to both the main board and the AltX. The decline in the number of listed companies may be attributed to a number of factors:
- Corporate consolidation and the declining demand for new equity issues in the domestic market;
 - More onerous listing requirements and the corporate governance rules of the JSE (for instance, there were 35 de-listings in 2005); and
 - Low interest rates and the availability of financing from private equity firms, which encourages privately owned companies to opt for debt and private equity financing rather than equity financing from the JSE.

497. From an equities perspective, the year 2005 witnessed more listings and fewer de-listings than over the past six years – there were 19 new listings, which is two more than in 2004 and significantly more than in 2003. However, few companies used the JSE to raise capital for expansion or investment through initial public offerings (IPOs). The low IPO rate in South Africa contrasts with the situation in other emerging and developed markets. According to a survey by Ernst & Young, 29 countries (many of whom are emerging markets) raised more than US\$1 billion in IPOs in 2006. This is because JSE listings are led by AltX listings (small company listings and some companies moving from the main board to the AltX to attract attention), inward listings by foreign companies and unbundling. Nonetheless, the AltX has been more successful in attracting SMEs than its predecessors, the Development Capital Market (DCM) and Venture Capital Market (VCM), with 23 companies listed on the AltX as of August 2006. The JSE is also proving to be an attractive market for foreign companies. In 2005, Oando Plc of Nigeria and Tawana Resources from Australia opted to list.
498. Another challenge is that JSE-listed companies are still dominated by white-owned companies. The Presidential Black Business Working Group recently noted that despite the promulgation of the EEA and BEE programmes, a 2005 survey of the top 200 companies in South Africa indicated that only five firms had black ownership of 50 per cent or more. Together, all the black-owned companies constitute only 1.2 per cent of the JSE's total capitalisation. This is not surprising, given that the equity and empowerment strategies are fairly recent and their impact in terms of asset ownership will be gradual. More effort, however, needs to be applied to attain the goal of at least 30 per cent black ownership by the end of the second decade of democratic freedom.
499. International experience has shown that the two-tier stock exchange system with differentiated listing requirements is generally successful in attracting small enterprises and increasing access to equity for small firms. However, differentiated listing requirements in themselves may not be enough to attract investors. Marketing and showcasing small listed companies on the AltX would enhance the interest of companies and investors, as has been done on both the NASDAQ and the Alternative Market of the London Stock Exchange. Evidence shows that few of the companies on the AltX are monitored by stock-broking firms, as most of these firms tend to prefer larger market stocks that generate higher commission. Incentives, CSR and B-BBEE strategies may need to be explored to encourage broker involvement in the alternative market in general and black-owned firms in particular.
500. The JSE has made some effort in marketing AltX companies. Ten of the 23 listed companies were invited by the Investment Analysis Society of South Africa to make presentations on their operations to an audience including stockbrokers, individual private client investors and small institutions. These efforts must be stepped up if the AltX is to avoid the pitfalls of the DCM and VCM listings, which are not too successful in attracting large institutions (who prefer larger corporations) and small investors (who equate the DCM/VCM market with unmanageable risk). The recently introduced FTSE/AltX Index enables investors to track the performance of the Exchange for the first time, and is also a step in the right direction.





501. The Bond Exchange of South Africa, formally registered as an exchange in 1996, previously traded as the Bond Market Association. BESA is a self-regulatory body licensed by the FSB. It regulates the market in fixed-income securities and associated derivative instruments. BESA offers a three-day rolling settlement using a bond-automated trading settlement system.
502. BESA lists over 375 bonds issued by the central and local government, public sector corporations and major companies. While South African government bonds account for most of BESA's new bond issues, the share of corporate bonds has steadily increased from less than 5 per cent in 2000 to 22 per cent in 2005. Government bonds are even more dominant in market-turnover terms, as the seven most liquid government bonds comprise almost 90 per cent of BESA's turnover, with total corporate debt comprising less than 3 per cent. BESA's market turnover declined from R11.67 billion in 2001 to R8.1 billion in 2005, mainly as a result of historically low interest rates and a more stable macroeconomic environment.
503. Bought out by the JSE in 2001, SAFEX consists of two divisions: Financial Derivatives and Agricultural Derivatives. Due to SAFEX, the JSE is ranked second globally for single stock futures.

Infrastructure

504. During the CRM, discussions on infrastructure focused on problems flagged in the CSAR regarding the facilitation of an enabling environment for economic activity. These include poor infrastructure in rural areas and its impact on market access, and the relatively high cost of using certain key infrastructure (e.g. telecommunications, ports and rail), which impacts on the cost of doing business.
505. The CRM was informed of various national initiatives to support development in rural areas, including the Accelerated and Shared Growth Initiative for South Africa (AsgiSA), Project Consolidate by the Department of Provincial and Local Government, and the Infrastructure Development Improvement Programme. (These are further elaborated on in the chapters on economic governance and socio-economic development.)
506. The CRM was informed that the government had approved high levels of investment for rail and port infrastructure development. It is also undertaking restructuring of state-owned port facilities to make them more efficient. Changes to be made include reforming tariffs to bring them in line with cost structures, separating cargo handling from the National Ports Development Corporation (the latter will be charged with maintaining and developing relevant infrastructure) and opening up port operations to the private sector by way of concession agreements. The vast majority of international trade enters and leaves South Africa through its commercial ports; hence the efficiency of port infrastructure is a key determinant of the country's competitiveness. This has a direct impact on the creation of jobs and expansion of productive output.

507. The high cost of telecommunications was attributed to the high cost of linking up to global telecommunications networks. The CRM also noted that increased competition in the sector is contributing to reduction in user costs, as has been observed in other jurisdictions.

Small, Medium and Micro-Enterprises

508. The CSAR notes that the views of informal traders were not solicited during the assessment process. The CRM therefore interacted extensively with small, micro- and informal traders during the provincial consultations.
509. One of the issues that preoccupied the CRM is the coexistence of the second economy alongside the first. The CRM requested statistical data on the size and magnitude of these economies, government policy on the second economy and the steps being taken to bridge the gaps between the two.
510. Very little research has been done to estimate the size of the second economy, as it is difficult to measure. It is estimated that South Africa has about 22 million informal workers whose lives are characterised by acute poverty. Though the second economy is very large, its contribution to GDP is relatively low, estimated at just 4.6 per cent in 2004.
511. The Southern African Regional Poverty Network (SARPN) estimated that the average turnover of a business in the second economy was R68 930 in 2004 and that an average of 2.3 persons was employed in each business. The total number of informal outlets was estimated at 749 500, consisting of 261 000 hawkers, 127 600 spaza shops, 40 100 shebeens and 320 800 other outlets. Other statistics are that South Africans spent a staggering R51.7 billion in the second economy in 2004 – close to the combined turnover of R59 billion of South Africa's two largest chain stores. In the second economy, about R16.7 billion was spent on food and R15.9 billion on transport, mainly taxis.
512. President Thabo Mbeki has identified the integration of the second economy into the first as a key objective of government policy. Central to this strategy is AsgiSA. Skills development, procurement policy and asset ownership under this initiative will be a strategic vehicle for promoting economic transition and integrating the second economy into the first. AsgiSA also addresses specific issues relating to the development of SMMEs, such as barriers to entry and competition in certain economic sectors; the current regulatory environment and its effect on SMMEs; and problems with public sector organisations, capacity and strategic leadership and their effect on service delivery.
513. The CRM met with the Minister of Trade and Industry, the Deputy Minister, the Deputy Director-General and other officials from the DTI. It also interacted with DFIs (e.g. the IDC and DBSA) and SME support institutions such as the National Development Agency (NDA) and SEDA. The CRM confirmed that the government has a number of initiatives for facilitating access to finance: agriculture (Land Bank); infrastructure (DBSA); community and industrial development (IDC); SMME wholesale finance (Khula); SMME non-financial





support (SEDA); civil society organisations (CSOs), such as the NDA; BEE (NEF); and Youth (Umsobomvu Youth Fund).

514. The CRM noted that despite all the initiatives in place, women, youth, people with disabilities and SMMEs continue to experience problems with access to finance due to various institutional requirements, such as the development of a business plan. It was stated that the process of approving a business plan was also cumbersome and liable to abuse. Some stakeholders alleged that while their business proposals had been rejected, their ideas were used by other people to obtain financing. Everywhere stakeholders stated that more work had to be done with regard to information dissemination and capacity building. Stakeholders also expressed the desire for these institutions to decentralise their services to provincial and municipal areas. They observed that the DTI seemed to operate at arm's length from the organisations and there was not enough oversight of organisational performance.
515. Problems expressed by SMMEs include the lack of market access and entry to sectors historically dominated by white conglomerates. During the apartheid years, the ownership and activities of South African corporations were highly concentrated, a phenomenon due to the exclusions of the minority regime. Since the democratic dispensation in the post-apartheid era, South Africa has introduced a number of policy reforms such as trade liberalisation, BEE and new competition rules in an attempt to unbundle traditional conglomerates and empower previously marginalised black South Africans to venture into the corporate sector, albeit with marginal success. To a large extent, the economy still maintains its distinctive characteristics, including the very large, though reduced, conglomerates.
516. Because of high horizontal and vertical integration of businesses it is common practice for large South African businesses to control the value chain from manufacturing to retailing. Banks, for example, own insurance companies and the latter own the retail outlets whose space is occupied by supermarkets with ownership links to the banks. In such a business environment new entrants not only face very steep barriers to entry but SMMEs, in particular, find it difficult to maintain their competitiveness to survive. The CRM is of the view that the business sector needs to be transformed through policy to dismantle such linkages, so that certain sectors (e.g. retailing) have fewer barriers to entry by SMMEs. Only through such reforms can the economy create capacity to generate additional jobs and meet the ultimate objectives of BEE.
517. Some stakeholders cited the problem of cultural inhibition to entrepreneurial activity. The CRM was informed that, despite the ready availability of small business financing options in South Africa, many potential entrepreneurs are unwilling to venture into the business world due to a general lack of interest. For example, it was noted that greater effort should be made to teach farm entrepreneurs agricultural economics and farm management to ensure that newly established farms do not become bankrupt due to mismanagement. The CRM believes that entrepreneurial inhibitions can only be countered through better education and skills development programmes.

518. The CRM raised the matter of the DTI's oversight role over agencies under its mandate. It learnt that the DTI upholds an agency management protocol, which includes appraisal of the organisations' five-year strategic plans, three-year business plans and annual operational plans. Emanating from consensus on the alignment of mandates and objectives to priorities of the DTI's business plan, annual shareholder compact agreements are entered into as a service level agreement between the DTI and the agencies. This is reinforced through the management of the reporting mechanism and appraisal process in line with the requirements for quarterly, mid-term and annual reporting and audits. The DTI noted that the agencies under its mandate have so far attained satisfactory compliance records with their reporting. The CRM is, however, of the view that given the degree of clientele dissatisfaction, in particular with regard to SME finance and support agencies, there is a need to re-examine the role and effectiveness of these agencies, as well as their relevance and adequacy in these changing economic times.
519. The CRM noted that there has been some effort by the government to address the above issue. In an attempt to consolidate microfinance support services, SEDA was formed through a merger of Ntsika Enterprise Promotion Agency, the National Manufacturing Advice Centre (NAMAC) and the Community Public-Private Partnership (CPPP) Programme, whose mandates had been non-financial support, technology, and rural or natural resource development respectively. SEDA's current focus is on facilitating start-ups, promoting growth and supporting turnaround. It is decentralising to the provinces and districts. The NDA, which targets the poorest of the poor in seeking to shift them from hopelessness to basic viability, is moving more towards a community-centred than an individual approach to be more effective. The CRM was informed that the Khula programme as conceived by the DTI is a wholesale financial institution intended to act through delivery channels, including commercial banks and retail financial intermediaries. Some of the problems cited could have been due to a lack of understanding of its role.
520. The CRM learnt that the National Credit Regulator was established under the DTI on 1 June 2006 and is responsible for the implementation, compliance monitoring and enforcement of the provisions of the National Credit Act of 2005. Among other things, these are to minimise reckless lending, establish a register of credit providers, and promote prudent and responsible management of credit information, including hand-up information to third parties such as credit bureaus. Provisions for the regulation of credit bureaus, as well as the establishment of a National Consumer Tribunal to protect consumer rights, became effective on 1 September 2006. The remainder of the National Credit Act will come into effect on 1 June 2007, including the provision of credit-related information such as an annual, free credit report to consumers to ensure transparency and accuracy in credit reporting.
521. From the foregoing, it would seem that the national approach to the second economy comprises a number of tailored interventions, each targeting specific aspects. This calls for greater coordination and a more holistic approach at the top to maximise effectiveness. The CRM is of the view that the DTI should undertake an assessment of the effectiveness of all SME support agencies within its mandate and consider facilitating a more hands-on role in small business financing.





522. The CRM is of the view that DTI should explore opportunities for forming joint ventures between black business and white entrepreneurs or foreign partners. Mentoring initiatives should be encouraged, whereby for instance a retired chief executive officer (CEO) could be attracted to provide managerial, administrative and technical assistance to the new entrepreneur. It must be possible to develop a synergetic, systematic business link between some firms in the first economy and some others in the second through subcontracting.
523. The CRM appreciates that some of the proposed initiatives are being explored under the new B-BBEE strategies. It is also encouraged by the DTI's Regional Industrial Development Strategy (2006), which refers to the development of business incubators such as the Innovation Hub in Pretoria where international and local businesses are assisted to develop their business in the research and technology sectors. However, this approach should be extended to the special economic zones and township-based businesses, and the incubator approach should be used to support second-economy enterprises.

