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**The enforcement of the King IV Code with emphasis on the role of
the board of directors for corporate governance in South Africa**

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This dissertation is submitted in fulfilment of the requirements
for the degree of Master of Laws (Business Law)

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2019

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ABSTRACT

Corporate governance refers to the processes used to manage a company. The governing body of an organisation, which includes the board of directors of a company, is responsible for corporate governance. The King IV Code (The Code) recommends principles and practices to achieve good corporate governance in South Africa. While, following of the Code by directors is voluntary, there is a need for its enforcement, because the decisions of directors affect all stakeholders. Internal and external stakeholders of the company benefit from good corporate governance. The Code can be enforced by its application, the business judgement rule, the Johannesburg Stock Exchange (JSE) listing requirements and the Companies Act 71 of 2008. This study adopts a desktop research incorporating case law, legislation, journals, diagrams, articles, research papers and a comparative analysis of expert views to examine the effect and enforceability of the Code. The research is exploratory in nature and includes a literature study, which provides an understanding of the need for enforcement of the Code. The objective of this study is to examine the application of the Code on the boards of directors to establish why it needs to be enforced and the mechanisms through which it can be enforced.

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List of Abbreviations

B-BBEE	Broad-Based Black Economic Empowerment
CAB	Companies Amendment Bill
CEO	Chief Executive Officer
CGF	Corporate Governance Framework
CIPC	Companies and Intellectual Property Commission
CPD	Continuous Professional Development
IIRC	International Integrated Reporting Council
IODSA	Institute of Directors of South Africa
IT	Information Technology
JSE	Johannesburg Stock Exchange
MOI	Memorandum of Incorporation
OECD	Organisation for Economic Co-operation and Development
SMEs	Small and Medium-Sized Enterprises

CHAPTER 1

INTRODUCTION

I. INTRODUCTION

Corporate governance is defined as ‘the exercise of ethical and effective leadership by the governing body and incorporated legal entities (such as companies), towards achievement of the governance outcomes of ethical culture, good performance, effective control and legitimacy’.¹ The principles of transparency, fairness, accountability and responsible behaviour are important to attain good corporate governance.² Corporate governance is recognised internationally³ and is concerned with the practices used to manage a company.⁴ Therefore, good corporate governance depends on the ability to make sustainable decisions based on economic, social and environmental factors.⁵

South African corporate law is mainly regulated by the Companies Act⁶ (the Act) and the Code.⁷ In 1992, the King Committee formed through the Institute of Directors of South Africa (IoDSA) codified standards of conduct applicable to all listed companies (King 1).⁸ In 1992, the King II Code reviewed the King I Code and included the notion of ‘triple bottom line reporting’. In 2009, the King III Code⁹ was published in response to the Companies Act of the time.¹⁰ The Code was published in 2016 in reply to issues such as financial instability, climate change

¹ IoDSA, The King IV Code (2016) 11.

² TM Booysen, ‘Governance: Promoting good governance – imperatives for accountability’ (2015) 3 available at https://www.cgfresearch.co.za/Portals/0/docs/2015/Articles/20150518_Promoting_good_governance_Imperatives_for_accountability.pdf, accessed on 30 May 2020.

³ OECD, G20/OECD Principles of Corporate Governance, OECD Report to G20 Finance Ministers and Central Bank Governors (2015) available at <https://www.oecd.org/corporate/ca/Corporate-Governance-Principles-ENG.pdf>, accessed on 2 May 2020; R Harris *Corporate Governance Law Reform in South Africa* (unpublished masters thesis, University of Pretoria, 2016) 8; WHC Parry *The Responsibilities of the Board of Directors in Promoting the Principles of Corporate Governance* (unpublished masters thesis, University of Cape Town, 2014) 1.

⁴ B Coyle *Corporate Governance* 5 ed (2010) 3.

⁵ TM Booysen op cit note 2 at 3.

⁶ The Companies Act 71 of 2008.

⁷ IoDSA, The King IV Code (2016); OECD, ‘OECD Corporate Governance Factbook’ (2019) 39 and 43, available at <https://www.oecd.org/corporate/Corporate-Governance-Factbook.pdf>, accessed on 30 May 2020.

⁸ T Wiese *Corporate Governance in South Africa: With International Comparisons* 2 ed (2017) 19.

⁹ Ibid.

¹⁰ The Companies Act 71 of 2008.

concerns, technological disruptions and more rigorous stakeholder expectations.¹¹ The King Codes have shaped the landscape of corporate governance in South Africa.

Corporate governance was created as a result of the ownership of the company being separated from its control;¹² directors became responsible to manage the company over which the owners of companies had no control,¹³ leading to an abuse of power by directors.¹⁴ For this reason, corporate governance was introduced.¹⁵ Directors came to be responsible not only for the health of the company, but also for the broader economy, the environment and society.¹⁶

In the case of *South African Broadcasting Corporation Ltd v Mpofu*¹⁷ the court held:

‘Integrity is a key principle underpinning good corporate governance. Put clearly, good corporate governance is based on a clear code of ethical behavior and personal integrity exercised by the board, where communications are shared openly . . .’¹⁸

The responsibility for corporate governance and the strategic direction of the company is placed on the board of directors.¹⁹ There is a high standard of conduct required of company directors;²⁰ a director must perform his/her functions according to the standard set in the Act²¹ and implement a Corporate Governance Framework (CGF).²² Therefore, there is a need for mechanisms to enforce good corporate governance, to inform the strategic direction of a company.

¹¹ Wiese op cit note 8 at 19.

¹² GJ Rossouw, A Van der Watt & DP Malan ‘Corporate governance in South Africa’ (2002) 37(3) *Journal of Business Ethics* 289; N Kondlo *The Importance of Corporate Governance in South African Family-Owned Companies: Effects of Ownership and Board Composition on Performance* (unpublished masters thesis, University of Western Cape, 2016) 7.

¹³ Ibid.

¹⁴ Ibid.

¹⁵ Rossouw, Van der Watt & Malan op cit note 12 at 289.

¹⁶ IoDSA *The King IV Code* (2016) 21 – 24.

¹⁷ (2009) 4 All SA 169 (Gauteng High Court).

¹⁸ At paragraph 64.

¹⁹ MM Botha ‘The Role and Duties of Directors in the Promotion of Corporate Governance: A South African Perspective’ 2009 *Obiter* 702.

²⁰ Deloitte ‘Duties of Directors’ (2013) 4 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/ZA_Duties-Of-Directors_101017.pdf, accessed on 31 May 2020.

²¹ Deloitte ‘Duties of Directors’ (2013) 5 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/ZA_Duties-Of-Directors_101017.pdf, accessed on 31 May 2020; S 76 of the Companies Act 71 of 2008.

²² TM Booysen op cit note 2 at 3; J Palmer & TM Booysen ‘Do You Really Need A Corporate Governance Framework?’ (2017) 1 – 3 available at <https://www.cgfresearch.co.za/Portals/0/docs/2017/Articles/20170228-Do-you-really-need-a-Corporate-Governance-Framework%C2%AE.pdf>, accessed on 30 May 2020.

In the case of *Minister of Water Affairs and Forestry v Stilfontein Gold Mining Co Ltd* it was held:

‘Practising sound corporate governance is essential for the well-being of a company and is in the best interest of the growth of South Africa’s economy, particularly in attracting new investments and potential investors.’²³

Investors are now accepting the overwhelming evidence that good corporate governance procedures lead to better performing companies and that investors benefit both in the long and short term.²⁴ Directors must possess the relevant experience and be capable of steering the company towards profitability and sustainability,²⁵ by maintaining good corporate governance procedures to attract better investors.²⁶

II. BACKGROUND

Poor directorial decisions and weak corporate governance are often at the heart of many corporate meltdowns.²⁷ The enforcement of the Code will lead to better decision-making and mitigate governance challenges that directors encounter, because the Code recommends principles and practices for the achievement of good corporate governance.²⁸ The Code replaced the King III Code in 1 April 2017²⁹ as an outcomes-based set of guidelines for a changing world.³⁰ The Code addresses fundamental problems of unethical leadership,³¹ inadequate board composition,³² over-

²³ 2006 (5) SA 333 (w) para 16.7.

²⁴ D Crowther & S Seifi *Corporate Governance & Risk Management* (2010) 8.

²⁵ TM Booysen op cit note 2 at 4.

²⁶ Ibid.

²⁷ J Leach *The Correct Understanding of the Business Judgment Rule in Section 76(4) of the Companies Act 71 of 2008: Avoiding the American Mistakes* (unpublished masters thesis, University of Cape Town, 2014) 3.

²⁸ Harris op cit note 3 at 6.

²⁹ PWC ‘A Summary of the King IV Report on Corporate Governance for South Africa’ (2016), 4 available at <https://www.pwc.co.za/en/assets/pdf/king-iv-steering-point.pdf>, accessed on 30 May 2020.

³⁰ Ibid 1.

³¹ IoDSA, The King IV Code (2016) Part 5.1, Principle 1, Recommended Practice 1; Ernst & Young, ‘Are you ready to implement King IV? A shift of focus: The King IV Report on Corporate Governance’ (2016) 8 available at [http://www.ey.com/Publication/vwLUAssets/ey-governance-with-king-iv2016/\\$FILE/ey-governance-with-king-iv-2016.pdf](http://www.ey.com/Publication/vwLUAssets/ey-governance-with-king-iv2016/$FILE/ey-governance-with-king-iv-2016.pdf), accessed 23 October 2018; Deloitte ‘King IV: Bolder Than Ever’ (2016) 5 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/DeloitteZA_KingIV_Bolder_Than_Ever_CGG_Nov2016.pdf, accessed on 30 May 2020.

³² IoDSA, ‘Governance issues for boards to consider in 2016,’ (2016), 4 available at https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/05E93ACB-10BE-4507-9601-307A66F34BD8/IoD_CGN_Governance_Issues_paper.pdf, accessed on 30 May 2019; IoDSA, The King IV Code (2016) Part 5.3, Principle 7, Recommended Practice 6; IoDSA, The King IV Code (2016) 28; IoDSA, The King IV Code (2016) Part 5.1, Principle 1, Recommended Practice 1; Ernst & Young op cit note 31 at 12.

remuneration of directors,³³ value creation,³⁴ inadequate stakeholder communication,³⁵ cyber security,³⁶ risk oversight³⁷ and over-regulation.³⁸ This underlines the need for the Code to be enforced.

Corporate governance provides the benefits of increased transparency and accountability,³⁹ creation of wealth,⁴⁰ shareholder confidence,⁴¹ stakeholder confidence,⁴² access to finance,⁴³ improved market value⁴⁴ and improved efficiency and performance of the company.⁴⁵ Corporate governance ensures sound decisions that reduce risk and increase returns.⁴⁶ According

³³ Deloitte 'King IV Remuneration Governance' (2017) 4 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/za_Deloitte_KingIV_Remuneration_Governance_01032017.pdf, accessed on 3 May 2020; IoDSA, The King IV Code (2016) Part 5.4, Principle 14, Recommended Practice 26 – 27; IoDSA, The King IV Code (2016) Part 5.3, Principle 8, Recommended Practice 65 – 66; IoDSA, The King IV Code (2016) Part 5.3, Principle 7, Recommended Practice 36; IoDSA, The King IV Code (2016) Part 5.3, Principle 10, Recommended Practice 79; Ernst & Young op cit note 31 at 17; R Naidoo *An essential Guide for South African Companies* 3 ed (2016) 49.

³⁴ IoDSA, 'General Guidance Note, Summary of King IV Disclosure Requirements' (2016), 2 available at https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/49D62EF3-F749-403C-BE47-73C50F27F30F/General_Guidance_Note_on_Summary_of_King_IV_Disclosure_Requirements.pdf, accessed on 30 May 2020; Ernst & Young op cit note 31 at 10; IoDSA *The King IV Code* (2016) 4.

³⁵ IoDSA, 'General Guidance Note, Summary of King IV Disclosure Requirements' (2016), 7 available at https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/49D62EF3-F749-403C-BE47-73C50F27F30F/General_Guidance_Note_on_Summary_of_King_IV_Disclosure_Requirements.pdf, accessed on 30 May 2020; Ernst & Young op cit note 31 at 18.

³⁶ IoDSA, The King IV Code (2016) 3; M Damianides 'Sarbanes-Oxley and IT Governance: New Guidance on IT Control and Compliance' (2005) 22(1) *Information Systems Management* 77–78.

³⁷ IoDSA, The King IV Code (2016) 30; Y Smit *A Structured Approach to Risk Management for South African SMEs* (unpublished doctoral thesis, Cape Peninsula University of Technology, 2012) 56; IoDSA, The King IV Code (2016) Part 5.4, Principle 11, Recommended Practice 1 and 6.

³⁸ IoDSA, The King IV Code (2016) 30.

³⁹ JD Sullivan, A Wilson & A Nadgrodkiewicz 'The role of corporate governance in fighting corruption' 1 available at https://www2.deloitte.com/content/dam/Deloitte/ru/Documents/finance/role_corporate_governance_sullivan_eng.pdf, accessed on 30 May 2020; MS Radebe 'The Benefits of Good Corporate Governance to Small and Medium Enterprises (SMEs) in South Africa: A View on Top 20 and Bottom 20 JSE Listed Companies' (2017) 15(4) *Problems and Perspectives in Management* 274; D Crowther & S Seifi op cit note 24 at 10; PM Masegare *Critical Analysis of Corporate Governance Implementation and Control Systems within the Municipal Sector in Gauteng Province in South Africa* (unpublished doctoral thesis, University of Kwazulu-Natal, 2016) 33.

⁴⁰ Sullivan, Wilson & Nadgrodkiewicz op cit note 39 at 6; McKinsey & Company 'Global Investor Opinion Survey: Key Findings' (2002) 2 available at <http://www.eiod.org/uploads/Publications/Pdf/II-Rp-4-1.pdf>, accessed on 3 September 2018.

⁴¹ OECD op cit note 3 at 19; HJ Gregory & S Austin, 'Corporate governance issues for 2015' (2014) available at <https://corpgov.law.harvard.edu/2014/12/12/corporate-governance-issues-for-2015/>, accessed on 13 April 2018; Radebe op cit note 39 at 274.

⁴² Radebe op cit note 39 at 273 – 274.

⁴³ R Naidoo *Corporate Governance: An Essential Handbook for South African Companies* 2 ed (2009) 38; D Crowther & S Seifi op cit note 24 at 15; Masegare op cit note 39 at 27.

⁴⁴ M Ncube 'Corporate Governance, Firm Valuation and Performance' (2006) Paper presented at a Conference on 'Can Africa Claim the 21st Century' *African Development Bank* 2; Sullivan, Wilson & Nadgrodkiewicz op cit note 39 at 6.

⁴⁵ D Crowther & S Seifi op cit note 24 at 11 – 15.

⁴⁶ Kondlo op cit note 12 at 21.

to Serretta, Bendixen and Sutherland, a director needs to adhere to his/her corporate governance responsibilities to create value and a sustainable company.⁴⁷ Kondlo asserts that a company must establish best-suited practices of corporate governance, as the practices will differ depending on its context.⁴⁸ It is evident that the Code provides different companies with appropriate guidelines.⁴⁹ This further underlines the need for appropriate enforcement.

The Code can be enforced through its application, because once it is adopted, an application of the principles is assumed as having been accepted and the company is bound to explain how it has been implemented to give effect to the governance outcomes, in its annual reports.⁵⁰ According to Meyer, to prevent companies from merely stating of corporate governance, the Code has provided relevant principles and practices for boards of directors to apply and explain, giving effect to the specific underlying governance principles.⁵¹ Further, Natesan states that by insisting that directors explain why they took certain actions, the Code ensures they ‘apply their minds to the challenge of achieving the goal set by the principle’.⁵² Therefore, directors cannot hide behind mindless compliance.⁵³

Enforcing good corporate governance principles of the Code affords protection to directors if they can demonstrate they exercised good business judgement by taking reasonable steps to comply. However, according to Booysen, there should be a clear distinction of the consequences for directors who blunder in their duties.⁵⁴ The person’s seniority of appointment, pay grade, experience and the extent of the damage must be considered.⁵⁵ It is not proper to place an unqualified person in a directorship position, since a business failure could adversely affect the company and its board. Further, a director faces a potential delinquency order from a court, which

⁴⁷ H Serretta, M Bendixen & M Sutherland ‘Core Corporate Governance Dilemmas Facing Boards: A South African Perspective’ (2009) 12(2) *South African Journal of Economic and Management Sciences* 198.

⁴⁸ Kondlo op cit note 12 at 20; JJ Du Plessis. ... et al *Principles of Contemporary Corporate Governance* (2005) 11.

⁴⁹ M Meyer ‘The 4 Kings Of King IV: A New Era Of Corporate Governance’ (2017) available at <http://www.talenttalks.net/4-kings-king-iv-new-era-corporate-governance/>, accessed on 11 May 2018.

⁵⁰ Ibid; P Natesan & P Du Plessis ‘Why King IV’s ‘apply and explain’ is so important’ (2019) available at <https://www.iodsa.co.za/news/438882/Why-King-IVs-apply-and-explain-is-so-important.htm>, accessed on 8 April 2019; S Dlamini ‘JSE makes King IV provisions mandatory for listed entities’ (2017) available at <https://www.iol.co.za/business-report/jse-makes-king-iv-provisions-mandatory-for-listed-entities-9915866>, accessed on 9 January 2019.

⁵¹ Meyer op cit note 49.

⁵² P Natesan & P Du Plessis op cit note 50.

⁵³ Ibid.

⁵⁴ TM Booysen op cit note 2 at 2.