Investment Promotion

524. Barclays Bank acquired 53.6 per cent of the shares of ABSA Bank on 27 July 2005 and the holding was increased to 56.6 per cent at the end of that year. The transaction was the largest single foreign direct investment (FDI) made in South Africa since 1994 and the largest investment of Barclays outside of the UK. Barclays and ABSA are working steadily to create the leading bank in sub-Saharan Africa. Apart from this transaction, South Africa has in the recent past not been attracting as much FDI, especially of the Greenfield variety, as anticipated. By contrast, it is an emerging outward investor, ranking among the top ten largest developing country investors in 2004. It must also be stated that the investment of South African companies elsewhere is not matched with similar investment in rural South Africa.
525. The CRM observed that increased FDI flows would facilitate attainment of the 6 per cent economic growth rate the country needs to reduce unemployment and poverty by half. Most stakeholders, however, agreed that although there is some easing of foreign exchange limits, further liberalisation of these controls could send a positive signal to foreign investors about the growing robustness of South Africa's economy.
536. The CRM was informed that South Africa supports the investment of its companies outside its borders, particularly in the rest of Africa. The foreign exchange thresholds for companies investing in Africa are more robust than those investing elsewhere. Other factors that boost the investment of South African companies in Africa are: proximity; integrated business infrastructure; preferential trade agreements with many countries in the sub-region; the relative size of the various economies; and investment in infrastructure and mining by South African companies acting as a spur for trade in the region.
527. South Africa's SOEs, such as the DBSA, IDC, Eskom and Transnet, have become key links in the drive to invest on the rest of the continent, either in their own right or as levers for private sector development and investment. According to the IDC, its investment portfolio

in the rest of Africa includes 33 approved projects in 11 countries, with several others forthcoming. The DBSA has infrastructure projects in the SADC region and the rest of Africa. These two institutions are repositories for information and research on the region. Transnet and its various divisions are active in the region, with Spoornet operating and managing rail links in 14 countries. Eskom is involved in the development of the power sector in the SADC and the rest of Africa. Other investments by public enterprises are in the energy, telecommunications, water, transport, tourism, financial services and agricultural sectors.

State-Owned Enterprises

528. A number of South African SOEs operate in sectors such as transport, defence, telecommunications, energy (oil, gas and electricity), agriculture, mining, DFIs, water and research, with an historical equity value of R145.4 billion.
529. Government ownership is dispersed among nine government ministries known as executive authorities. These are the Ministries of Public Enterprises, Telecommunications, Agriculture, Transport, Water Affairs, Defence, Trade and Industry, Minerals and Energy, and Finance.
530. The regulatory framework for SOEs includes the SOE Enabling Statute, the PFMA of 1999, the Companies Act of 1973 and Treasury Regulations. SOEs are encouraged to adhere to corporate governance codes such as the King I and II Reports. The Department of Public Enterprises has been developing codes of corporate governance and shareholder protocols for SOEs. Moreover, they are subject to parliamentary oversight via relevant portfolio committees.
531. South Africa has detailed the objectives and principles of restructuring in the “Policy Framework: An Accelerated Agenda Towards the Restructuring of State-Owned Enterprises”, which was publicly launched on 10 August 2000. In the document it is argued that the country’s SOE agenda defines a new way of restructuring SOEs in the developing world, providing a viable alternative to the “sell-off” strategy advocated previously by multi-lateral agencies. The aims of this strategy at the macro-level include:
- Improving efficiency and effectiveness at enterprise level;
 - Contributing to the macroeconomic health through attracting FDI;
 - Reducing borrowing requirements; and
 - Helping to achieve social imperatives such as employment growth and wider economic participation by previously disadvantaged groups.





At the enterprise and sector level restructuring involves:

- Improving the efficiency and effectiveness of the entity;
- Accessing globally competitive technologies where appropriate;
- Mobilising private sector capital and expertise;
- Assisting in the creation of effective market structures in sectors currently dominated by SOEs; and
- Assisting in enhanced service delivery.

532. The CRM discussed matters relating to SOEs with the Minister of Finance, trade unions and broader civil society. It met with the IDC and DBSA, two state-owned DFIs. The CRM was informed that the issue of ownership by the state will be dealt with case by case.
533. Some of the SOEs (e.g. IDC, DBSA and Eskom) have been doing rather well and no fiscal transfers are made to them. On the contrary, they pay income tax and dividends. Some of the SOEs provide strategic services, such as rail transport, and there is need for caution as to how their restructuring should be approached. Trade unions, in particular, support the retaining of state control in areas of strategic interest or provision of basic services.
534. Only one SOE – Telkom (37 per cent government ownership) – is currently listed. Implicitly, listing will only be considered if there is need to raise capital or some other strategic interest. Additionally, the listing of Telkom led to massive job losses, which had its own fall-outs. The strategy of the Ministry of Public Enterprises is to balance wider ownership and participation in the South African economy that may result from privatisation with appropriate social plans for limiting the impact of any unavoidable job losses. A representative of the trade unions also noted how wary they are of privatisation because it leads to transfer of ownership into the hands of a few. The CRM was also informed that there had been some experimentation with transferring state ownership to certain social groups, but that this had not resulted in increased profitability or competitiveness of the transferred entity. Moreover, it was acknowledged that there were unprofitable assets that were still with the state.
535. The SOE sector should be characterised by high levels of efficiency, which can only be achieved through proper strategic direction, appropriate capacity building, and promotion of enabling regulatory and competitive frameworks.
536. The CRM was impressed by South Africa's approach of seeking a viable alternative to SOEs rather than following the traditional sell-off strategy used by many African countries. It also noted the many SOEs in South Africa that are performing competitively and are worthy of emulation by other countries. However, the difficulties experienced by those SOEs that are not performing at optimal levels must be acknowledged and confronted.

Best Practice 9: State-Owned Enterprises

South Africa's SOEs are a vital part of its economic infrastructure. SOEs operate in the electricity, transport and landline telecommunications sectors and are responsible for a significant percentage of input costs to high-growth industries such as tourism, exports, and information and communication technology (ICT). Many SOEs are successful and require no fiscal transfers; in fact, they pay dividends and taxes to the government. For example, Transnet in the transport sector accounts for over 3 per cent of South Africa's GDP, and Eskom, which is involved in power generation and distribution, supplies over 94 per cent of South Africa's electricity, having revenues of over R30 billion a year and substantial profits. SOEs such as the IDC, Eskom, PetroSA, Transnet and South African Airways have also stepped up investment efforts in the rest of Africa in recent years.

Specialised SOEs such as the IDC are a vital part of South Africa's development efforts. The IDC, a DFI with R39 billion in capital and reserves, takes part in developing South Africa while creating more jobs. The aim is to create 52 000 jobs a year by 2011, double its current performance. This will advance the government's general target of halving unemployment by 2014. The IDC has stakes in many listed and unlisted companies in South Africa, with a portfolio of R26 billion, from which it earned R283 million in the 2005 fiscal year.

The success of South African SOEs is in part attributable to the government's strategy of partial privatisation, corporatisation and the articulation of a clear corporate governance framework for SOEs. SOEs operate within the ambit of various laws, including the SOE Enabling Statute, the PFMA of 1999, the Companies Act of 1973, and the Protocol on Corporate Governance in the Public Sector, which incorporates elements of the King II Report, including:

Composition of the board: The boards of SOEs should comprise both executive and non-executive directors, with a majority of non-executives. The maximum period of a director's appointment is set at three years. A unitary board structure, as opposed to a two-tier structure, is more appropriate for SOEs. The board should appraise a director's skills, experience and performance on an annual basis.

Committees: At a minimum, SOEs are directed to establish audit, remuneration and nomination committees.

Shareholder compact: The relationship between the SOE board and the government is governed by a shareholder compact. It sets specific objectives and performance targets to which all board members commit and includes possible remedial action in the case of non-performance. Moreover, the directors of wholly owned SOEs are expected to follow disclosure principles similar to those of private companies listed on the JSE. As a result, the SOE immediately informs the government of any information deemed to have a material effect on the value of the SOE.

Sources: Mawson, N. 2006. "IDC sets 52 000 jobs target for 2011", Mining Weekly, 29 June, www.miningweekly.co.za; IDC, 2005. Annual Report 2004-2005, South African Year Book, p. 269; South Africa, 2005. Investment Climate Statement, US State Department; and Department of Public Enterprises, 2002. Protocol on Corporate Governance in the Public Sector, September.





537. The CRM is of the view that South Africa's current strategy for SOEs, though commendable, should continue to be fine-tuned. The range of restructuring objectives, although reminiscent of the complex developmental terrain of SOE operation, may result in a lack of focus, which has been the shortcoming of SOEs elsewhere. It will therefore be necessary to prioritise some objectives above others at sector or enterprise level, while ensuring that all objectives are realised at programme level. Furthermore, the country should be more open to traditional means of divesting state interest, in particular for non-performing SOEs. A prerequisite should be adequate engagement with social partners, including civil society, to explain the strategy adopted and its broad impact on national development, poverty reduction and job creation.

Women's Entrepreneurial Development

538. The CRM received documentation from the DTI confirming its commitment to address issues of gender equity and economic growth as part of its business mandate. Accordingly, the DTI is currently considering a strategic framework that would encompass the provision of business information, entrepreneurial education and training, financing, international trade development support, research and statistics on women entrepreneurship, in order to mainstream gender issues in corporate governance. The initiatives would focus on black women's business organisations and associations, women's cooperatives, and women in the informal sector.
539. Interactions with stakeholders indicated that women still experience hardship in accessing finance for economic activity. They are also poorly represented in corporate sector and management positions.

Constraints to Growth

540. The constraints to growth discussed by the CRM include a complex regulatory environment; inflexible labour laws; red tape; capacity and skills shortages; a high rate of mortality due mainly to three killer diseases (malaria, tuberculosis, and HIV and AIDS); crime; insecurity; and corruption.
541. In discussions with BUSA, the issues constraining growth were identified: education; infrastructure development; cost of doing business; labour issues; the creation of an environment of trust; and crime. Violent crime is of concern to both the private sector and the government. Private sector representatives informed the CRM that it was increasingly difficult to attract relevant skills from abroad due to apprehension around crime. The CRM was informed of the Business Against Crime Initiative that combats crime by installing closed-circuit monitors. The initiative is wholly supported by the private sector. Some stakeholders stated there was insufficient focus on white-collar crime, which is also prevalent.

iii. Recommendations

542. The APR Panel recommends that South Africa:

- Continue, in consultation with the stakeholders, the process of reforming corporate governance laws to align them with current international practice and the democratic transformation of the country. [Government; CIPRO; Social Partners]
- Consider reforming labour laws to promote, inter alia, the creation of more jobs. CSOs should be engaged in and educated on the broader impact of reformed laws on the creation of jobs and poverty reduction. [Government; Department of Labour; Trade Unions; Private Sector; Civil Society]
- Re-examine avenues available for commercial dispute resolution to hasten efficiency in this area. Mechanisms for alternative dispute resolution and arbitration should be explored and supported. [Government; Judiciary; Business Community; Relevant Professional Bodies and Organisations]
- Explore modalities for enterprise development, in particular among historically disadvantaged populations at community level, and provide the requisite support for capacity development in this regard. The regulatory framework should be reformed to be less burdensome for SME operators. [Government; DTI; BUSA; Social Partners]
- Continue to explore ways to encourage small entrepreneurs and partner them with established companies, such as by subcontracting, developing business hubs and incubators, employing mentoring programmes using retired entrepreneurs, and communicating this effectively to designated beneficiaries. [Government; DTI; BUSA; Social Partners]
- Continue efforts to promote and showcase small companies listed on the AltX. Brokerage firms should be encouraged to be involved in the AltX. [JSE; DTI]
- Review existing DFIs and support initiatives for SMEs to assess their efficiency and effectiveness. A holistic policy for development finance should be elaborated on and implemented. [Treasury; DTI]
- Continue to liberalise foreign exchange controls in order to encourage FDI. [Government; Department of Finance; SARB; Parliament]
- In line with AsgiSA, step up current efforts to reduce logistical bottlenecks in infrastructure. The APR Panel encourages the formation of more PPPs in infrastructure development. [Government; Parliament; Department of Public Enterprises; Private Sector; DFIs]





- Ensure that the second national telecommunications operator is in full operation in the short to medium term, in order to increase competition in the telecommunications sector and monitor the competitive environment to reduce high telecommunication costs. [Government]
- Encourage corporate South Africa to invest massively in rural South Africa to transform the second economy and promote employment in rural areas. Companies willing to embark on this venture should be provided with the necessary incentives and logistics support. [Corporate South Africa; Parliament; Government; Provincial Governments]
- Require South African companies operating elsewhere on the continent to observe South Africa's corporate governance standards in their operations. They should be encouraged to undertake SRI programmes. [Government; BUSA]
- Continue to fine-tune current SOE strategy and engage adequately with social partners, including civil society, to explain the strategy adopted and broad impact it has on national development, poverty reduction and job creation. [Government; Department of Public Enterprises; SOEs]
- Engage with social partners to tackle the issue of crime resolutely. The APR Panel believes that this should be done in tandem with a call for moral regeneration and with the support of religious and cultural ethos. [Government; judiciary; SAPS; Department of Home Affairs; Business Community; Cultural and Religious Leaders; Other Social Partners]
- Step up skills development efforts to ensure the availability of adequate capacity at all levels. In the short to medium term, consideration may be given to the use of outside expertise to spur production. [Government; Social Partners]
- Step up efforts at gender empowerment and mainstreaming in the private sector through the B-BBEE codes, training, financing schemes, and so on. [Government; Private Sector; Social Partners]

Objective 2: To Ensure that Corporations Act as Good Corporate Citizens with regard to Human Rights, Social Responsibility and Environmental Sustainability

i. Summary of the CSAR

Historical Context

543. In 1994, the South African labour market was characterised by high levels of poverty, extremely low levels of remuneration, income inequality, low skill and education levels, antagonistic labour relations, insufficient protection of labour and people with disabilities, and the absence of a comprehensive social security network. Since then, many of this

has changed for the better as South Africa has reformed its labour, human rights and environmental codes. It has provided empowerment programmes and skills development programmes for the historically disadvantaged groups, including black empowerment charters for each business sector.