⁵⁵ Ibid.

can critically affect a director's chance of being placed on a board again.⁵⁶ Therefore, the Code should be enforced through the business judgement rule where a director who fails in his/her statutory/fiduciary duties can escape liability, if he/she took reasonable steps to become informed in the process leading to a decision.⁵⁷

The Code should be enforced through the JSE, which is licensed as an exchange under the Securities Services Act.⁵⁸ According to Bhika, institutional investors practise governance initiatives that enhance the market value of client portfolios.⁵⁹ Further, investors have adopted a hands-on role in the management and business affairs of their investee companies to safeguard their interests.⁶⁰ In addition, increased institutional investor ownership can better monitor and enhance corporate governance procedures.⁶¹ All listed companies must comply with the JSE listing requirements, which are 'amended from time to time'.⁶² Therefore, it is in the interest of listed companies to comply with the JSE listing requirements and the Code to attract better investors who will assist in ensuring the company practises good corporate governance.

While the Code is voluntary; it can be argued that many of its principles are in effect mandatory and should be enacted into law.⁶³ According to Malherbe and Segal, corporate governance in South Africa has transformed from a 'soft' ethical issue to a 'hard' issue, necessary for the success of capital markets and the corporate economy.⁶⁴ Further, according to Coyle, various corporate governance principles have been codified into laws, while others remain uncoded.⁶⁵ In the absence of any statutory requirement to apply the principles of the Code, some companies fail to comply because non-compliance does not attach any legal sanctions.⁶⁶ However, Harris concludes that there are many reasons for legally codifying corporate governance principles

⁵⁶ Ibid.

⁵⁷ Naidoo op cit note 33 at 212; A Visser 'Line Challenge, The Application and Enforcement of King IV' (2016), 3 available at https://www.adamsadams.com/wp-content/uploads/2016/11/King-IV_APPLICATION_ENFORCEMENT.pdf, accessed on 18 October 2018.

⁵⁸ Act 36 of 2004.

⁵⁹ V Bhika *Corporate Governance in South Africa: The Role of Institutional Investors* (unpublished masters thesis, University of Cape Town, 2014) 7.

⁶⁰ V Bhika op cit note 59 at 6 – 7.

⁶¹ Ibid.

⁶² JSE Listing Requirements 1.2; Wiese op cit note 8 at 23; Parry op cit note 3 at 24.

⁶³ Harris op cit note 3 at 6.

⁶⁴ S Malherbe & N Segal 'Corporate governance in South Africa' (2001) available at http://www.tips.org.za/files/Corporate_Governance_in_South_Africa.pdf, accessed on 30 May 2020.

⁶⁵ Coyle op cit note 4 at 36; Nexia SAB&T 'King IV Report' (2016), available at <https://www.nexia-sabt.co.za/sabtips/king-iv-report/>, accessed on 4 April 2019.

⁶⁶ Coyle op cit note 4 at 36.

on issues such as the role of the Chief Executive Officer (CEO) and information technology governance.⁶⁷ In summary, there is a need for principles of the Code to be codified in the interest of a sound corporate economy.

The Constitution requires that the theory and practice of company law considers the interests of all stakeholders.⁶⁸ While the Code is not a law as such, many of its principles are reflected as law in the Act,⁶⁹ which sets out *inter alia* the duties and liabilities of directors and prescribed officers,⁷⁰ and provisions for the appointment of a company secretary⁷¹ and an auditor.⁷² Not only does the Act encourage accountability and transparency,⁷³ but also provides for a new body called the social and ethics committee.⁷⁴ This illustrates how the Code may be enforced through provisions of the Act.

The relationship between the Code and the Act is grounded in section 7(b)(iii) of the Act, which states the goal to:

‘Promote the development of the South African economy by . . . - encouraging transparency and high standards of corporate governance as appropriate, given the significant role of enterprises within the social and economic life of the nation.’

Section 7(1) of the Act requires a predictable working environment where regulatory bodies ensure adequate regulatory governance of companies.⁷⁵ If the board of directors acts in a manner that contravenes any provision of the Act, it can result in a penalty being imposed by the Companies and Intellectual Property Commission (CIPC).⁷⁶ Therefore, enforcing the Code will drive directors to comply with their corporate governance obligations.

⁶⁷ Harris op cit note 3 at 31.

⁶⁸ Wiese op cit note 8 at 31.

⁶⁹ Nexia SAB&T op cit note 65.

⁷⁰ S 77 of *Companies Act 71 of 2008*.

⁷¹ Ss 86 and 88 of the *Companies Act 71 of 2008*.

⁷² Ss 90 and 92 of the *Companies Act 71 of 2008*.

⁷³ S 34 and Ch 3 of the *Companies Act 71 of 2008*.

⁷⁴ S 72(4) of the *Companies Act 71 of 2008*.

⁷⁵ Parry op cit note 3 at 24.

⁷⁶ S 171, s 185, s 186, s 187 of the *Companies Act 71 of 2008*; Parry op cit note 3 at 22.

III. ISSUE

The main issue this study seeks to examine, and address is the following:

- (a) *Whether compliance with the King IV Code can be enforced on the board of directors with regards to corporate governance in South Africa?*

To address this issue an examination is needed of the application of the Code on the function of boards of directors, to provide evidence of the need for its enforcement and why it should be enforced. The study will identify how the Code can be enforced through the business judgement rule, the listing requirements of the JSE and its synergy with certain provisions of the Act.

IV. RESEARCH METHODOLOGY

The study is by desktop research comprising of case law, legislation, diagrams, and articles to analyse the effect and enforceability of the Code. It includes a study of the subject of corporate governance, providing an understanding of the benefits and challenges faced with corporate governance and the need for its enforcement through the Code. A comparative analysis of the views of various academics, authors and experts in academic articles, research papers and journals will be highlighted to examine the effect and enforceability of the Code. Electronic and website references will contribute significantly to this study. The research is exploratory in nature, as it will examine corporate governance in South Africa.

V. RESEARCH OBJECTIVES

The objective of this study is to examine the principles and recommendations of the Code and its application to boards of directors to establish why it needs to be enforced and the mechanisms through which it can be enforced. Therefore, it is important to research the definition and evolution of corporate governance, the effect and enforceability of the Code and the extent to which the Code addresses corporate governance challenges in South Africa. This analysis will focus on the individual directors and their roles in terms of the Code. The Code is relatively new and has rarely been investigated by many scholars.⁷⁷ The subject is important because corporate governance is

⁷⁷ A Chakanika *Corporate Governance in South Africa: Progress and Challenges* (unpublished masters thesis, University of Cape Town, 2013) 3.

important to promote investment, especially in South Africa, where foreign direct investment is crucial.⁷⁸

⁷⁸ Harris op cit note 3 at 8.

CHAPTER 2

THE IMPORTANCE OF CORPORATE GOVERNANCE

I. INTRODUCTION

This chapter seeks to explain why corporate governance is an important concept that should be enforced, in the process examining the concept, theories, and benefits of corporate governance and citing evidence of its international recognition. The theories of corporate governance enable understanding of the concept, and how it applies to directors and affects other stakeholders, the categories of whom will be scrutinised. Further, the Organisation for Economic Co-operation and Development (OECD) principles which provide a foundation for corporate governance systems internationally will be discussed.

II. THEORIES OF CORPORATE GOVERNANCE

There are many theories relating to the concept of corporate governance, such as the shareholder theory, the agency theory and the stakeholder theory which will be discussed below.

(a) *The shareholder theory*

According to the shareholder theory, the objective of a company is to generate profits and increase shareholder wealth, since the shareholder invests in the company and the operations of the company depend on the capital provided by the shareholder.⁷⁹ According to Pfarrer shareholder theorists believe that the shareholders' intention is to further their self-interest to gain profit for the benefit of society as a whole.⁸⁰ Further, according to Vermaelen, investors should be notified in advance that the objective of the company is not purely profit making, but to also contribute to wider society.⁸¹ However, Rønnegard and Smith assert that this theory presents a major hindrance to corporate social responsibility because directors might be inclined to ignore social responsibility

⁷⁹ MD Pfarrer *What is the Purpose of the Firm? Shareholder and Stakeholder Theories* in J O'Toole & D Mayer *Good business: exercising effective and ethical leadership* (2010) 86; T Wiese *Corporate Governance in South Africa: With International Comparisons* (2014) 8.

⁸⁰ MD Pfarrer op cit note 79 at 87.

⁸¹ T Vermaelen 'Putting a price tag on corporate social responsibility' (2011), available at <https://knowledge.insead.edu/ethics/putting-a-price-tag-on-corporate-social-responsibility-930>, accessed on 30 May 2020.

issues⁸² as inconsistent with their statutory/fiduciary duty to make decisions that further the interests of shareholders.⁸³ Figure 1 represents the shareholder theory of corporate governance where the purpose of the company is to generate profit for shareholders whom are motivated by their own self-interests.



Figure 1 – The shareholder theory⁸⁴

It is important to consider the rights of shareholders because they contribute financially towards the creation of the company with the expectation of a positive return on investment. However, if the shareholder interests become primary then they decide the direction of the company instead of the board of directors. This underlines the importance of the independence of the board of directors to manage the company without hindrance from shareholders as discussed in the next theory of corporate governance.

(b) *The agency theory*

The agency theory emphasises a contractual relationship between shareholders (principals) who delegate the authority to the directors (agents) to make decisions.⁸⁵ According to Adegbite, Amaeshi and Amao, the agency theory proposes that corporate governance concerns the creation of monitoring mechanisms by shareholders to control directors and maximise shareholder wealth.⁸⁶ A contrary view is proposed by Rossouw, Van der Watt and Malan that corporate

⁸² D Rönnegard & NC Smith 'Shareholder Primacy, Corporate Social Responsibility, and the Role of Business Schools' 2014 134 *Journal of Business Ethics* 463 – 464.

⁸³ JL Campbell 'Why would corporations behave in socially responsible ways? An institutional theory of corporate social responsibility' (2007) 32(3) *Academy of Management Review* 952.

⁸⁴ F Narbel & K Muff 'Should the Evolution of Stakeholder Theory be Discontinued given its Limitations?' (2017) 7(5) *Theoretical Economics Letters* 1360.

⁸⁵ Coyle op cit note 4 at 12.

⁸⁶ E Adegbite, K Amaeshi & O Amao 'The politics of shareholder activism in Nigeria' (2012) 105 *Journal of Business Ethics* 391.

governance problems arise between directors and shareholders because of the separation of ownership and control.⁸⁷ Figure 2 illustrates the relationship between directors and shareholders in the agency theory of corporate governance. Figure 2 illustrates that while shareholders (owners) appoint directors (controllers) to act in their interests and manage the company, both directors and shareholders are still motivated by their own self-interest. Coyle asserts that for this reason many conflicts of interest arise.⁸⁸ While the agency theory attempts to resolve opposing interests between shareholders and directors,⁸⁹ the interests of directors are favoured over the interests of the shareholder,⁹⁰ resulting in a danger that directors who are not monitored by the shareholder will not act in the best interests of the company.⁹¹ Therefore, the agency relationship should exist to ensure that directors act in the best interests of the company.⁹²



Figure 2 – The agency theory⁹³

The agency theory suggests that managing the conflict between shareholders and directors is an important function of the board of directors.⁹⁴ Therefore, one view of the agency theory associates corporate governance with structural functionalism by assuming that people can be

⁸⁷ Ibid; Rossouw, Van der Watt & Malan op cit note 12 at 289.

⁸⁸ IoDSA, 'Old Mutual row puts conflicts of interest into the spotlight' (2019), available at <https://www.iodsa.co.za/news/459686/Old-Mutual-row-puts-conflicts-of-interest-into-the-spotlight.htm>, accessed on 4 August 2019.

⁸⁹ KM Eisenhardt 'Building Theories from Case Study Research' (1989) 14(4) *The Academy of Management Review* 532.

⁹⁰ Kondlo op cit note 12 at 13.

⁹¹ Ibid 11.

⁹² Ibid.

⁹³ H Abdullah & B Valentine 'Fundamental and Ethics Theories of Corporate Governance' (2009) 4(1) *Middle Eastern Finance and Economics* 90.

⁹⁴ L Donaldson, & HJ Davis 'Stewardship Theory or Agency Theory: CEO Governance and Shareholder Returns' (1991) 16(1) *Australian Journal of Management* 50.

treated as functions.⁹⁵ The contrary view is that people cannot be treated as mere functions and other stakeholders of the company must also be valued.

(c) *The stakeholder theory*

Stakeholders are those individuals or groups who contribute directly or indirectly to the company, and the stakeholder theory focuses on the creation of trust between all stakeholders and the company.⁹⁶ For instance, Hung asserts that directors must balance the conflicting interests of different types of stakeholders⁹⁷ as detailed below. Figure 3 illustrates the different types of stakeholders and their relationship with the company. It is evident from Figure 3 that there is a ‘reciprocal duty of support’ where the company and stakeholders are dependent on each other.

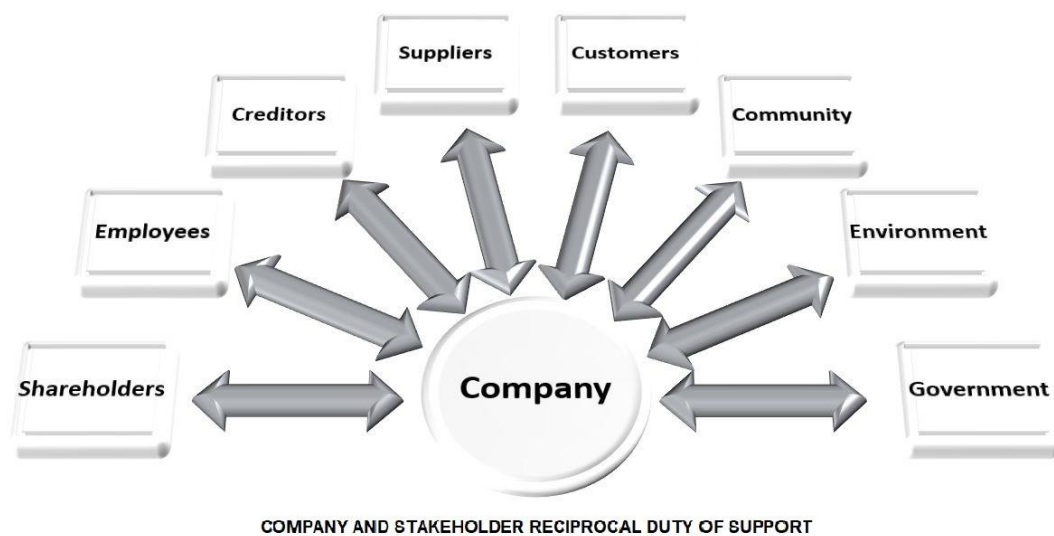


Figure 3 – The stakeholder theory⁹⁸

⁹⁵ B L'huillier 'What does "corporate governance" actually mean?' (2014) 14(3) *Corporate Governance: International Journal of Business in Society* 306.

⁹⁶ IoDSA, The King III Code (2009) Principle 3.2.

⁹⁷ H Hung 'A typology of the theories of the roles of governing boards' (1998) 6(2) *Corporate Governance Scholarly Research and Theory Papers* 101 – 111; T Donaldson & LE Preston 'The Stakeholder Theory of the Corporation: Concepts, Evidence and Implications' (1995) 20(1) *Academy of Management Review* 79.

⁹⁸ Donaldson & Preston op cit note 97 at 69.

(i) *The shareholders*

Shareholders play a passive rather than active role in corporate governance.⁹⁹ Du Plessis defines a shareholder as an ‘individual, institution, company, or other entity that owns shares in a company’.¹⁰⁰ Accordingly, shareholders are responsible for creating employment for other important stakeholders, such as employees.

(ii) *The employees*

Employees spend most of their lives working in the company.¹⁰¹ According to Bainbridge employees are involved in operational participation, which relates to day-to-day business activities and programmes that promote strategic participation in major policy decisions regarding corporate governance.¹⁰² This said, it is also important for directors to ensure proper procedures exist for employees to report any misconduct.¹⁰³

(iii) *The creditors*

Creditors provide access to finance for the company.¹⁰⁴ Creditors need to be confident that they will be repaid the money lent,¹⁰⁵ with an interest in the continuance of the company as a sustainable institution.¹⁰⁶

(iv) *The suppliers*

Suppliers are interested in the continuance and sustainability of the company to ensure a continuous supply of goods and services.¹⁰⁷ This is also important for customer retention.¹⁰⁸

⁹⁹ JJ Du Plessis. ... et al *Principles of Contemporary Corporate Governance* 2 ed (2011) 25; Wogu, E, O ‘Corporate Governance: The Stakeholders Perspective’ (2016) 4(4) *International Journal of Business and Management Review* 47 – 48.

¹⁰⁰ JJ Du Plessis. ... et al op cit note 99 at 25.

¹⁰¹ Kondlo op cit note 12 at 15.

¹⁰² SM Bainbridge *Corporate Decision-Making and the Moral Rights of Employees: Participatory Management and Natural Law* (unpublished masters thesis, University of California, 1998) 741 – 742; JJ Du Plessis. ... et al op cit note 99 at 28 – 29; Wogu, E, O ‘Corporate Governance: The Stakeholders Perspective’ (2016) 4(4) *International Journal of Business and Management Review* 47 – 48.

¹⁰³ Kondlo op cit note 12 at 15.

¹⁰⁴ A Hargovan ‘Geneva Finance and the “Duty” of Directors to Creditors: Imperfect Obligation and Critique’ (2004) 12 *Insolvency Law Journal* 134.

¹⁰⁵ JJ Du Plessis. ... et al op cit note 99 at 29.