Labour Relations

544. The CSAR notes that labour legislation includes laws promulgated under the Labour Relations Act of 1995. Codes of good practice have been developed, including a statutory code by NEDLAC, the body representing business, labour, civil society and the government. A non-statutory code of practice has been issued by the Commission for Conciliation, Mediation and Arbitration (CCMA).
545. Businesses are expected to resolve labour disputes internally. If these attempts fail, either party can take the matter to the CCMA. The CCMA held 153 570 hearings over 128 018 disputes during the 2004/05 fiscal year. Some 51 per cent of the hearings were for conciliation and 27 per cent for arbitration. The Labour Court is used as a last resort, although its rulings can be appealed to the High Court for industrial disputes.
546. Department of Labour inspectors are empowered to examine the workplace to enforce compliance with workplace safety and fairness regulations. Employers are required to address identified workplace issues and are subject to fines and court summons for violations. Inspectors have the statutory power to close down a business until the workplace regulation has been complied with.
547. In general, labour regulations are adequate in South Africa, with the following exceptions:
- Inadequacy of whistleblower legislation under the Protected Disclosures Act of 2000.
 - The EEA's provisions for gender equity are not followed, especially higher up the employment ladder of larger companies. In 2006, only 16.8 per cent of executive managers and 11.5 per cent of directors were women.
 - There are significant differences in remuneration. For example, the ratio of the earnings of CEOs of medium to large companies compared with those of employees earning a minimum wage rose from 35:1 in 1994 to 55:1 in 2004. Significant differences in wage rates also occur between men and women, unionised and non-unionised workers, and formal and informal sector workers. It was noted that many women work in the non-unionised and informal sectors.

Corporations and Communities

548. The CSAR notes that CSR projects in communities are driven by legislation in the areas of BEE and skills development, as well as voluntary projects for HIV and AIDS. Significant public-private initiatives include the Business Trust, National Business Initiative (NBI) and President's Business Working Group.





549. Companies listed on the JSE spent approximately R2.4 billion on corporate social investment (CSI) projects in 2005, with an equivalent amount of staff time. CSR projects are largely pursued in the mining and industrial sectors, with mining companies being active in mining communities. Partnerships between business and other stakeholders are increasing, especially with regard to HIV and AIDS, health, skills development, job placements and housing.
550. The King II Report and the GRI encourage TBL reporting to reveal corporate track records relating to economic, social and environmental goals. In South Africa, however, sustainability reports incorporating such principles tend to be limited to MNCs. A bright spot in this regard is the newly established SRI at the JSE, which monitors the social, economic and environmental investments of companies listed on the Index.
551. The CSAR notes that stakeholders have called for municipalities to create and articulate clear strategies for poverty eradication and job creation as part of an integrated, beneficial investment approach that includes increasing CSI. Others call for South Africa to engage in an open, multi-stakeholder dialogue in order to define and articulate the meaning of CSR and investment, corporate governance and TBL reporting. There are also calls for additional research into the business case for CSR and SRI.
552. The CSAR raises concerns about the impact of current reporting and corporate governance standards on small, medium and micro-businesses. The ability and affordability of smaller enterprises to apply environmental standards and comply with regulatory legislation are also questioned.

Environmental Protection

553. Primary statutes governing the environment include the Constitution, NEMA and the Environment Conservation Act (ECA) of 1989. These regulate citizens' right of access to environmental goods and services, and provides for stakeholder consultation in setting corporate policy and management plans. The ECA regulates harmful environmental practices through environmental impact assessment (EIA) regulations that have been implemented since 1997. New EIA regulations are currently being developed to incorporate changes in environmental laws.
554. The CSAR notes that stakeholders are concerned about the effectiveness of environmental inspections. For the past two years, the Environmental Management Inspectorate of the Department of Environment and Tourism (DEAT) has dealt with cases of environmental non-compliance. National and provincial reports on the state of the environment have documented past and present corporate activities causing environmental degradation, such as the pollution of air, water and land by industries and mining. Provinces and national departments with functions impacting on the environment also submit annual reports on their environmental management plans or environmental implementation plans prepared in terms of NEMA. The quality of these provincial and national reports needs improvement.

555. The CSAR acknowledges the progress made in enforcing environmental rules, including the early success of the Environmental Management Inspectorate within the DEAT, known as the “Green Scorpions”. The DEAT received 72 reports of environmental degradation and non-compliance with environmental requirements in the fiscal year 2005/06. Of these, 38 had been referred to the provinces for investigation and the remainder were investigated by the DEAT. Ten of the investigated cases resulted in compliance, seven resulted in legal action and two were successfully prosecuted. The CSAR does not indicate what progress has been made with the remaining 19 cases.
556. Current challenges to the environment include rapid urbanisation, congestion of roads, air pollution and spillages of untreated sewerage. Rapid urbanisation has resulted in an increased demand for land, which threatens biodiversity, especially the rare and endangered species inhabiting the wetlands and riverine systems.

Black Economic Empowerment

557. According to the CSAR, legislation on BEE is having a significant impact on the corporate sector. The structure and composition of boards of companies and their management are changing as a result of new legislation and social imperatives. There is also an impact in terms of ownership and control of equity. The CSAR highlights the following concerns raised by stakeholders with regard to the BEE framework: it benefits the elite without being broad based; it does not clearly address young people; it does not address conflicts of interest and corruption as a result of BEE; the issues of skills transfer to the historically disadvantaged and the out-migration of white skilled people are not studied adequately; and insufficient attention is given to the debt-based structure of BEE deals and their effect on corporate governance standards.
558. The CSAR discloses areas where consensus did not emerge, such as the views that weak monitoring reduces the effect of human rights and environmental legislation; companies are not held accountable for meeting targets for women and people with disabilities in corporate leadership and professional positions; there is undue emphasis on attracting black male professionals to high-level corporate jobs and a need for a broader-based programme that also prioritises women; flexibility in the economy is required given the development status of the country; and the labour market needs to offer greater protection to all employees.

ii. Findings of the CRM

Labour Relations

559. Based on deliberations during the mission, the CRM concluded that South Africa has a good framework for protecting its human rights and labour rights. Most businesses adhere to human rights and other labour codes, although some stakeholders mentioned instances of abuse in labour-intensive industries such as textiles and farms. The CRM also confirmed





the challenge cited in the CSAR regarding the need for a proper system of whistleblower protection. It observed that while the Protected Disclosures Act of 2000 exists, South Africa lacks a culture of whistleblower protection and such persons are often unfairly victimised despite their good intentions.

560. The CRM explored the issue raised in the CSAR of the large disparity in incomes between South African CEOs and senior management of companies and their employees. While many companies in South Africa have consistently paid large dividends to shareholders in recent years, many employees still earn relatively low wages. For example, in August 2006 a newspaper quoted a Cosatu official as disclosing that the CEO of a large food retailer is paid R57 million per annum, while some retail workers at minimum wage earn less than R1000 a month. It should be noted that minimum wages in the wholesale and retail sector are variable, with the lowest paid workers in the sector (working less than 27 hours a week) earning between R6.14 to R7.72 per hour in the current period.²⁸
561. The 1996 Report of the Presidential Commission on labour policy discloses the background to the present-day minimum wage policy in South Africa. The Report notes that, for a variety of reasons, it is difficult to make accurate and conclusive international comparisons of wages and productivity, and hence of unit labour costs. The available evidence does, however, suggest that the average unit labour costs in South Africa are higher than those in comparable middle-income developing countries. This would imply a reluctance to raise such costs, as it may impact on the competitiveness of the enterprise. The practice is to encourage collective bargaining between workers and industry.
562. The Report notes that the labour market policy should reinforce the national goals of enhancing employment and productivity, and tackling poverty and inequality. It observes that poverty cannot be eliminated when extremely low wages are paid or earnings inequalities are manifestly extreme. There may be trade-offs between promoting greater equity and industrial peace for those in employment and increasing access to employment by those without jobs. The CRM agrees that wages should be determined using a practical, incremental approach balancing the various goals of South Africa as a development state.
563. Trade union representatives emphasised that while job creation efforts should continue, the quality of jobs should be analysed and the low-wage conundrum addressed. Greater disclosure of executive remuneration, share options and other incentives is needed in companies' annual reports.

Corporations and Communities

564. Stakeholders acknowledged various instances of CSI in their communities. It was noted that the national government has supported many CSR initiatives through tax rebates to business. The development of B-BBEE charters was seen as contributing to the transformation of commerce and industry. Despite these notable efforts and the emphasis on CSR and the TBL,

²⁸ Source: Government Gazette 8413, Vol. 488, No. 28559, obtained from www.labour.gov.za.

however, stakeholders reiterated that these initiatives do not significantly challenge the rift between the first and second economies. They emphasised that corporate governance must address the burning issues of poverty alleviation and growing inequality. In this context, tackling unemployment should be at the forefront of CSR initiatives.

565. Stakeholders felt that CSR initiatives such as the Mzansi Account for the un-banked were generally positive developments. The CRM believes the Mzansi Account has helped to bring a banking and savings culture to many people.

Best Practice 10: The Mzansi Account for the Un-Banked

South Africa's four major banks (ABSA, First National Bank, Nedbank and Standard Bank) as well as the Post Bank offer the Mzansi Account, which represents the first major initiative to cater for the under-banked and un-banked populations of South Africa. These major banks were responding to voluntary obligations under the Financial Sector Charter. At the time of the launch of the Mzansi Account in October 2004, the Banking Association estimated that about 13 million South Africans were among the un-banked. By June 2006, over 3.3 million Mzansi bank accounts had been opened and other banking institutions had joined in offering these accounts.

The Mzansi Account has the following features:

- There are no management fees.
- One free cash deposit can be made per month.
- ATM transaction charges are the same regardless of the bank machine used (among the participating banks).
- Transactions are limited to deposits, withdrawals and debit card payments.

As of February 2006, FNB's Mzansi customers could also set up debit orders and do third-party payments on their cellphones.

Sources: www.southafrica.info; "FNB improves Mzansi service offerings", 28 February 2006, <http://mg.co.za>; Shezi, A, "Putting cash away may be consumers' saving grace", 12 July 2006, www.businessday.co.za.

566. Communities raised the issue that they would like to be involved and benefit from investments in their communities. They would like to participate in, for example, share ownership of companies such as mining entities in their locality. Corporations should be encouraged to source their supplies from the communities in which they operate and thus build the capacity of those involved in the supply chain. For example, vehicle manufacturing plants should not only provide contracts to local suppliers, but also develop training programmes for them. This would ensure that suppliers meet their standards, while also developing small businesses in the community and consequently contributing to closing the gap between the first and second economies.
567. The CRM was informed that the Medical Research Council of South Africa (MRC) introduced an indigenous knowledge systems (IKS) programme to learn from and provide entrepreneurial opportunities for the commercialisation of drugs developed from the knowledge base of





local communities. In 2005, the MRC estimated that over the next three years, the IKS programme would create 200 permanent jobs in local communities.²⁹

568. The issue of CSR for South African MNCs operating in the rest of Africa was also discussed. Stakeholders noted the need for a change in the mindset from a purely South African operation doing business in the rest of Africa, to that of a truly regional or sub-regional company. Stakeholders felt that the best South African corporate governance and labour practices should be implemented in other African countries.

Education and Skills Development

569. Different challenges in education and skills development were noted in the provinces. For example, in the Northern Cape, job opportunities have been limited to the mining and agricultural sectors. This has led to a mass exodus to Gauteng and the Western Cape where job opportunities are more readily available. To attract and retain people with the required skills, the Northern Cape has identified the need to develop the health sector in the province and provide funding for training programmes such as the Premier's Education Trust Fund.
570. Stakeholders acknowledged the positive role of the Services Sector Education and Training Authorities (SETAs) in training and developing employees with appropriate skills. It was also noted that many enterprises are training workers. Nevertheless, some felt that greater emphasis could be placed on developing specific skills relevant to particular industries through dedicated programmes.
571. The CRM was informed of stakeholders' concerns about the general lack of appropriate skills development programmes in many of the tertiary institutions in South Africa. They cited the example of a large industrial firm that imported hundreds, if not thousands, of highly skilled welders from abroad, as there were not enough welders in the country with the requisite skills, even with the high unemployment rate. This contrasts with the availability of many unemployed graduates, as evidenced by the emergence of the South African Graduate Development Association (SAGDA).
572. The CRM is of the view that businesses should help close the gap between their skills needs and the skills provided by tertiary institutions (e.g. colleges and universities) through internship, learnership and apprentice programmes. An example is the corporate funding of CIDA City College (Box 5.1).
573. Stakeholders in the Northern Cape cited successes with the government's Expanded Public Works Programme (EPWP), which has helped foster skills development for many people living in local municipalities and provided them with opportunities to bid for tenders. However, there are challenges in the implementation of the EPWP, including consumer satisfaction with the quality of service rendered by some black contractors. Efforts should also be made to expand the programme to include more beneficiaries as contractors.

²⁹ Source: The MRC's PowerPoint presentation on IKSs presented to the Parliament's Science and Technology Portfolio Committee on 14 June 2005, www.pmg.org.za.

Box 5.1: Skills Development at CIDA City College

Stakeholders in Gauteng cited the example of corporate funding of CIDA City College as a good practice worthy of emulation in CSR and CSI activity.