¹⁰⁶ Ibid; Wogu, E, O ‘Corporate Governance: The Stakeholders Perspective’ (2016) 4(4) *International Journal of Business and Management Review* 47 – 48.

¹⁰⁷ AC Mallin *Corporate Governance* 3 ed (2010) 44.

¹⁰⁸ AC Mallin op cit note 107 at 44.

(v) *The customer*

It is important for the company to maintain loyal customers who will not be inclined to enter into another business relationship with competitors.¹⁰⁹ However, modern customers are more aware of corporate behaviour and will tend to demand that the company acts in a socially responsible manner to the community.¹¹⁰

(vi) *The community*

A community is interested in the sustainability of the company, because this will provide more employment.¹¹¹ Moreover, according to Du Plessis, the community increasingly seeks to be satisfied that companies act in an environmentally friendly manner, avoiding pollution of soil and the local environment.¹¹²

(vii) *The environment*

Climate risk is a factor in almost every business and its investment portfolio, presenting significant risks and opportunities for boards of directors.¹¹³ Since the introduction of the Kyoto Protocol in 2005,¹¹⁴ lowering greenhouse gas emissions has become integral to every business in key global trading markets. Therefore, the environment has become an important stakeholder, since shareholders assign more value to companies that take cognisance of opportunities posed by climate change.¹¹⁵

¹⁰⁹ Kondlo op cit note 12 at 15.

¹¹⁰ AC Mallin op cit note 107 at 44; Wogu, E, O 'Corporate Governance: The Stakeholders Perspective' (2016) 4(4) *International Journal of Business and Management Review* 47 – 48.

¹¹¹ Naidoo op cit note 43 at 38.

¹¹² JJ Du Plessis. ... et al op cit note 99 at 31.

¹¹³ Ibid 32; IoDSA, 'What are directors' duties in respect to climate change?' (2018), available at <https://www.iodsa.co.za/news/415733/What-are-directors-duties-in-respect-to-climate-change.htm>, accessed on 4 August 2019.

¹¹⁴ Signatories to The Kyoto Protocol undertook legally binding commitments to reduce greenhouse gas emissions for the period 2008 to 2012.

¹¹⁵ IoDSA, 'What are directors' duties in respect to climate change?' (2018), available at <https://www.iodsa.co.za/news/415733/What-are-directors-duties-in-respect-to-climate-change.htm>, accessed on 4 August 2019.

(viii) *The government*

The government protects the interests of stakeholders by providing companies with incentives that reduce divergence between private and social returns.¹¹⁶ Further, it monitors investment in various industries and notes taxation raised from companies.¹¹⁷ Du Plessis points out that the government analyses corporate trends relating to employment levels, black economic empowerment and supply and demand of goods and services,¹¹⁸ making the government an important stakeholder.

The stakeholder theory maintains that the objective of corporate governance is to consider the interests of key stakeholders. However, directors should give priority to more important stakeholders, making corporate governance under the stakeholder theory a task of balancing competing interests.

III. THE BENEFITS OF CORPORATE GOVERNANCE

Correctly applied, corporate governance leads to many benefits for directors and the company, including better management, greater transparency and accountability, improved access to finance and better performance and market value of the company (Figure 4). In addition, good corporate governance heightens the confidence of investors, shareholders, and stakeholders (Figure 4). Figure 4 illustrates these benefits which will also be discussed below.

¹¹⁶ Coyle op cit note 4 at 15; Wogu, E, O 'Corporate Governance: The Stakeholders Perspective' (2016) 4(4) *International Journal of Business and Management Review* 47 – 48.

¹¹⁷ JJ Du Plessis. ... et al op cit note 99 at 35.

¹¹⁸ JJ Du Plessis. ... et al op cit note 99 at 35.



Figure 4 – The benefits of corporate governance

(a) *An increase in transparency and accountability*

Good corporate governance is an effective anti-corruption tool because it promotes transparency and accountability.¹¹⁹ According to Crowther and Seifi, transparency ensures that information is ‘freely available and accessible to those affected by decisions’.¹²⁰ Not only does corruption affect all businesses, from global conglomerates to small and medium-sized enterprises,¹²¹ but it can also have a devastating effect on a national economy. Corruption leads to reputational damage and loss of stakeholder confidence.¹²² It follows that directors must ensure they are not unwittingly contributing to corruption;¹²³ they should engage in collective action to make the business more transparent through good corporate governance processes.¹²⁴

(b) *Improves investor confidence*

While good corporate governance has been seen to have depended on compliance, analysts are now viewing it as part of good business, since it assists in gaining the confidence of investors,

¹¹⁹ Sullivan, Wilson & Nadgrodkiewicz op cit note 39 at 1; Wogu, E, O ‘Corporate Governance: The Stakeholders Perspective’ (2016) 4(4) *International Journal of Business and Management Review* 47 – 48.

¹²⁰ D Crowther & S Seifi op cit note 24 at 10.

¹²¹ Sullivan, Wilson & Nadgrodkiewicz op cit note 39 at 1.

¹²² McKinsey & Company op cit note 40 at 8.

¹²³ Sullivan, Wilson & Nadgrodkiewicz op cit note 39 at 1.

¹²⁴ D Crowther & S Seifi op cit note 24 at 10.

consumers and the community.¹²⁵ A survey by McKinsey of more than 200 investors with approximately \$2 trillion in assets in 31 countries revealed that a well-governed company attracts more investors.¹²⁶ Further, Radebe states that high-quality corporate governance measures reassure investors and reduce investor due diligence costs.¹²⁷ Therefore, improved corporate governance reduces capital costs, retains shareholders and attracts more investors.¹²⁸

(c) *Improves shareholder and stakeholder confidence*

Corporate governance provides protection to shareholders and stakeholders of the company.¹²⁹ Sullivan, Wilson and Nadgrodkiewicz argue that companies with strong corporate governance measures have fewer agency risks relating to shareholders.¹³⁰ Radebe states that more stakeholders will want to engage with a company that is transparent about its policies and details how they work.¹³¹ While Partner argues that the company should establish and promote a stakeholder engagement process,¹³² Masegare adds that directors should utilise integrated reporting to engage with stakeholders.¹³³

(d) *Improves access to finance*

Good corporate governance creates market confidence and business integrity,¹³⁴ since it assists in securing equity capital, which is crucial to long-term investment.¹³⁵ According to Gregory and Austin, while most companies strive for shareholder wealth creation, in reality, contributions to the wider economy have a further reach than profit.¹³⁶ Radebe states that noticeable progressive

¹²⁵ Radebe op cit note 39 at 273 – 274.

¹²⁶ McKinsey & Company op cit note 40 at 4.

¹²⁷ Radebe op cit note 39 at 273.

¹²⁸ Ibid; Bubbico, R, Giorgino, M & Monda, B ‘The impact of Corporate Governance on the market value of financial institutions: empirical evidences from Italy’(2012) 10.

¹²⁹ OECD op cit note 3 at 19; Grant Thornton, ‘Corporate governance and company performance’ (2019) 20, Grant Thornton available at <https://www.grantthornton.co.uk/globalassets/1.-member-firms/united-kingdom/pdf/documents/corporate-governance-and-company-performance.pdf>, accessed on 12 December 2020.

¹³⁰ Sullivan, Wilson & Nadgrodkiewicz op cit note 39 at 6.

¹³¹ Radebe op cit note 39 at 274.

¹³² AJ Partner ‘Corporate Governance for Small-to-Medium Enterprises’ (2010), available at <https://www.swaab.com.au/publication/corporate-governance-for-small-to-medium-enterprises-smes>, accessed on 30 May 2020.

¹³³ Masegare op cit note 39 at 91.

¹³⁴ OECD op cit note 3 at 31.

¹³⁵ Ibid.

¹³⁶ HJ Gregory & S Austin op cit note 41; Radebe op cit note 39 at 274.

advancements of corporate governance occur when both the economy and market grow.¹³⁷ Further, Engelbrecht suggests that international investors increasingly demand good governance based on moral standards and improved market performance.¹³⁸ Ethical business sets a standard against which stakeholders make decisions.¹³⁹ Therefore, good corporate governance improves access to finance by attracting more investors, shareholders and equity,¹⁴⁰ thereby decreasing borrowing rates and the cost of capital.¹⁴¹

(e) *Improves performance and market value of the company*

Companies with strong corporate governance practices outperform those with weaker governance practices.¹⁴² Radebe argues that even in an emerging market with a poor investment environment, a well-governed company is likely to perform better than its competitors.¹⁴³ Studies have indicated that good corporate governance can influence the market value of the company.¹⁴⁴ Further, Brown and Caylor identify seven corporate governance factors¹⁴⁵ with which to score a valuation of the company.¹⁴⁶ Therefore, corporate governance is vital to the company's long-term development, because it increases the company's market value and rating.¹⁴⁷

(f) *Developing an effective and efficient management*

Corporate governance benefits a company by creating effective and efficient management of the company.¹⁴⁸ Not only does it provide an early warning system against all risks, but it also leads to

¹³⁷ Ibid.