CIDA is a registered, accredited, private, non-profit higher education institution offering a low-cost, high-quality, three-year Bachelor of Business Administration degree in the business and technology fields. The campus is located in the Johannesburg central business district and includes an R86 million building donated by Investec Bank. According to the CIDA website, over 1300 students are currently registered.

Under the CIDA City programme, businesses help fund students and courses are geared to provide them with skills relevant to the corporate sector. Corporate donations to CIDA City College are tax deductible in South Africa, the USA and the UK. Professionals from companies such as PricewaterhouseCoopers, Monitor Company, Gemini Consulting, Investment Solutions and Investec Bank lecture at the college. Members of the corporate sector help fund the college and its programmes, including Investec Bank, First National Bank, Dimension Data, Microsoft, McGrawHill, JP Morgan and Deutsche Bank. Some business partners provide students with internships and hire City College graduates. CIDA asks that its business partners sponsor a student's tuition (R7500 per year for three years) and/or a student's accommodation, food and transport (R7500 per year for three years), and/or formally mentor and guide a student.

CIDA City notes that its students are required to reciprocate by helping to operate and manage the college and also by returning to their rural schools and communities to teach what they have learnt. The students' reward for this activity is "changing the nation through skills transfer".

Source: www.cida.co.za and CSM stakeholder meeting in Gauteng.

574. Insufficient municipal development planning was also identified as a concern. In the Northern Cape, some towns were built around a single company or industry, such as agriculture or mining. These communities were vulnerable to downturns in those industries. The situation is being remedied by planners at the Department of Minerals and Energy, as the government is looking beyond just the mine, for example, when a mining town is established. However, more needs to be done in this regard. Pockets of high unemployment (up to 75 per cent) are the inevitable legacy in the Northern Cape and other provinces that have been the victims of the closure of railway and mining operations.
575. Provincial development plans were also criticised by some stakeholders and compared with the national government strategy and record. It was disclosed that the government has contributed to nodal developments in each province. For example, in the Northern Cape, it has focused on fostering development around two nodal points, Galeshewe and Kgalagadi. However, this has resulted in asymmetric development of the province, as the rest of the province has been relatively neglected. Even Kgalagadi has received far less attention than Galeshewe. Stakeholders observed that all community stakeholders, including provincial





governments, should foster economic development in as many communities as possible. For example, in Namaqualand, a coastal area bordering the Atlantic Ocean, fisheries and other development activities centred on the sea can be launched. Other areas could be Priestly, the poorest part of the Northern Cape, and Siyanda, where the private sector has already invested in tourism. A traditional leader noted that even in Kgalagadi itself more attention needs to be given to the development of rural roads.

Environmental Protection

576. The CRM noted that the government has provided the appropriate legislative framework for environmental protection. NEMA was cited as a good set of laws making provision for all the regulations coordinating national standards for emissions, effluence and pollution, among other things. The government has also made provision for registering and rehabilitating environmental degradation inherited from the past. New environmental safety regulations came into effect on 1 June 2006, helping to foster sustainable development in South Africa. However, the effectiveness of implementation, the enforcement of environmental standards and the capacity of inspectors were identified as challenges. It was further observed that regulators appeared to operate at arm's length from the industry.
577. The CRM was informed that the new environmental management inspectors (popularly known as "Green Scorpions") are starting to enforce environmental laws better, especially in Gauteng. Stakeholders recommended that more of these officials be introduced throughout the country.
578. Many environmental problems are a legacy of the pre-1994 government, when enforcement of environmental regulations was even weaker than at present. Nonetheless, various examples of present environmental degradation were cited, including mercury dumping in KwaZulu-Natal by a company that is no longer in business; asbestos contamination in the Northern Cape; groundwater contamination by a large company seemingly undeterred by environmental fines; and challenges in natural gas extraction in Potchefstroom in the North-West.
579. Some members of civil society noted that the problem lies in the bottom-line-first approach of business. Some companies appeared to be concentrating on short-term profits at the expense of long-term sustainability. It was further observed that more South Africans should be made aware of the potential for ecotourism, especially if environmental laws are vigorously applied. This is very important for tourism and for conserving the unique environment in South Africa.
580. A stakeholder representing organised business noted that South Africa has a good track record in the implementation of corporate policies. However, adherence to these policies was problematic due to the voluntary nature of the goals and the fact that many companies did not undergo a full rigorous audit on their non-financial reporting. Furthermore, some companies hired casual temporary labour instead of full-time workers and this could go

on for several years. He recommended that more companies undergo a full annual audit of their practices so that all stakeholders could ensure adherence to the highest corporate governance practices.

581. A member of the business community informed the CRM that the concept of TBL reporting had started in South Africa and that, in his view, South African companies were “ahead of the game” in this regard.
582. The CRM was notified that 16 member companies of the JSE have agreed to use the structure for TBL reporting, which includes elements of sustainability and community development. Moreover, a business representative noted that South African companies subscribe to the Global Compact, which sets high norms and standards for corporate governance, including how companies work with governments. BUSA, an umbrella body for business, is currently studying ways and means of implementing the Global Compact in South African MNCs. These rules seek to ensure that human rights, anticorruption mindsets and concern for the environment are embedded at member companies.

Best Practice 11: The JSE and Triple Bottom Line Reporting

A Socially Responsible Investment (SRI) Index inspired by the Dow Jones Sustainable Group Index and the FTSE4Good Index in the UK was launched by the JSE in 2004. The JSE developed criteria for measuring the TBL at listed companies that undertook assessment for the Index. The companies are asked to complete a questionnaire which, together with publicly available and any supplementary information, is used to assess and score the company on economic, social and environmental criteria.

The JSE does not release company-specific scores publicly and the SRI is used solely to showcase all companies that qualify for inclusion. However, there has been an evolution in terms of what the JSE has published on the SRI constituents. In the first year of the listing in 2004, the JSE did not publish any rankings on how companies performed relative to each other. In the second year, the 2005 Index constituents were announced by environmental classification (high, medium and low environmental impact categories), as well as in alphabetical order. In the third year, top performers in each environmental classification were announced.

In the third year of the SRI, more companies requesting evaluation passed the minimum criteria for listing on the Index. In 2004, 51 out of 74 companies made it into the Index; in 2005, 49 out of 58; and in 2006, 58 out of 62. Nicky Newton-King, Deputy CEO of the JSE, noted in a press release on the 2006 SRI that “we developed the Index with the clear intention to focus the debate on what the TBL means for business in South Africa, whilst recognising the efforts of those companies with good sustainability practices”.

In June 2006, the JSE launched SASIX, which will allow to evaluate their performance in their corporate and SRIs. South Africa is following the example of the Rio Exchange in Brazil in this respect. Business leaders who are promoting SASIX’s evaluation of CSR in South Africa hope it will help foster a culture of accountability.

Source: www.jse.org.za.





Black Economic Empowerment and Community Economic Development

583. The EEA was the main driver of social and economic transformation, including BEE, until the passing into law of the B-BBEE Act in January 2004. The Act had been overtly criticised, even at forums such as the Growth and Development Summit of June 2003, for the slow pace of implementing employment equity. Only a small black elite appeared to have benefited and the Department of Labour was insufficiently resourced to enforce compliance.
584. The B-BBEE Act of 2003 responds to some of the criticisms of many South Africans against the EEA. It is designed to guide the transformation process in South Africa to be more broad based. It aims for a higher economic growth rate and more equitable income distribution. It also caters for changes in ownership, management structure, skills development, market access and investment strategies designed to uplift previously disadvantaged populations (Indian, Coloured and Black people) in different business sectors. Corporate stakeholders informed the CRM that the B-BBEE Act came into being to define and pursue empowerment strategies better, with a view to bringing about improved grassroots involvement.
585. B-BBEE legislation obliges local and district municipalities, provinces and the national government to hire black-owned contractors as part of procurement rules. A points system is used to award contracts. Firms with a large number of people from previously disadvantaged communities, women and/or people with disabilities as employees, are awarded extra points.
586. Stakeholders noted that the private sector is still heavily dominated by white-owned business. The small black business elite are also out of touch with their communities. Furthermore, B-BBEE programmes seem not to have benefited women as much as they have men. Most rural communities are yet to see the benefits of BEE.
587. However, it has been estimated that the thriving black middle-class emerging from BEE, and particularly those earning at least R154 000 a year, has grown by 368 per cent between 1998 and 2004. Although the numbers benefiting from the BEE programme are still relatively small and the productive side of the economy still lags behind the demand side, BEE is nevertheless impacting favourably on the growth rate of the economy.
588. The CRM is of the opinion that it is imperative to redress the inequities of the past. While sectoral codes of good practice have been developed through the B-BBEE charters, it is important to ensure that the private sector complies with the spirit of the programme. Many sector charters are still not complete and it is too early to evaluate the success of the programme. One programme viewed positively by many stakeholders is the Financial Sector Charter.

Best Practice 12: The Financial Sector Charter

The Financial Sector Charter is the response of the financial sector to the imperatives of B-BBEE. Under the Charter, financial institutions have committed themselves to “actively promoting a transformed, vibrant and globally competitive financial sector that reflects the demographics of South Africa, and contributes to the establishment of an equitable society by effectively providing accessible financial services to black people and by directing investment to targeted sectors of the economy”.

The Charter came into force in January 2004 after agreement was reached with all stakeholders at the Financial Sector Summit hosted by NEDLAC, a multilateral social dialogue forum on social, economic and labour policy. Stakeholders in NEDLAC party to the Charter included the government, business, labour and community members. The Charter was signed on 20 August 2002 via a Summit Declaration on Transformation of the Financial Sector.

In 2005, financial institutions reached consensus on delivering the following results by 2008 to fulfil Charter commitments:

- Improving access to financial services for low-income communities;
- R42 billion commitment to increasing investment in low-income housing;
- R5 billion funding to small and medium black-owned enterprise;
- R1.5 billion commitment to agriculture;
- R25 billion funding of transformational infrastructure;
- Increasing funding for BEE transaction financing;
- Accelerating employment equity and skills development within the financial sector;
- Increasing procurement from BEE-accredited enterprises; and
- Achieving BEE ownership and control targets.

Source: <https://www.fscharter.co.za>.

iii. Recommendations

589. The APR Panel recommends that South Africa:

- Take steps to protect whistleblowers effectively. [National Prosecuting Authority]
- Make plans to provide for additional infrastructure in environmentally sensitive areas and for more effective urban land usage to prevent sprawl, sewage spillage and air pollution. [Government]
- Provide resources for capacity building and enforcement of environmental laws. Proper oversight of environmental performance reporting is recommended. [DEAT; Local Authorities]
- Evaluate SETAs and forge more partnerships with the private sector in skills development and job creation. [Department of Trade and Industry; Department of Labour]





- Enhance capacity building and promote awareness of the beneficial effects of entrepreneurship. Undertake training programmes for potential entrepreneurs in business planning and access to finance. [Department of Trade and Industry; Department of Labour]
- Spread the benefits of development to as many areas of the provinces as possible, outside the national nodes of development. [Provincial Planning Authorities]

Objective 3: To Promote Adoption of Codes of Good Business Ethics in Achieving the Objectives of the Corporation

i. Summary of the CSAR

Measures to Promote Ethics

590. The transition to democracy has been a strong catalyst for examining the governance arrangements in both the private and public sectors. The King II Report, in particular, has played a pivotal role in promoting corporate integrity in South Africa through its influence on legislative reforms and regulatory measures, JSE listing requirements and banking sector regulations. It also led to the update of the Protocol on Corporate Governance in the Public Sector.
591. While the King II Report is seen to provide a sound corporate governance structure for South Africa, concerns are raised in the CSAR that as a private sector initiative, its protagonists have their own vested interests. Closely related to this is the prescription versus non-prescription debate, particularly in respect of issues that are ethical in nature, and the proper integration of ethics management into existing business and management processes.

Promoting Integrity

592. Public sector integrity has been enhanced by strengthening financial reporting and accountability through the PFMA, MFMA, Treasury Regulations and the Code of Conduct for the Public Sector. The Department of Public Enterprises has also developed a policy framework for SOEs. Active ethics management is advanced by the National Public Sector Anticorruption Strategy that is implemented by various state organs such as the Scorpions, Public Protector and National Prosecuting Authority (NPA).
593. Professional and business bodies, such as SAICA, the Law Society of South Africa, BUSA and IoD play a key role in promoting codes of good business ethics among their members. In the non-governmental organisation (NGO) and not-for-profit sector, a code of ethics is in place that is promoted by the Charities AIDS Foundation Southern Africa (CAFSA).

594. The CSAR noted unethical practices in the interface between business, the government and political parties, particularly in public tendering systems.

Regulatory Framework

595. The FSB is responsible for enforcing the SSA, which consolidates provisions of the Insider Trading Act of 1998 and other legislation for financial markets. The CSAR notes that despite efforts since it was formed in 1999, the FSB has not been successful in prosecuting insider traders. There is a need to strengthen regulations for hostile takeovers significantly by reviewing the Securities Regulations Code that is overseen by the SRP, a regulatory body established in accordance with Chapter XVA of the Companies Act of 1973.
596. The CSAR notes that South Africa is fully committed to adhering to the IFRS. IRBA was established by the new Auditing Profession Act of 2005 to oversee the previously self-regulated auditing profession and legislation covering mandatory audit committees in public interest companies has been enacted.
597. The CSAR observes that South Africa is fully committed to adherence to IFRS and the Basel II standards for the banking sector. The country is a member of the FATF on money laundering, as well as the Eastern and Southern Africa Anti-Money Laundering Action Group (ESAAMLG). Legislation covering whistle-blowing and anticorruption is in force.
598. The CSAR, however, questions the effectiveness of the anticorruption efforts, particularly the inadequacy of reporting on whether commercial crimes (including money laundering) are being effectively prosecuted. The CSAR also raises the issue of uncertainty regarding the parliament's role and its effectiveness in ensuring that codes of conduct are adhered to in SOEs and Chapter 9 institutions.