¹³⁸ M Engelbrecht *The Art of Shape Shifting: Facilitating Strategic Foresight to Independent Non-Executive Directors – A Strategic Approach to Corporate Governance in SA* (unpublished doctoral thesis, University of Stellenbosch, 2012) 86.

¹³⁹ Masegare op cit note 39 at 40.

¹⁴⁰ D Crowther & S Seifi op cit note 24 at 15.

¹⁴¹ Ibid.

¹⁴² Sullivan, Wilson & Nadgrodkiewicz op cit note 39 at 6.

¹⁴³ Radebe op cit note 39 at 273. Bubbico, R, Giorgino, M & Monda, B 'The impact of Corporate Governance on the market value of financial institutions: empirical evidences from Italy' (2012) 10.

¹⁴⁴ M Ncube op cit note 44 at 2.

¹⁴⁵ These factors include election of board members on an annual basis; the company has no poison pill; option repricing did not occur within the last three years; average option granted in the past three years did not exceed 3%; directors have attended at least 75 % of board meetings or provided a valid excuse if not attending; the board guidelines are in each proxy statement and directors are subject to stock ownership guidelines.

¹⁴⁶ M Ncube op cit note 44 at 15; LD Brown & ML Caylor 'Corporate Governance and Firm Valuation' (2006) 25(4) *Journal of Accounting and Public Policy* 411.

¹⁴⁷ Naidoo op cit note 43 at 38.

¹⁴⁸ D Crowther & S Seifi op cit note 24 at 11; Grant Thornton, 'Corporate governance and company performance' (2019) 20, Grant Thornton available at <https://www.grantthornton.co.uk/globalassets/1.-member-firms/united-kingdom/pdf/documents/corporate-governance-and-company-performance.pdf>, accessed on 12 December 2020.

effective risk management.¹⁴⁹ Crowther and Seifi state that being effective and efficient entails the adequate use of resources and the creation of processes that lead to results that addresses the needs of the company.¹⁵⁰ In summary, corporate governance ensures an effective and efficient management that ensures the appropriate use of resources.¹⁵¹

IV. THE OECD PRINCIPLES ON CORPORATE GOVERNANCE

In 2007, South Africa became a key partner in the OECD, which works together with governments to establish international standards for environmental, economic, and social challenges.¹⁵² The OECD principles (Figure 5) have become an important tool for implementation of corporate governance, creating an international benchmark.¹⁵³ Figure 5 illustrates the six OECD principles for laying the foundation for corporate governance for each relevant institution.



Figure 5 – The OECD principles of corporate governance ¹⁵⁴

¹⁴⁹ Ibid.

¹⁵⁰ Ibid.

¹⁵¹ D Crowther & S Seifi op cit note 24 at 15.

¹⁵² OECD 'South Africa and the OECD', available at <http://www.oecd.org/southafrica/south-africa-and-oecd.htm>, accessed on 2 May 2020.

¹⁵³ OECD op cit note 3 at 3.

¹⁵⁴ Ibid 5.

(a) *Implementation of a corporate governance framework*

The OECD principles recommend the creation of an effective CGF, which must be in accordance with the rule of law, have effective enforcement and promote transparent and fair markets.¹⁵⁵ All shareholders must be treated equally and afforded adequate redress if their rights are affected.¹⁵⁶ The CGF must assist economic markets to operate in a manner that contributes to good corporate governance.¹⁵⁷ Since the rights of stakeholders are important, the CGF must encourage cooperation between the company and stakeholders to create wealth, employment and financial stability.¹⁵⁸

The OECD recognises the importance of disclosure and transparency, because it ensures an accurate account of a company's performance, financial situation, ownership and governance.¹⁵⁹ Since, directors are responsible for the creation of the CGF, they must ensure that it provides strategic guidance, effective monitoring and management of the company.¹⁶⁰ According to the OECD, provided the relevant legal and financial obligations are met, corporate governance is about maximising value.¹⁶¹ Therefore, the OECD has helped create international recognition for good corporate governance, in which directors play a foundational role.

V. CONCLUSION

This chapter illustrates the importance of corporate governance and its need for enforcement, especially because empirical evidence demonstrates the positive economic impact of strict enforcement of corporate governance,¹⁶² suggesting that good corporate governance should become mandatory. It is also a process that helps companies achieve desirable goals.¹⁶³ Applied correctly, corporate governance provides several benefits for directors and the company, and other reasons for the need for enforcement is that it prevents corruption and encourages transparency¹⁶⁴ and improves a company's access to finance and market value, leading to greater investment and

¹⁵⁵ OECD op cit note 3 at 13.

¹⁵⁶ Ibid 18.

¹⁵⁷ Ibid 29.

¹⁵⁸ Ibid 34.

¹⁵⁹ Ibid 37.

¹⁶⁰ Ibid 45.

¹⁶¹ Coyle op cit note 4 at 14.

¹⁶² A Pietrancosta 'Enforcement of Corporate Governance Codes: A Legal Perspective' 2014 *Doctrine* 28.

¹⁶³ P Natesan & P Du Plessis 'Making corporate governance universal' (2019), available at <https://www.iodsa.co.za/news/435112/Making-corporate-governance-universal.htm>, accessed on 13 August 2019.

¹⁶⁴ Radebe op cit note 39 at 274.

employment.¹⁶⁵ In addition, corporate governance is a key to healthy financial markets,¹⁶⁶ improving efficiency and operational performance.¹⁶⁷ Further, it creates stronger bonds between directors, shareholders and other relevant stakeholders.¹⁶⁸

Corporate governance is important enough to be recognised internationally through the OECD,¹⁶⁹ which forms an international reference point for a CGF.¹⁷⁰ It should be mandatory for directors to implement a CGF. The shareholder theory looks towards the interests of shareholders¹⁷¹ in contrast to the agency theory which focuses on the relationship between directors and shareholders.¹⁷² However, the stakeholder theory is the dominant corporate governance theory in South Africa by virtue of the provisions in the Code.¹⁷³ The Code, which encourages a stakeholder-inclusive approach to corporate governance, will be discussed in the next chapter.

¹⁶⁵ Pietrancosta op cit note 162 at 27.

¹⁶⁶ Ibid.

¹⁶⁷ D Crowther & S Seifi op cit note 24 at 11.

¹⁶⁸ OECD op cit note 3 at 34.

¹⁶⁹ Ibid 3.

¹⁷⁰ Ibid.

¹⁷¹ MD Pfarrer op cit note 79 at 86; Wiese op cit note 79 at 8.

¹⁷² Coyle op cit note 4 at 12.

¹⁷³ IoDSA, The King IV Code (2016) Part 5.5, Principle 16.

CHAPTER 3

THE NEED FOR APPLICATION OF THE KING IV CODE ON THE ROLE OF THE BOARD OF DIRECTORS AS A MEANS OF ENFORCEMENT OF CORPORATE GOVERNANCE

I. INTRODUCTION

This chapter will examine how the application of the Code affects the role of directors in corporate governance, with emphasis on enforcement in the event of non-compliance, providing an analysis of a practical implementation of corporate governance duties of directors and including a critical analysis of the functional governance areas of the Code and examining the objectives, structure and application of the Code. This analysis is required to understand why the Code should be enforced as it attempts to resolve some of the major corporate governance challenges. The King Codes have already made significant strides in terms of their outcomes, principles and practical aspects of corporate governance.¹⁷⁴ The Code took effect on 1 April 2017,¹⁷⁵ replacing the King III Code in the light of changes to the regulatory and corporate governance landscape and difficulties in adopting the King III Code's principles, which faced criticism in the context of a shift in approach from capitalism towards integrated thinking.¹⁷⁶

The Code shifts its principles towards practical implementation and real-world action.¹⁷⁷ It is concise (the 75 principles of King III were condensed to 17 principles)¹⁷⁸ and includes practices which give effect to each principle.¹⁷⁹ Further, the King III Code chapters were reduced from nine

¹⁷⁴ Deloitte, 'King IV: Bolder Than Ever' (2016) 3 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/ZA_King_IV.pdf, accessed on 11 May 2018.

¹⁷⁵ Wiese op cit note 79 at 22.

¹⁷⁶ Werksmans 'A review of The King IV Report on Corporate Governance (2016), 6 – 8 available at <https://www.werksmans.com/wp-content/uploads/2013/05/061741-WERKSMANS-king-iv-booklet.pdf>, accessed on 30 May 2020; P Langeni *The Value of Corporate Governance: A Comparison Between the Perceived Value of King III and King II* (unpublished masters thesis, University of Pretoria, 2018) 100.

¹⁷⁷ I Steyn '4 Vital Differences Between King III and King IV on Corporate Governance' (2018) available at <https://www.experthub.info/business/doing-business-in-sa/compliance/4-vital-differences-between-king-iii-and-king-iv-on-corporate-governance-2/>, accessed on 30 May 2020; Ernst & Young op cit note 31 at 4.