Leadership, Organisation and Shareholders

599. The CSAR notes that director training is provided by the IoD. The B-BBEE charters have also begun to address the need for previously disadvantaged group representation at the board level.
600. Many companies are also addressing the need for more diversity and gender representation independent of BEE or B-BBEE-related programmes. The CSAR notes that an area requiring action is the low level of diversity and gender representation on many large and medium-sized companies' boards.
601. Poor shareholder activism is reported in the CSAR as being a major issue affecting corporate integrity in the country.
602. The CSAR deplors the fact that scanty information is available on the ethical conduct





of South African companies operating abroad. The CSAR does, however, make a case for corporate governance-related support systems to guide South African companies operating abroad, particularly in fragile democracies. Also, the CSAR notes that the extraterritorial provisions in the Prevention and Combating of Corrupt Activities Act of 2004 will have a negative effect on the competitiveness of South African corporations operating in Africa. The CSAR also raises matters that go beyond corporate governance, including ethical and conduct-related issues regarding South African troops deployed abroad as peacekeepers, and the country's military institutions.

ii. Findings of the CRM

Measures to Promote Ethics

603. The CRM concurred that post-1994 South Africa has taken great steps in putting in place the legal framework for improving corporations' adoption of good business ethics in achieving their objectives. These reforms emerged from the positive and influential role of the King II Report. The CRM also confirmed that various legislative instruments and mechanisms are in place to promote ethics. At the level of the state, the PFMA, MFMA and Treasury Regulations, over which the Auditor-General has oversight, enhance financial reporting and accountability. A policy framework for SOEs is in place, although parliamentary oversight over their compliance with codes of good business ethics needs to be enhanced. Within the non-profit and NGO sector, a code of ethics is championed by CAFSA. There is legislation for combating corruption, money laundering and insider trading. Other developments the CRM found are rules governing whistle-blowing, anticorruption measures (which have extraterritorial implications), and interim amendments to the Companies Act calling for mandatory audit committees in public interest companies and giving legal force to accounting standards and reporting.
604. On the whole, the CRM found that South Africa is an open economy that is more resistant to insider trading than some other advanced economies. Yet the country has had some notable scandals, including the R1 billion failure of the healthcare group, Macmed in 1999, the largest in South African history. Other examples include failures of the Regal Treasury Bank in 2001, Saambou Bank in 2002 and the collapse of Leisurenet in 2002, affecting 5000 employees and almost 1 million South Africans. Self-dealing, poor oversight by corporate boards and a weak regulatory environment were cited as the principal causes.
605. The CRM noted that efforts to strengthen the regulatory environment are ongoing. Insider trading is prohibited by the SSA, which came into effect on 1 February 2005. Importantly, the Act introduces stricter penalties of up to R50 million and/or ten years' imprisonment for various forms of market abuse. What now remains is, first, for the King II Report to inform the ongoing corporate law reforms so that the oversight role of corporate boards may be strengthened. Second, ongoing efforts to strengthen the oversight role of the various regulators need to be intensified, particularly those of the FSB as regards the non-banking financial services (other than medical schemes) and the SARB as regards the banking institutions, to stave off the recurrence of past scandals.

Best Practice 13: The King Reports

The King I and II Reports, home-grown to South Africa, have been accepted by many countries in Africa and worldwide as being very comprehensive, which is a remarkable achievement. These Reports will continue to influence corporate governance in South Africa, Africa and the world for many years to come.

The King II Report not only touches on the significant aspects of corporate governance (boards and directors; risk management; internal audits; integrated sustainability reporting; accounting and auditing; compliance and enforcement), but also establishes the nexus between economic, societal and environmental goals. It addresses such issues as social transformation, ethics, safety, health, environment and social responsibility in Africa. In the South African context, the code of the King II Report deals specifically with matters relating to employment equity and BEE. It emphasises the need for companies to move from the single to the triple bottom line, which embraces the economic, environmental and social aspects of a company's activities.

The King II Report has played a pivotal role in promoting corporate integrity in South Africa through its positive influence on legislative reforms and regulatory measures, JSE listing requirements and banking sector regulations. It has also led to the update of the Protocol on Corporate Governance in the Public Sector.

The King Reports introduce seven characteristics of good corporate governance: discipline; transparency; independence; accountability; corporate responsibility; fairness; and social responsibility.

Source: APRM CRM compilation from the King Reports and stakeholder interviews, July 2006.

606. The CRM found that successful prosecution for insider trading is low. In its first 29 months, the Insider Trading Directorate, a subcommittee of the FSB, investigated 124 cases. Ten of these led to a settlement with payment of a fine, six cases led to civil proceedings and one case was forwarded for criminal prosecution. Despite this shortfall in prosecutions, there are positive developments in strengthening the regulations. The Insider Trading Act of 1998 and the legislation governing the JSE have been consolidated into the SSA, which incorporates enhanced provisions that strengthen enforcement and sanctions for insider trading. Importantly, the SSA provisions prohibiting insider trading now cover market manipulation and abuse. These reforms are highly regarded internationally and are accompanied by an electronic system that regulates trade in the country. Known by the acronym STRATE, it is credited with clearly improving the integrity of the financial market system in South Africa.
607. The CRM found that “shareholder activism” may get a boost when locally listed companies introduce electronic voting systems at their annual meetings, instantly showing investor mood as resolutions are put to the vote. Electronic voting counts and displays result as the shareholders click a button, capturing the yes or no consensus as the votes mount up on





the screen. As well as being an instant mood gauge, it also makes the process far quicker than manually registering attendees and tallying their votes by hand. Sanlam became the first South African company to adopt e-voting when it tested the technology at its annual meeting in May 2006. Other JSE-listed companies that are assessing the technology include Anglo-Gold Ashanti, Gold Fields, Nedbank and Absa.³⁰ However, shareholder activism can only improve once institutional share-owners take seriously their ownership responsibilities to enforce the rules on breach of duties by directors and managers. A welcome development in this regard is the increasing engagement in corporate governance discourse in the public domain by fund managers in the private sector and the Public Investment Corporation, which manages civil servants' pension funds.

608. The CRM found that the Prevention and Combating of Corrupt Activities Act of 2004 is a useful instrument for addressing corruption. This Act has unbundled the crime of corruption by criminalising various specific activities in addition to the general crime of corruption. The CRM was informed of difficulties envisioned in enforcing and implementing the Act. For example, although the Act provides for the establishment and endorsement of a register for regulating the activities of the private sector, there is reluctance in this sector to use the register.
609. Although apprehensions exist that the extraterritorial provisions in the new Act against corruption may have a negative effect on the competitiveness of South African corporations operating in Africa, the CRM supports such provisions because the fight against corruption cannot be won without the observance of extraterritorial ethical codes by both domestic and international actors and relationships. Such provisions would considerably reduce corruption. The challenge is, first, the need to strengthen the modalities for enforcing the extraterritorial provisions and, second, the need to step up the prosecutions for corruption through better coordination of the agencies involved in enforcing anticorruption laws, namely the Office of the Auditor-General; Office of the Public Protector; Office of the Public Service Commission; Independent Complaints Directorate (ICD); South African Police Service (SAPS) Commercial Crime Unit; SAPS Anticorruption Unit; NPA; Directorate of Special Operations (Scorpions); Asset Forfeiture Unit; Special Investigating Unit; Department of Public Service and Administration (DPSA); National Intelligence Agency; South African Revenue Service (SARS) and the National Anticorruption Forum. Unless South Africa avoids dualism in the code of behaviour between its domestic companies and those operating elsewhere in Africa, it will not only fail in curtailing corruption at home, but its image and reputation abroad will also become tarnished, as indicated in the 2006 Bribe Payers Index (BPI) report of Transparency International, which ranked South African firms operating overseas as being the seventh worst in propensity to bribe when operating outside their country. Hence adherence to the code in the King II Report both at home and elsewhere by South African companies is imperative.

³⁰ Business Day, 20 July 2006, Johannesburg, <http://allafrica.com/stories/200607200257.html>.

Best Practice 14: Regulation of the Auditing Profession

The Auditing Profession Act (APA) of 2005 strengthens corporate governance by providing greater regulation of auditors through the IRBA, the newly established Independent Regulatory Board of Auditors. Auditors are now obliged to report to the IRBA any irregularities they come across when performing an audit. They may face a prison term of up to ten years for making a false report. The APA also calls for the rotation of auditors and provides mechanisms for strengthening the independence of auditors.

According to the National Treasury, the recently passed APA will:

- Enhance the integrity of the auditing profession in South Africa;
- Protect the public interest;
- Improve the independence and effectiveness of the IRBA while making it and independent auditors more accountable;
- Boost the independence of auditors; and
- Make the auditing profession more equitable and accessible for all South Africans.

The Act will attain its stated goals by:

- Allowing for the investigation of improper conduct and for disciplinary hearings;
- Providing standards for the qualification, competence, ethics and conduct of auditors; and
- Encouraging education and research into areas affecting the auditing profession, including participation in international professional activities.

Source: APA and stakeholder interactions during the APRM CRM, July 2006.

Corporate Social Responsibility for South African Companies Operating in Africa

610. The vast majority of the top 100 companies listed on the JSE have a clear Africa focus. Examples of leading MNCs based in South Africa are Standard Bank, which operates in 16 African countries; Shoprite Checkers, a food retailer operating in 14 countries; MTN, a telecommunications company in Cameroon, Nigeria, Rwanda, South Africa, Swaziland and Uganda; and SABMiller, a brewery company present in 13 African countries.
611. An example of typical CSR-related activity by South African MNCs is Shoprite Checkers in Zambia, where the company has been under pressure to source more of its goods locally. It has done so through business partnerships with Zambian small-scale horticultural farmers, under the Luangeni and Chamba Valley Projects. The horticultural producers are trained by the Ministry of Agriculture and private companies. However, this positive activity for the local community can be contrasted with a report that Shoprite does not address employee/stakeholder issues in the same manner as it does in South Africa. For example, Zambian employees are not covered by an Occupational Safety Policy (as of 2004) and the collective agreement only briefly mentions medical regulation, protective clothing and accidents.





iii. Recommendations

612. The APR Panel recommends that South Africa:

- Maintain the integrity of the capital market by strengthening the capacity of the FSB to prosecute insider traders successfully. [Government; FSB; DTI]
- Strengthen regulations governing hostile takeovers by reviewing the Securities Regulations Code No. 36 of 2004. [Government; DTI; SRP]
- Improve oversight over the compliance of corporations with the codes of conduct of the King II Report to minimise major corporate failure and collapse. [DTI; FSB; JSE]
- Strengthen the fight against corruption by enforcing the provisions of the Prevention and Combating of Corrupt Activities Act of 2004 that require private companies to register their activities, as well as the Act's extraterritorial provisions; and step up prosecutions for corruption through better coordination of the government agencies involved. [Government; Relevant Agencies; Public Service Commission]
- Strengthen procurement tendering procedures and systems to eliminate unethical procurement practices in the interface between business, the government and political parties. [Government; Private Sector; Political Parties]
- Consider adding a clause setting a time period in which transitioning politicians and civil servants refrain from working in areas that might cause conflict of interest with regard to government contracts. [DPSA]
- Strengthen parliamentary oversight over codes of conduct for SOEs through capacity development initiatives. [Parliament; SOEs; Department of Public Enterprises]
- Improve information dissemination on the effectiveness of current anti-money laundering efforts. [Government; Financial Intelligence Centre; SARB]
- Continue to ensure increased levels of diversity and gender representation at board level in the corporate sector. [DTI; Private Sector]
- Require disclosure of companies' compliance with the King II Report's code of corporate practices and conduct in business operations abroad. [JSE; Government; BUSA, MNCs; FSB; SARB]

Objective 4: To Ensure that Corporations Treat all Their Stakeholders in a Fair and Just Manner

i. Summary of the CSAR

Protecting Shareholders' Rights

613. The CSAR notes that minority shareholder protection is provided for in the Companies Act of 1973, as well as in common law and the King II Report's voluntary codes that have been adopted as JSE listing requirements. These include the right to attend, vote and participate at meetings of shareholders, as well as the right to a share of the dividends and the proceeds from the sale of surplus assets. Furthermore, it is noted that the Minister of Trade and Industry has the power to appoint inspectors to protect shareholder rights, and the Specialised Commercial Crime Court Unit also has the power to provide civil and criminal remedies in cases of shareholder abuse.
614. In addition to the Companies Act, a number of statutes promote shareholder rights, including the Promotion of Access to Information Act (PAIA) of 2000 and the FICA of 2001. The B-BBEE Act of 2003 requires the broadening of shareholding among the previously disadvantaged population of South Africa, and also that women benefit from at least 40 per cent of the shareholding transactions made.
615. The CSAR notes that the government has strengthened financial reporting and accountability by SOEs through the PFMA and the MFMA by, inter alia, incorporating elements of the codes for corporate governance of the King II Report and updating the government's codes of conduct, including a Protocol on Corporate Governance in the Public Sector.
616. The CSAR discloses that the SRP was established in terms of the Companies Act of 1973 to regulate takeovers and mergers of businesses. Its mandate is to ensure fair and equal treatment of security holders in all transactions.
617. The CSAR observes that there is a palpable lack of shareholder activism and inadequate monitoring of companies by asset managers acting on behalf of minority shareholders. Most shareholders are represented by asset managers and pension fund trustees. Awareness and understanding of corporate governance in the broader community of shareholders need to be extended. Related issues include conflicts of interest, a lack of understanding of investor rights and inadequate resources for building shareholder awareness.
618. The effectiveness of existing shareholder remedies in South Africa was a matter of concern for stakeholders. Small shareholders often lack resources to approach a court for orders, an area that needs to be strengthened through the corporate law reform programme. Other stakeholders were concerned about the communication and consultation process being used to make changes to the Companies Act and its provisions for shareholder rights.