¹⁷⁸ Naidoo op cit note 33 at 48; KPMG 'King IV Summary Guide' (2016) 6 available at <https://assets.kpmg/content/dam/kpmg/za/pdf/2016/11/King-IV-Summary-Guide.pdf>, accessed on 30 May 2020; Steyn op cit note 177.

¹⁷⁹ Grant Thornton South Africa, 'King III vs King IV, what you really need to know' (2017) 1 available at https://www.grantthornton.co.za/globalassets/1.-member-firms/south-africa/pdfs/kingiv_feb17.pdf, accessed on 30 May 2020.

to five chapters in the Code, which is illustrated in Figure 6.¹⁸⁰ Figure 6 illustrates these chapters which are designed to provide guidance from leadership, strategy and governance to delegation, reporting and the management of stakeholder relationships. Although the principles in the Code were reduced in number to allow directors to exercise judgement and have a level of flexibility there is a danger of misinterpreting the principles.¹⁸¹ The Code includes a wider variety of organisations, with five sector-specific supplements to provide guidance for small-to-medium enterprises, non-profit organisations, public sector entities, municipalities and pension funds.¹⁸² The Code also asserts that the board of directors is primarily responsible for corporate governance.¹⁸³ The previous reference to the ‘board of directors’ under the King III Code has now changed to the ‘governing body’ under the Code¹⁸⁴ so as to include other organisations, which lack a board of directors.¹⁸⁵ However, this study will refer to the board of directors specifically as they fall under the definition of ‘governing body’.

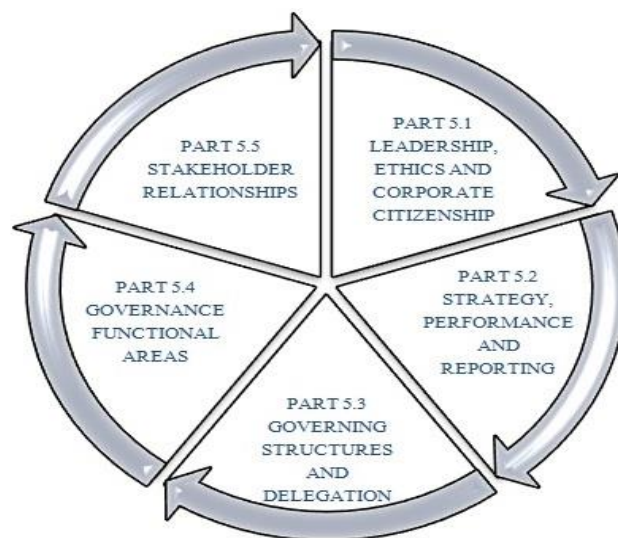


Figure 6 – The five chapters of the King IV Code¹⁸⁶

¹⁸⁰ Ibid.

¹⁸¹ D Anyango *An Exploration of Possible KING-IV Implementation Challenges Relating to Remuneration Disclosures* (unpublished master’s thesis, University of Witwatersrand, 2017) 40 – 41.

¹⁸² Naidoo op cit note 33 at 49.

¹⁸³ IoDSA, King IV Code (2016) 12.

¹⁸⁴ IoDSA, ‘The King IV Report on Corporate Governance’ (2016) 27.

¹⁸⁵ Grant Thornton South Africa op cit note 179 at 1.

¹⁸⁶ Grant Thornton South Africa op cit note 179 at 3.

II. THE APPLICATION OF THE KING IV CODE AS A METHOD OF ENFORCEMENT

Many directors and companies approach compliance with the Code in a ‘tick-box’ manner, which reduces compliance to a set of mechanical actions, without addressing the underlying goal.¹⁸⁷ Mervyn King asserted that many companies simply viewed compliance with the King Codes as a cost of doing business and simply followed as many of the recommended practices as they could, without proper appreciation.¹⁸⁸ However, the ‘apply and explain’ disclosure regime of the Code can be seen as a method of enforcement, since it forces directors to disclose how their actions helped the company achieve its goals.¹⁸⁹ Further, according to Natesan, the Code encourages companies to take a more proactive approach to corporate governance and reap the rewards for doing so.¹⁹⁰ Therefore, an explanation on how the practices are implemented to give effect to the related governance outcomes must be disclosed.¹⁹¹ Figure 7 illustrates how directors can apply the Code to achieve the governance outcomes. Figure 7 illustrates that to achieve the governance outcomes, directors must practice the recommendations of the Code in a manner that gives effect to the overarching principles.



*Figure 7 – The application of the King IV Code*¹⁹²

The legal status of the Code, comprises of a set of voluntary principles and practices.¹⁹³ In the event of a clash, legislation will triumph over the Code.¹⁹⁴ Alternatively, directors must still holistically apply the Code according to practice and guidance notes designed to achieve the four

¹⁸⁷ P Natesan & P Du Plessis op cit note 50.

¹⁸⁸ Ibid.

¹⁸⁹ Ibid; Naidoo op cit note 33 at 49.

¹⁹⁰ Ibid.

¹⁹¹ KPMG op cit note 178 at 6.

¹⁹² Grant Thornton South Africa op cit note 179 at 2.

¹⁹³ Deloitte, ‘King IV: Bolder Than Ever’(2016)10 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/ZA_King_IV.pdf, accessed on 11 May 2018.

¹⁹⁴ Ibid.

governance outcomes of good performance, effective control, legitimacy and an ethical culture.¹⁹⁵ Directors can achieve this by creating an application register, indicating the extent to which the required principles and outcomes have been achieved.¹⁹⁶ This register must be updated annually, endorsed by the board and disclosed on accessible communication platforms.¹⁹⁷ Further, the Code advises directors to set goals, delegate responsibility and assess progress through accountable reporting.¹⁹⁸ This reveals a fundamental shift from compliance-driven disclosure to outcome-based reporting.¹⁹⁹ Therefore, the language of ‘apply and explain’ aptly conveys the Code’s intention to be more than a voluntary code.²⁰⁰

(a) *The importance of the King IV Code in leadership and ethics*

The first principle of the Code is good leadership – the key starting point for developing good governance.²⁰¹ Good governance is not based on principles and practices, but on the character of those tasked with governance;²⁰² the Code’s principles are designed to emphasise effective and ethical leadership, by focusing on the characteristics of the people involved in governance.²⁰³ Directors must act with integrity, in the best interests of the company and avoid conflicts of interest.²⁰⁴ Further, directors must be competent and demonstrate working knowledge of the rules and laws applicable to the company to equip them to adequately fulfil their governance responsibility.²⁰⁵ This underlines the need to enforce the Code, because ethics permeate everything

¹⁹⁵ Naidoo op cit note 33 at 48; Grant Thornton South Africa op cit note 179 at 2.

¹⁹⁶ Deloitte, ‘King IV: Bolder Than Ever’ (2016) 10 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/ZA_King_IV.pdf, accessed on 11 May 2018.

¹⁹⁷ Ibid.

¹⁹⁸ IoDSA, The King IV Code (2016) 28.

¹⁹⁹ Deloitte, ‘King IV: Bolder Than Ever’ (2016) 10 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/ZA_King_IV.pdf, accessed on 11 May 2018.

²⁰⁰ Ibid.

²⁰¹ R Wyngaard ‘King IV – Principle 1: Governance and Leadership’ (2018), available at <https://www.youtube.com/watch?v=MixPJQg4Cck>, accessed on 29 September 2019.

²⁰² The Ethics Institute, ‘KING IV: Focus on Ethical Leadership, not Ethics Management’ (2016) available at <https://www.tei.org.za/index.php/resources/press-releases/7285-king-iv-focus-on-ethical-leadership-not-ethics-management>, accessed on 12 September 2019.

²⁰³ Ernst & Young op cit note 31 at 8.; PWC ‘King IV Code brings the role of ethical and effective leadership to the fore’, available at <https://www.pwc.co.za/en/press-room/king-four-draft.html>, accessed on 12 December 2020.

²⁰⁴ IoDSA, The King IV Code (2016) Part 5.1, Principle 1, Recommended Practice 1.

²⁰⁵ Ibid; Wyngaard op cit note 201.

the company does and the Code guides directors in the practice of ethical leadership, which is linked to ethical corporate citizenship.²⁰⁶

While delegation of functions to a board committee is a critically important part of a directors governance role,²⁰⁷ the board nevertheless remains accountable.²⁰⁸ For this reason, the Code recommends that directors ensure that any delegation of power is clear, effective and intended for the purpose of enhancing the overall effectiveness of the board of directors.²⁰⁹ Effective, ethical leadership entails a proper application of the Code by directors.²¹⁰

The need for ethical leadership is underlined by the creation of social and ethics committees in the Act.²¹¹ The Ethics Institute's view that effective ethics management includes close collaboration with the management functions of companies,²¹² is one of the reasons that has led to a recommendation in the Code for the establishment of social and ethics committees in companies for the oversight of ethics²¹³ and to ensure directors and the wider company are equipped to deliver an ethical culture within the company.²¹⁴ This can be achieved by drafting a social and ethics charter to expressly incorporate the Code and the statutory requirements of the Act.²¹⁵ Further, directors must ensure employees are acquainted with the company's ethical standards by training employees, publishing internal codes of conduct and incorporating such codes of conduct in employee contracts.²¹⁶ However, the Code does not provide a detailed practical approach to ethics management,²¹⁷ but a broad approach to allow directors to exercise good

²⁰⁶ Ibid; Ernst & Young op cit note 31 at 8; PWC 'King IV Code brings the role of ethical and effective leadership to the fore', available at <https://www.pwc.co.za/en/press-room/king-four-draft.html>, accessed on 12 December 2020.