Recognising the Rights of other Stakeholders

619. The CSAR notes that the Companies Act of 1973 does not explicitly cater for the rights of stakeholders other than shareholders. However, companies listed under the JSE Board are encouraged to interact with other stakeholders, and many stakeholder rights are provided for in specific legislation such as environmental, labour rights, human rights and consumer rights laws. This approach has been recommended in the 2004 government policy documents on the corporate law reform process.
620. The CSAR observes that the PAIA allows for such access as a constitutionally protected right. The Protected Disclosures Act of 2000 offers protection to whistleblowers. The CSAR notes that these two Acts have helped increase access to information and protect whistleblowers. However, stakeholders were concerned about the practical effectiveness of the legislation. The CSAR notes that there is limited case law in this area, and that a recent related case (*Davis v Clutchco*) has been interpreted in different ways by stakeholders.
621. Creditor protection is provided through common law provisions on contracts and the Companies Act of 1973. The CSAR discloses that the government is preparing to develop more explicit creditor rights through the forthcoming bankruptcy and insolvency legislation. The CSAR notes that the corporate law reform process has informed policy-makers that creditors in other countries have increasingly relied on contract laws to enforce their rights, and that company legislation should as a result be less creditor oriented.
622. The CSAR notes that the government encourages dialogue with stakeholders and this is legislated in areas such as collective bargaining with unions, workplace forums, in the Environmental Management Programme Reports and EIAs. An example is made of mining companies that are required to engage with all stakeholders, including the communities in which they operate. The government has also used the BEE sector charters to drive stakeholder engagement. For example, in the financial charter process, companies have been encouraged to create products that benefit the poor, who are often neglected by the corporate sector.
623. The CSAR reveals that community needs and business accountability to communities are not properly explored by the corporate sector. Furthermore, the voluntary nature of CSR-related activity is noted as a problem. Companies also rarely report such CSR-related activity, although it could have been done as part of their TBL reporting. The CSAR further notes that accountability mechanisms for non-financial reporting are rarely used in South Africa.
624. The codes for corporate governance of the King II Report advocate an inclusive approach to the recognition by business of the needs of stakeholders. The definition of stakeholders includes the community in which the company operates, as well as the company's customers, employees and suppliers. All these groups need to be considered when developing the company's strategy. The CSAR notes that the JSE encourages listed companies to

engage regularly with stakeholders and that its SRI provides clear details on stakeholder engagement.

625. The CSAR discloses that stakeholders voiced concerns about how the interests of the poor and marginalised are considered, especially in industries that do not require Environmental Management Programme Reports or EIAs. Some stakeholders believe there is lack of understanding in the business community of broad stakeholder issues, including stakeholder engagement and rights, and that few companies report in depth on their stakeholders or provide details of major conflicts or measures for resolving these issues. Other stakeholders noted that even in communities served by NGOs and non-profit organisations, there were concerns about holding these intermediaries accountable and whether issues important to the community were being heard through them.
626. Stakeholders observed that there are few accountability mechanisms for non-financial reporting and that readership of sustainability reports is low. The inability of stakeholders to enforce corporate commitments to voluntary mechanisms such as the UN Global Compact was also criticised. While noting the beneficial nature of CSR programmes, stakeholder-related legislation and voluntary mechanisms, stakeholders observed that these activities by their very nature do not address the fundamental divide between the formal and informal sectors of South African society.

ii. Findings of the CRM

Protecting Shareholders' Rights

627. The legislative framework protecting shareholder rights is adequate in several respects. The business sector, however, inherited many challenges from the apartheid era, including restricted access to the economy by previously disadvantaged people. The challenge for South African business is therefore to maintain and improve on corporate governance standards, while drawing the second economy into the mainstream. The education of future members of the business community has also not been neglected. It was observed that almost all universities currently have a corporate governance programme.
628. From a discussion with the JSE, the CRM confirmed that the Exchange has high listing standards for its 386 member companies, including listing rules mandating compliance with the standards of the King II Report. The JSE itself is audited and all members undergo two audits a year. The JSE's Surveillance Department closely examines capital adequacy standards for its member companies. The JSE has protected the interests of shareholders by helping with the development of South African laws, such as the legislation on insider trading. While there have been no prosecutions for insider trading thus far, a name-and-shame campaign has deterred many from the practice.





629. Representatives from the business and civil society groups noted that a key issue in corporate governance in the public sector is the strict accountability structures mandated by the PFMA's and the MFMA's rules for procurement. As a consequence, public institutions are finding it more difficult to attract outside directors for their boards of directors. This situation exacerbates the ever-present capacity and skills development challenges at municipalities and other public institutions. It was observed that outside directors can now be imprisoned under the PFMA and the MFMA. A business representative commented: "The problem is no one wants to sit on boards and audit committees – people want to add value but [are] not prepared to take the risk", adding that this problem illustrated the unintended consequences of well-meaning legislation. Judge Mervyn King, Chairperson of the King Committee responsible for the King II corporate governance standards, informed the CRM that in his opinion, "you can't legislate against dishonesty". A better approach would be that all boards of directors, in both the public and private sectors, should seek to be more transparent and disclose as much information as possible, such as information reported under the TBL approach.

Recognising the Rights of Other Stakeholders

630. As of July 2006, parts of the National Credit Act of 2005 came into force in South Africa. The Act aims to ensure that all companies that charge interest and provide goods or services on credit register with the National Credit Regulator and follow strict guidelines on lending practices to prevent reckless lending. The sanction for not registering is a 12-month jail sentence and a fine. Under the Act, credit providers are bound to check whether a prospective client is over-indebted. Failure to do so may mean that they will not have legal recourse to collecting any money owed. From September 2006, credit bureaus are also bound to give each South African one free credit report per year, with the aim of ensuring transparency and contributing to the accuracy of such reports. The Act also sets up a Credit Tribunal for adjudicating credit-related disputes. By July 2007, all sections of the Act will have come into force.

631. The CRM learnt that key legislation for personal and corporate insolvencies is the Companies Act of 1973, Close Corporations Act of 1984 and Insolvency Act of 1936. While there is no public official supervising insolvencies or performing the role of a regulator for insolvencies, the insolvency system is supervised in South Africa by the High Court, through the Master of the High Court. Personal as well as partnership bankruptcy is provided for under the Insolvency Act. Under the legislation, a creditor, a debtor or the debtor's agent can petition the court to declare a debtor bankrupt. The creditor votes for a trustee to administer the bankruptcy proceedings under oversight of the Master of the High Court. The trustee provides security for proper administration of the bankruptcy and this cost is part of the cost of the bankruptcy administration. The winding up of a company is provided for under the Companies and Close Corporations Acts. Liquidation of a company can be instigated by the company itself or its creditors through the High Court. The Court makes bankruptcy orders and oversees company liquidations. It appoints trustees, liquidators and judicial managers from the private sector and selects liquidators from a panel of liquidators. A new member of the panel needs to work with a more experienced member for two years before acting as the sole liquidator.

632. The CRM learnt that the DTI is drafting a Consumer Protection Bill designed to address the following consumer-related issues:
- The lack of adequate disclosure available to the consumer;
 - Instances of misleading information in advertising and other corporate representations;
 - Quality and safety issues in goods and services and the lack of adequate product liability;
 - Unfair contractual terms and fraudulent schemes;
 - The invasion of consumer privacy;
 - The fragmented nature of legislation and inadequate consumer remedies and redress; and
 - Uncoordinated enforcement mechanisms.
633. The Consumer Protection Bill provides for the creation of a National Consumer Commission to regulate consumer protection activity, including the promotion of voluntary consumer codes, legislative reform and enforcement of consumer protection laws along with the existing Office of Consumer Protection and the Consumer Affairs Committee (CAFCOM). The Bill will also replace six existing Acts in full and two Acts in part.

iii. Recommendations

634. The APR Panel recommends that South Africa:
- Encourage minority shareholders to be fully aware of their rights and the need to monitor corporations actively. Shareholders should also consider pooling funds for a shareholders' association whose activities would include shareholder education. [JSE; DTI]
 - Include provision in the corporate law reforms for easing financial and legal constraints for shareholders seeking legal redress. [DTI]
 - Ensure that a wide segment of the population is consulted in the corporate law reform process. [DTI]
 - Raise awareness of the benefits of TBL reporting requirements in the corporate sector, while highlighting companies that do provide such reporting. [Chambers of Commerce; JSE; BUSA; DTI]
 - Embark on a national search for suitable outside directors for municipal and public agencies and organisations to ensure proper oversight of budgets. The campaign should help counter apprehension of stringent MFMA rules. [National & Provincial Departments of Local Government]
 - Enact the Consumer Protection Bill and assess whether legislation meets its consumer protection goals. [DTI]





Objective 5: To Provide for Accountability of Corporations, Directors and Officers

i. Summary of the CSAR

Timely and Accurate Disclosure

635. The CSAR observes that the South African legislative framework requires disclosure of material information so as to enable investors, shareholders and other relevant stakeholders to make informed decisions. The key legislation giving the public the right to access information under the custody of public bodies is the PAIA.
636. The country is currently at the implementation stage of accounting standards reforms that will apply to the national and provincial spheres of government and public entities under their ownership control. The CSAR contends that it will take time to fully implement expanded financial reporting requirements for concerned public entities covering the disclosure of both financial and non-financial information, as envisaged by the PFMA³¹ and the ASB.
637. Within the private sector, the Companies Act of 1973 mandates companies registered under the Act to provide shareholders with financial-related information, such as profit and loss and the state of affairs of the company. The Act mandates that the financial statements disclosures follow generally accepted accounting standards (known as “little GAAP”), which are based on general usage, rather than on formal statements. Conversely, JSE listing rules and the Accounting Practices Board require financial statements to comply with the disclosure requirements of the IFRS (“big GAAP”). Issues relating to the application of both sets of standards are discussed in the following section.
638. TBL reporting, as championed by the King II Report and the GRI, has transformed the way non-financial information is being disclosed by both private and public sector enterprises. To move forward the King II Report agenda, the JSE has launched the SRI Index to promote socially responsible investment practices.
639. The CSAR notes that there are no material differences in disclosure requirements between South African and international accounting and auditing standards. As regards TBL reporting, the CSAR contends that disclosure by companies is strong in these areas: employment equity and transformation; ethics-related policies and practices; CSI; whistleblower hotlines; HIV and AIDS; health and safety policies and practices; as well as environmental management.
640. Conversely, the CSAR underscores that compliance-related challenges exist. First, in the area of TBL reporting, less frequently disclosed issues include: environmental accidents

³¹ The Public Finance Management Act, Act 1 of 1999, must be read together with the Public Finance Management Amendment Act, Act 29 of 1999. The two Acts do not make sense on their own, as the initial consolidated Bill had to be separated into two Bills for technical reasons to comply with the Constitution, which determines various procedures for the passage of Bills through the Parliament.

or fines; accounting for CSI; monitoring of resource utilisation; ISO 14001/9000 internal or external auditing; compliance with ethical standards; and discussion of targets and/or objectives. Second, divergences exist in reporting structures, which may present difficulties in ensuring that organisations report all relevant information in a consistent and comparable manner, making it hard to flag non-disclosure of material issues. Third, disclosure of executive pay, especially when share options are included, is inadequate given the increasingly large wage gaps between executives and the average workers. Lastly, research is required to properly define issues of materiality in disclosure requirements, particularly with respect to contingent liabilities and non-financial matters.

Accounting and Auditing Standards

641. South Africa's standard-setting body, the Accounting Practices Board, took a decision in 1993 to harmonise Statements of GAAP with the IAS. In February 2004, it issued the text of the IFRS without any amendments and therefore Statements of GAAP are the exact replica of the IFRS. Consequently, where an entity is preparing financial statements in terms of Statements of GAAP, it is in effect complying with the IFRS. Revised JSE listing requirements oblige listed companies to comply with the IFRS for financial periods commencing on or after 1 January 2005. Furthermore, the newly created IRBA requires auditors to apply the IAS when performing any assurance engagement. The CSAR concludes that there are no material differences between South African and international accounting and auditing standards.
642. Within the public sector, three sets of accounting standards are followed. First, SOEs apply the IFRS. Second, government ministries and departments and other agencies follow a modified cash-basis of accounting, referred to as the Generally Recognised Accounting Practice (GRAP). Third, municipalities prepare financial statements according to either the GRAP or the Generally Accepted Municipal Accounting Practice (GAMAP), issued by the Institute for Municipal Finance Officers (IMFO).
643. As noted earlier in this section, the country has started with a long process of implementing PFMA-related reforms of accounting standards applying to the national and provincial spheres of the government and related public entities.
644. The CSAR highlights a difference in the financial statements disclosure requirements of the Companies Act of 1973 compared with the JSE. The Act requires that financial statements of companies registered under it should comply with "little GAAP", which is based on general usage, rather than on formal statements such as those issued by the accounting profession. By contrast, since October 2000, the JSE listing requirements have specified that financial statements need to comply with "big GAAP" and, as a consequence, with the IFRS. Given that the Companies Act requires only "little GAAP", "big GAAP" lacks legal backing. Some experts propose that the Companies Act be modified to mandate "big GAAP", while others suggest that accounting issues be treated in a separate Accounting and Financial Reporting Bill.





645. The CSAR notes the position by the International Accounting Standards Board (IASB) that separate accounting standards for “limited interest companies” such as SMMEs should be promulgated.
646. According to the CSAR, the audit profession is regulated by the APA as from 1 April 2006. This Act strengthens corporate governance by providing greater regulation of auditors through the newly established IRBA. Auditors are now obliged to report to the IRBA reportable irregularities they come across when performing an audit and can face a prison term of up to ten years for false reporting. The APA calls for the rotation of auditors and provides mechanisms for strengthening their independence.
647. The JSE and the FSB examine prospectuses and annual financial statements for listed companies. The JSE, in partnership with SAICA, has established a GAAP Monitoring Panel responsible for investigating any complaints received from members of the public or investors relating to the inappropriate treatment of transactions in financial statements. The results are reported to the JSE, which takes action against the company. The auditors of such listed companies are reported to the IRBA for follow-up. In addition, SAICA receives a report on its members who have been implicated by the investigation for disciplinary action.
648. The CSAR notes that there have been very few reported court cases against auditors, implying that they are either performing excellently or that legislative provisions are underutilised or ineffective, or both.
649. The CSAR asserts that the issues covered in this section are being reviewed in the ongoing corporate law reform process. An important outcome of the process will be the establishment of an FRC to provide guidance on reporting standards (in conformity with APA requirements). A Bill for this purpose is expected to be introduced in the parliament in 2006.

Corporate Guidance, Monitoring and Accountability

650. The CSAR notes that South Africa has adopted a unitary board structure with both executive and non-executive directors. Strengthened by the King II Report, the Companies Act of 1973 governs the interface between the management, board and shareholders of companies. These provide for the proper exercise of directors’ duties in accordance with the cardinal principles of corporate governance, such as discipline, transparency, independence, accountability, responsibility, fairness and social responsibility.
651. The Companies Act mandates that company directors present annual financial statements to shareholders during annual general meetings (AGMs), which should include discussion

of the profit or loss and the state of affairs of the company. JSE listing rules further mandate listed companies to ensure that directors maintain full and effective control over their companies, including monitoring management's implementation of board strategies. The rules also recommend that boards should reserve specific powers for themselves and delegate others to management, while regularly monitoring implementation.

652. Common law prohibits directors from engaging in contractual interests with the companies in which they are board members, unless such transactions are approved at the AGM. The Companies Act also requires that directors declare their direct or indirect interests in full where they are materially affected.
653. The limited pool of competent directors in South Africa, in particular truly independent directors, means that a few individuals hold many directorships. The CSAR reports calls to limit the number of board appointments a non-executive director can hold. Additionally, concerns exist regarding related party transactions and the extent to which directors are accountable to all shareholders within conglomerate structures.
654. The lack of representation on boards (as well as in management) by black people, women and other disadvantaged groups, including people with disabilities, impacts negatively on their employment and income-generation opportunities. The CSAR raises the levels of compensation, independence, training and orientation of directors as areas of concern.
655. The CSAR highlights that shareholders in South Africa are lax in taking their ownership responsibilities seriously. According to the King II Report, the “inertia of shareowners and, more particularly, institutional share-owners, is largely responsible for the non-enforcement of the breach of duties by directors and managers”.
656. The CSAR notes that within the provisions of the PFMA, the shareholder compacts between the state and members of the board of public enterprises are equivalent to a performance agreement and contain key performance measures and indicators. In addition, Treasury Regulations require that the boards of SOEs conclude compacts with the state as shareholder.
657. Concerns are raised by the CSAR about the use of “special purpose entities” or subsidiaries for disguising material information from shareholders; the ability of public bodies to implement the legislated reporting structures, especially for SOEs in municipal and local government; and the “double burden” imposed on public entities by the Companies Act of 1973 and the PFMA of 1999, as the accountability structures for public entities require both parliamentary oversight and the consultation process for establishing shareholder compacts.
660. The CSAR raises concerns regarding the effective enforcement of sanctions for non-compliance with financial disclosure regulations, especially given the potential resource and capacity constraints within CIPRO. Other concerns include the ineffective and poor coordination of financial, microfinance, competition and company regulators that currently





work in silos, raising questions about the effectiveness of the enforcement of sanctions; the void of effective monitoring measures; and the inexistence of legislation governing the disclosure of certain types of non-financial matters, such as environmental risks, gender issues, women in management, and anti-sexual harassment policies and practices.

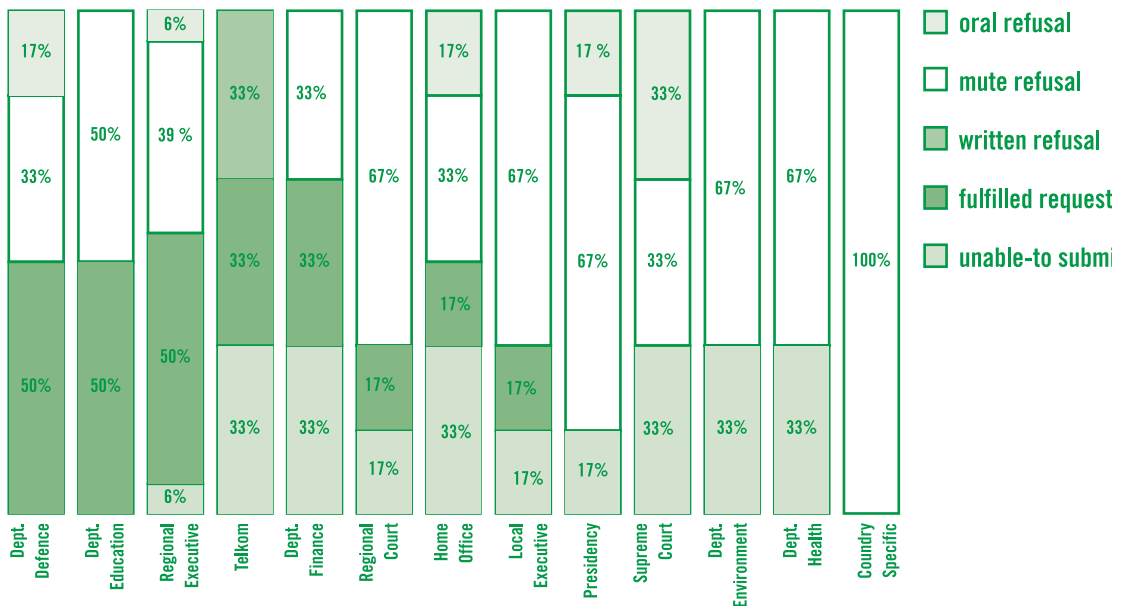
ii. Findings of the CRM

Timely and Accurate Disclosure

659. The PAIA of 2000 provides the legal basis for the citizenry's right of access to information held by public bodies in line with tenets of democratic governance.
660. It is believed that South Africa's legislation for the promotion of access to information is probably so far the only Act in the world that permits access to records held by both private and public bodies.
661. Despite this commendable legislation, certain concerns are not highlighted by the CSAR. In its report released in November 2004 (summarised in Figure 5.1), the Open Society Justice Initiative, in partnership with the Open Democracy Advice Centre (ODAC) in Cape Town, conducted a monitoring exercise on government agencies' compliance with the disclosure provisions of the PAIA. Ten seekers submitted 96 requests for information to 18 government institutions.³² The key outcome of the exercise was that "although none of the institutions surveyed in South Africa performed particularly well, their differences in performance were reinforced in follow-up interviews".³³
662. The survey found that government agencies that performed very well had made a serious commitment to implementing the PAIA. Conversely, the worst performers "possessed either non-functional systems or none whatsoever". The CRM concluded that although the PAIA is a good law, its implementation in practice is weak.
663. The CRM concluded that it is important that the government should develop a programme for monitoring the implementation of the PAIA. Importantly, government officials responsible for implementing the Act need ongoing training in its provisions. The capacity of government institutions to process requests for information needs to be improved. These efforts need to be supplemented by full political commitment to implement this legislation.

³² Access to Information in the Republic of South Africa: Results of the Open Society Justice Initiative Access to Information Monitoring Tool 2003, November 2004: www.justiceinitiative.org/db/.

³³ Ibid., p. 11.

Figure 5.1: Performance of Government Agencies on the PAIA

Source: Open Society Justice Initiative Access to Information Monitoring Tool

664. Within the public sector, the PFMA is one of the most important pieces of legislation passed by the new government. The PFMA promotes the objective of good financial management in the public sector in order to maximise service delivery through the effective and efficient use of limited resources. Importantly, the Act establishes the ASB responsible for setting the accounting standards applicable in the public sector. The PFMA has expanded financial reporting requirements for SOEs. Boards of SOEs must now disclose both financial and non-financial information to shareholders.
665. The CRM noted a key strength in the governance arrangements of SOEs in that the PFMA provisions and Treasury Regulations both require boards of SOEs to conclude compacts with the state as shareholder. Such compacts translate into a performance agreement and contain key performance measures and indicators. It is important for the government to continue its commendable efforts to ensure that SOEs are managed professionally. Importantly, SOEs need to be transformed into becoming instruments for creating an environment in which business can flourish. To ensure that SOEs meet these challenges, the OECD's Working Group on Privatisation and Corporate Governance of State-Owned Enterprises has developed a set of guidelines, completed in 2005, which may be useful to inform government policy in this regard.
666. In the private sector, the Companies Act of 1973 provides for the disclosure of financial information by companies registered under the Act. The JSE listing rules require that





financial statements of quoted companies comply with the IFRS disclosure standards. Since 2003, all companies listed on the JSE have to comply with the King II Report, which mandates disclosure of non-financial information. This code addresses core corporate governance issues, such as director independence and splitting CEO from chairperson positions, and also requires the use of GRI guidelines for disclosing social and environmental performance. The requirement to follow the King II Report placed the JSE at the forefront of stock exchanges worldwide in terms of promoting SRI criteria.

667. The CRM concurs with the CSAR that there is a need to strengthen the requirements to disclose executive pay. Understandably, the area of senior executive remuneration, especially that of granting of share options, stirs up public emotions, especially where such rewards provide executives with huge short-term benefits. There is also the issue of not-so-transparent pension and retirement packages for executives. Due to the negative perceptions and reality of these payments, the SEC in the USA under Chairperson Chris Cox voted unanimously to change the rules for reporting executive remuneration from 2007. Although the changes will not affect executive pay, they will result in more transparent disclosure thereof and hopefully indirectly limit excessive remuneration. The CRM is of the opinion that a similar approach will be of value to South Africa. It is understood from discussions with SAICA that the JSE is taking appropriate action.
668. The CRM concurs with the CSAR that there is a need to improve corporate disclosure requirements to eliminate divergence of reported information and ensure that organisations are reporting all relevant information in a consistent, comparable manner. The CRM concluded that non-compliance with disclosure requirements and weak enforcement by regulators appear to be the major concerns. Discussions with SAICA revealed that action is being taken to improve corporate reporting. A GAAP Monitoring Panel comprising the JSE and SAICA was established in 2002 and mandated to investigate any public reports of inappropriate disclosures by companies. The Panel will complement ongoing work of the JSE and the FSB regarding the examination of annual financial statements of listed companies. The Panel is said to be a stop-gap measure and will be replaced by an FRC for providing guidance on reporting standards as part of the ongoing corporate law reform process. The CRM agrees that these actions will remove financial disclosure concerns, provided the FRC, JSE and FSB have adequate capacity to conduct the investigations. Importantly, the enforcement power of the JSE needs to be increased.

Accounting and Auditing

669. The CRM concurs with the CSAR that accounting and auditing standards in the country are consistent with international standards. South Africa, through its highly developed professional bodies and firms, plays an important role in international standard-setting bodies.
670. Two concerns are, however, evident. First, there is no legal backing for “big GAAP”, as mandated by the JSE for listed corporations. The CRM understood that the current corporate law reform project will remove this shortcoming. Second, all companies listed

on the JSE, including SMMEs listed on the AltX, are required to comply with “big GAAP” and, consequently, the IFRS. This creates financial reporting complexities for SMMEs. The CRM concurs with the IASB, as reported in the CSAR, that separate accounting standards for “limited interest companies” such as SMMEs need to be promulgated. The CRM understood that as part of the revision of the Companies Act, SMMEs will be exempted from following the IFRS.

671. To this end, the CRM would like to highlight the work done by the Eastern, Central and Southern African Federation of Accountants (ECSAFA), which has prepared an “Exposure Draft on ECSAFA Guidance on Financial Reporting for SMEs”. The document endeavours to reduce financial reporting complexities for SMEs by providing that they apply only certain sections of the IASB Framework for the Preparation and Presentation of Financial Statements (certain principles in IAS 1: Presentation of financial statements; IAS 7: Cash flow statements; and IAS 8: Accounting policies, changes in accounting estimates and errors). The Guide is intended to fill the void created by the absence of acceptable standards available from the IASB.

Box 5.2: Thuthuka Education Upliftment Project

Thuthuka (a Zulu verb meaning “to develop”) is the response by SAICA to the need to transform the CA profession and make its membership reflect the country’s demography in terms of race and gender. It does this by promoting chartered accountancy as a first-choice career among individuals from previously disadvantaged backgrounds and supporting them through SAICA’s holistic bursary schemes and learning experience.


The TEUP was first launched in May 2002 in the Eastern Cape, funded by the National Skills Fund (NSF) of the Department of Labour, and Fasset (the SETA for Finance, Accounting, Management Consulting and other Financial Services). It has programmes in six provinces with the support of the NSF, Fasset, the Department of Science and Technology, Emperor’s Palace and others, including members of the accounting profession.

The TEUP has recorded numerous achievements. In 2005 and 2006, students supported by the project achieved high pass rates in Grade 12, university and other tertiary education programmes. Because of its positive impact, the initial grant funding of R62 million has been swelled by a further R75 million from the NSF for the roll-out to Limpopo and KwaZulu-Natal, a further R50 million for the five-year roll-out in Gauteng, R25 million from the Department of Science and Technology, and over R20 million in support from Fasset for various programmes.

Source: www.saica.co.za.

672. The CRM found that South Africa has highly skilled accountants and auditors who provide services similar to those available in developed economies. The major issue, however, is the chronic shortage of black chartered accountants (CAs) in the country, as was widely acknowledged by all stakeholders. By 2006, black accountants constituted less than 2.9 per cent of the accounting population. For example, in June 2006, only 717 of a total





of 25 113 CAs were black. As a result, SAICA has introduced the Thuthuka Education Upliftment Project (TEUP), as described above in Box 5.2.

673. The Independent Regulatory Board of Auditors, which was formerly the Public Accountants' and Auditors' Board (PAAB), SAICA, the Association for the Advancement of Black Accountants of Southern Africa and other professional firms have taken steps to increase the number of black CAs. In tandem with these noble initiatives, the CRM is of the opinion that the current educational systems and paradigms need to be transformed to produce the required number of highly skilled black CAs faster, thereby ensuring the consistent growth of high-calibre accountants in the country. An accounting technician-type of qualification will also need to be promoted to provide accounting clerk and bookkeeper skills, as CA qualifications alone will not meet the needs of the country.
674. The CSAR raises a number of concerns about effective oversight of the enforcement of sanctions and non-compliance in disclosure requirements. First, it is concerned about the use of special purpose vehicles to disguise information from stakeholders. An issue related to this is that directors are not accountable to all shareholders in respect of party transactions within conglomerate structures. According to the April 2003 World Bank Accounting and Auditing ROSC for South Africa: "The absence of effective regulatory enforcement mechanisms facilitates uncontrolled manipulation of accounting policies and a mere appearance of compliance, rather than one of substance. Many companies have the availability of highly skilled accountants and auditors who seem to use sophisticated accounting manipulations that may not be evident from a reading of financial statements. As a result, in many cases non-compliance of the established accounting standards takes place, yet giving the appearance of full compliance." The course of the ROSC review revealed that many South African companies perform off-balance-sheet transactions using special purpose entities created at home and abroad, and that huge amounts of liabilities and risk exposures remain hidden from stakeholders. Second, the enforcement of sanctions for non-compliance with financial disclosure regulations is weak, especially because of resource and capacity constraints at CIPRO. Lastly, poor coordination among key actors in financial, microfinance, competition and company regulators is adversely affecting the effective enforcement of sanctions.
675. The CRM noted that steps are being taken to improve the existing mechanisms for enforcing compliance with accounting and auditing standards. In February 2004, the Accounting Practices Board took a decision to issue the text of the IFRS without any amendments. Companies are therefore mandated to comply with the IFRS. From 1 April 2006, the APA provided greater regulation of auditors through the newly established IRBA. This has given the statutory regulator of the auditing profession a more effective governance structure and a broader mandate for efficient regulation.
676. The JSE and the FSB have stepped up their efforts to scrutinise the annual financial statements of listed companies. To complement this effort, the JSE, in partnership with SAICA, has established a GAAP Monitoring Panel for investigating complaints relating

to inappropriate treatment of transactions in financial statements. Within the ongoing company law reform, an FRC will be established to provide guidance on reporting standards in conformity with the APA. There are also ongoing reforms to strengthen public sector accounting standards so as to improve reporting of SOEs and local authorities, including municipalities. These reform efforts are commendable and, after discussion with SAICA, the CRM concluded that they will go a long way in removing existing weaknesses.

677. The discussion with the SARB revealed that the banking sector regulator, the Registrar of Banks located in the SARB, has adequate capacity to conduct its work. The financial market sector (long and short-term insurance, collective investment schemes, pension and retirement funds, etc.) is supervised by the FSB, which is a self-financed, independent statutory body. The FSB, in turn, is accountable to the Minister of Finance.

Corporate Accountability

678. What remains is for the government to consolidate these gains by enacting amendments to the Companies Act. It is important to provide regulators with adequate capacity in order to ensure that established statutory requirements are properly reinforced. Coordination mechanisms across related regulators are required to reduce duplication of effort and ensure that scarce resources are used effectively and efficiently. This is expected to reduce opportunities for corporate failure by improving the quality of reporting and by minimising occurrences of undetected financial statements reflecting misrepresentation and departures from established accounting and auditing requirements.
679. The CRM concurs with the CSAR that the Companies Act provides the legal basis for company directors to present to shareholders, during AGMs, the audited financial statements covering the profit or loss and the state of affairs of the company. The CRM also agrees that JSE listing rules further mandate listed companies with ensuring that directors maintain full and effective control over their companies, including monitoring of management. Common law prohibits directors from having contractual interests in the companies of which they are board members. A concern raised in the CSAR is that the limited pool of competent directors, particularly truly independent ones, implies that a few individuals hold several directorships. This undermines independence and increases opportunities for conflict of interest of directors serving on multiple boards. The CRM, however, is of the opinion that calls for a ceiling on the number of board appointments a non-executive director should hold may not be a feasible proposition. Action should focus on increasing the capacity of regulators so they can step up their oversight of compliance with the King II Report's code of conduct, as well as other legislation, particularly the proposed reforms to the Companies Act once the amendments are enacted by the parliament.
680. One area that the Code of Corporate Practices and Conduct, which enshrines the core principles in the King II Report, has influenced heavily is that of the board structure. Three important features are evident. First, the King II Report calls for a unitary board structure that has responsibility and is accountable for the performance and affairs of the company.





Such a board structure is common within countries that follow the Commonwealth system of law. It requires a balance of executive and non-executive directors, with a majority of non-executive directors, preferably independent of management. Independence was given a wide definition, departing from the historically tight-knit nature of the South African business community, to emphasise the need for diversity, both in terms of gender and race. Second, the roles of chairperson and CEO must be separate from the position of chairperson being held by an independent non-executive director. Third, further guidelines are given for audits, remuneration and nomination committees whereby independent non-executive directors should be heavily involved. Independent evaluation of board committees is a requirement. The King II Report has made directors in the country carefully evaluate the implications of accepting invitations to serve as a director of a company because of concerns about their ability to fulfil its obligations.

681. During apartheid, SOEs that controlled the utilities, infrastructure, industries and other key strategic sectors of the economy were overtly politicised without serious attention being given to their governance arrangements. Hence, by 1994, when democracy was taking root, the country's SOEs were in a parlous state in tandem with an economy that was slowing down as a result of inward-looking economic policies informed by political isolation and the legacy of racial segregation.
682. The advent of the King I Report offered SOEs and other companies operating outside the public sector a new and efficient corporate governance framework which, though borrowed from international best practices, was adapted to local circumstances. The King II Report advanced lessons learnt from implementing the King I Report to bring to the fore public interest issues and investor rights and interests in the arena of the operational environment and business dealings of South Africa's corporations, including SOEs.
683. A more recent development on the SOE front has been the comprehensive revision of the regulations accompanying the PFMA of 1999 to conform to several requirements of the King II Report. The Protocol on Corporate Governance for SOEs was revised and the MFMA of 2003 was introduced. This Act contains extensive governance obligations on the part of officials and executives associated with municipal financial administration.
684. The landmark initiative that transformed accountability of directors in South Africa is the King I Report of 1994. Unlike the 1992 UK Cadbury Code, which only deals with the financial aspects of governance, the King I Report viewed governance in a holistic manner and mandated company boards to deal with stakeholders linked to the company. The King I Report led to the enactment of the EEA, which legalised its affirmative action principles. The King II Report of 2002 moved the corporate governance agenda forward. A key distinguishing feature of this Report and its related code of corporate practices and conduct is that it approaches corporate governance from a principles perspective rather than rules-based approach and, consequently, defines corporate governance in broadly inclusive terms.

687. The CRM encountered divergent views on how the King II Report should be dealt with in South Africa's ongoing corporate law reform initiative. The draft Bill to be released for comment is expected to address the role of directors under company law. The King II Report's disclosure requirements are voluntary and although the JSE listing regulations require companies to comply, companies can refrain from doing so as long as appropriate reasons are given. One view, therefore, is that legal backing needs to be given to the King II Report's Code of Corporate Practices and Conduct. Opponents of this view argue that business is a difficult matter and because directors and others who run it cannot have the prescience to envisage what will happen from day to day, they need flexibility in the processes associated with administering their companies. They further argue that the rigidity of a statute not only introduces heavy compliance costs, but also does not make business sense. They refer to the USA, where corporate spending on compliance software may have been as high as US\$1.71 billion in 2005.
688. The CRM is of the view that the company law reform in South Africa should be informed by the King II Report and other best practices in corporate governance that are internationally available. This is important in an effort to restore investor confidence eroded by several both national and international corporate failures. However, the law reform project should take care of local contexts. It is important that ongoing consultations with stakeholders on company law reform should continue so that consensus can emerge to ensure that the law is practical from a business perspective and yet also strong enough to protect shareholders' rights. Irrespective of the final outcome of these consultations, the CRM acknowledges that the King II Report in its current self-regulatory form provides good guidance for both private companies and SOEs. It positions the country among the top-ranking emerging market economies that follow corporate governance codes. What is important, is the need for regulators to develop adequate institutional capacity for overseeing the implementation of the King I and II Reports and related codes.
687. A cross-cutting issue in the CSAR is that of gender mainstreaming and the low representation of women in the private sector. A report of the Employment Equity Commission in 2001 showed that women are inadequately represented across all sectors of the economy. Some 87 per cent of all top management positions are held by men, as well as 80 per cent of all senior management jobs. Women currently hold 37.6 per cent of all management and professional jobs combined, which includes the teaching and nursing professions. There are still many barriers preventing women from forging ahead in business. The necessary education and skills are also lacking, which makes access to financial assistance problematic.
688. The CRM noted that although more needs to be done, corporations are striving hard to empower previously marginalised individuals, including women. This is evidenced by the disclosures corporations make in line with the TBL reporting requirements, for example, in the area of employment equity and transformation.





iii. Recommendations

689. The APR Panel recommends that South Africa:

- Develop a programme for monitoring implementation of the PAIA. This will entail providing government officials responsible for implementing the Act with ongoing training on its provisions; building the capacity of institutions that process requests for information by the public; and supplementing these efforts with full political commitment to implement the PAIA. [Government Agencies; Public Protector; National Archives; DPSA; South African Human Rights Commission]
- Develop more transparent disclosure rules for executive pay, especially with regard to executive share options grants and pension and retirement packages. The JSE should step up its oversight responsibilities to monitor compliance with such disclosure requirements. [JSE; IoD]
- Enact amendments to the Companies Act to create an FRC for providing guidance on reporting standards. The Council, once created, should be given adequate capacity for ensuring proper enforcement of established statutory requirements. [Government; CIPRO]
- Ensure that regulators such as the JSE, Registrar of Banks, FSB, CIPRO, etc. have the required capacity to effectively discharge their oversight responsibilities over company compliance with the King II Report's code of conduct as well as other legislation, particularly the proposed reformed Companies Act once amendments are enacted by the parliament. [JSE; SARB; FSB; CIPRO]
- Improve coordination and effectiveness of financial, microfinance and company regulators that currently work in silos. [SARB; DTI; Ministry of Finance; FSB]
- Ensure, within ongoing corporate law reforms, that SMMEs are not mandated to comply with the costly "big GAAP" requirement but rather apply simplified accounting standards. The work done by ECSAFA may be a useful guide for policy in this area. [CIPRO]
- In tandem with ongoing initiatives by the IRBA and SAICA to increase the number of black CAs in the country, change the curricula in relevant institutions to respond to the need for more qualified accountants, so that skilled accountants can be produced at various levels (CAs, accounts clerks, etc.) to meet the challenges of the country. [Government; IRBA; SAICA; Relevant Professional Accountancy Bodies]
- Maintain ongoing dialogue with stakeholders to determine the extent to which the company law reform in the country can be informed by the King II Report, so that consensus can emerge to ensure that the law is practical from a business perspective and yet strong enough to protect shareholders' rights. [Government; Social Partners e.g. IoD, BUSA, SAICA, JSE]

- Enhance compliance with disclosure of environmental accidents and audit results, ethical standards and accounting for CSI. Consider introducing legislation and effective monitoring measures for governing disclosure of issues such as women in management and anti-sexual harassment policies and practices. Building on efforts by the JSE, this may require developing further systems for collecting, analysing and disseminating information about the performance of large corporations in these areas, as well as appointing a government lead agency for corporate responsibility, whose mandate would include the enforcement of social reporting requirements. [Government; DTI; JSE; IoD]
- Improve disclosure requirements for contingent liabilities and non-financial matters in line with the IFRS. [CIPRO; SARB; ASB; SAICA; JSE; IRBA]
- Continue to train more potential directors to increase the pool of competent directors, particularly of black people, women and other disadvantaged groups. [IoD]
- Give “big GAAP” legal backing by amending the Companies Act. [CIPRO]
- Expedite work on updating the public sector accounting standards by revising the PFMA to enhance the accountability of SOEs. [Government; SAICA; Professional Bodies for Accountants]
- Build the capacity of public bodies to implement the legislated reporting structures, especially for SOEs in municipal and local government structures, and eliminate the “double burden” imposed on public entities by the Companies Act and the PFMA. [Government; SAICA; Professional Bodies for Accountants; Provincial and Local Government Agencies]
- Introduce effective monitoring measures and legislation governing the disclosure of certain types of non-financial matters, such as environmental risks, gender issues, women in management, and anti-sexual harassment policies and practices. [IoD; JSE]