²⁰⁷ IoDSA, The King IV Code (2016) 29.

²⁰⁸ IoDSA, The King IV Code (2016) Part 5.1, Principle 1, Recommended Practice 1; Wyngaard op cit note 201.

²⁰⁹ IoDSA, The King IV Code (2016) Part 5.3, Principle 8, Recommended Practice 41.

²¹⁰ Ernst & Young op cit note 31 at 14 – 15.

²¹¹ L Van Vuuren *Ethics Risk Handbook* (2016) 2.

²¹² Ibid.

²¹³ IoDSA, 'The King IV Report on Corporate Governance' (2016) 29; Deloitte, 'King IV: Bolder Than Ever' (2016) 14 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/ZA_King_IV.pdf, accessed on 11 May 2018.

²¹⁴ IoDSA, The King IV Code (2016) 29; IoDSA, 'General Guidance Note, Summary of King IV Disclosure Requirements' (2016), 2 available at https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/49D62EF3-F749-403C-BE47-73C50F27F30F/General_Guidance_Note_on_Summary_of_King_IV_Disclosure_Requirements.pdf, accessed on 30 May 2020.

²¹⁵ Ernst & Young op cit note 31 at 9.

²¹⁶ F Myburgh & A De Costa 'The key differences between King III and King IV' (2017), available at <https://www.polity.org.za/article/the-key-differences-between-king-iii-and-king-iv-2017-01-11>, accessed on 30 May 2020.

²¹⁷ The Ethics Institute op cit note 202.

judgement.²¹⁸ In contrast, while the King III Code placed a larger focus on practical steps for ethics management, the Code could be argued to envisage ethics management as neither a goal in itself nor a mere ‘tick-box’ exercise, but an evolution to an ethical culture over time.²¹⁹

(b) *Board composition, diversity, and skills*

Companies are increasingly under pressure from stakeholders to appoint board members with diversity, to prevent insular decision-making.²²⁰ Finding the right mix of skills, competencies, capabilities, knowledge and diversity across both race and gender on the board of directors is not without challenges.²²¹ In recent years, diversity in the boardroom has become a hot topic,²²² especially in South Africa where the Broad-Based Black Economic Empowerment Act (B-BBEE)²²³ has been enacted, focusing on historically disadvantaged groups.²²⁴ The 2014 Board Practices Report indicated a ‘lack of generational diversity in boardrooms, with younger directors being in their 50’s’.²²⁵ While older directors have more experience, younger directors introduce a new perspective to the boardroom.²²⁶ The Code addresses this by recommending that the board is composed of ‘an appropriate balance of knowledge, skills, experience, diversity and independence’.²²⁷ Therefore, board diversity requires enforcement of the Code,²²⁸ enabling different perspectives on decisions and strategy.²²⁹

²¹⁸ Ibid.

²¹⁹ Ibid.

²²⁰ HB Kruger *The Impact of Board Diversity on Corporate Governance in Medium-Sized Private Enterprises in Gauteng* (unpublished masters thesis, University of South Africa, 2012) 22.

²²¹ IoDSA, The King IV Code (2016) Part 5.3, Principle 7, Recommended Practice 6.

²²² Deloitte, ‘King IV Diversity in the Boardroom (2017) 1 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/za_KGIV_BoardDiversity_FA.pdf accessed on 3 May 2020.

²²³ Act 53 of 2003.

²²⁴ Deloitte, ‘King IV Diversity in the Boardroom (2017) 4 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/za_KGIV_BoardDiversity_FA.pdf accessed on 3 May 2020.

²²⁵ Deloitte ‘2014 Board Practices Report Perspectives from the boardroom’ (2014) 8 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/ZA_board_practices_report_21092015.pdf, accessed on 4 May 2019.

²²⁶ Deloitte, ‘King IV Diversity in the Boardroom (2017) 3 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/za_KGIV_BoardDiversity_FA.pdf, accessed on 3 May 2020.

²²⁷ IoDSA, The King IV Code (2016) Part 5.3, Principle 7, Recommended Practice 6 – 7.

²²⁸ IoDSA, The King IV Code (2016) 28; Ernst & Young op cit note 31 at 14.

²²⁹ IoDSA op cit note 32 at 4.

Directors must apply an independent and objective mindset²³⁰ to ensure that they are able to lead and make decisions in the best interests of the company.²³¹ Further, directors must be properly skilled, in respect of which the IoDSA offers courses to ensure directors are adequately trained,²³² including the Certified Director qualification, which equips individuals with requisite knowledge and the Chartered Director (SA) qualification which is designed to enhance directorship as a profession in South Africa.²³³ The Code²³⁴ also recommends an assessment and evaluation of the performance of boards of directors every two years.²³⁵ Therefore, the Code supports its recommendation that the composition of boards should promote effective governance and better decision-making.²³⁶

The required level of board independence can be achieved by including independent non-executive directors.²³⁷ The Act's regulations, the Code and the listing requirements of the JSE, propose that approximately 60% of independent non-executive directors should be independent.²³⁸ However, the Code does not specifically address the activities of other non-executive directorships taken on by existing members of the board of directors.²³⁹ This needs to be included in the Code, because if an executive director takes on other non-executive directorships without consulting the CEO, this could be detrimental to the director's existing responsibilities as an executive director.²⁴⁰

²³⁰ IoDSA, The King IV Code (2016) 28; IoDSA, 'Board independence: King IV recommends a balanced approach' (2020), IoDSA available at <https://www.iodsa.co.za/news/486122/Board-independence-King-IV-recommends-a-balanced-approach.htm>, accessed on 12 December 2020.

²³¹ IoDSA, The King IV Code (2016) Part 5.1, Principle 1, Recommended Practice 1; IoDSA, The King IV Code (2016) 28.

²³² IoDSA, 'Director Certification Overview' (2019), available at <https://www.iodsa.co.za/page/DCOverview>, accessed on 6 November 2019.

²³³ Ibid.

²³⁴ IoDSA, The King IV Code (2016) Part 5.3, Principle 9, Recommended practices 71 – 74.

²³⁵ PWC 'Governing structures and delegation – A comparison between King IV and King III (2017), 15 available at <https://www.pwc.co.za/en/assets/pdf/king-iv-comparison.pdf>, accessed on 30 May 2020.

²³⁶ IoDSA, The King IV Code (2016) Part 5.3, Principle 7, Recommended Practice 6; IoDSA, The King IV Code (2016) 28; IoDSA, 'Board independence: King IV recommends a balanced approach' (2020), IoDSA available at <https://www.iodsa.co.za/news/486122/Board-independence-King-IV-recommends-a-balanced-approach.htm>, accessed on 12 December 2020.

²³⁷ IoDSA, The King IV Code (2016) 4.

²³⁸ Deloitte, 'King IV Diversity in the Boardroom (2017) 3 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/za_KGIV_BoardDiversity_FA.pdf, accessed on 3 May 2020.

²³⁹ PWC op cit note 235 at 12.

²⁴⁰ Ibid.

The CEO plays a very important role in governance and his/her functions should be clearly defined.²⁴¹ Directors must assess whether the arrangements for delegating leadership to the CEO are both adequate and hold the CEO accountable to the board.²⁴² However, the Code does not define the core functions of the CEO.²⁴³ In general, it recommends that the functions of the CEO include serving as ‘the chief link between management and the governing body’.²⁴⁴ There should be more detail regarding the monitoring of the actions of the CEO and his/her reporting to the board, creating in the process an ethical culture and strategic healthy and dynamic company.²⁴⁵

The functions of the corporate governance professional should be clearly defined in the Code, since the office is key to advising directors on maintaining good corporate governance. While the Code does make provision for the appointment of a corporate governance professional,²⁴⁶ it does not set out their functions,²⁴⁷ such as advising the board on corporate governance principles, risk management frameworks, board committee administration and communication with company stakeholders.²⁴⁸

(c) *Risk oversight and governance*

Every company faces the possibility of unforeseen circumstances that might affect its operations and reputation, requiring contingency plans, known as risk management.²⁴⁹ Konar affirms the need for boards to treat risk as integral to its normal operations.²⁵⁰ While current volatile conditions have forced most boards to become risk averse,²⁵¹ this may cause boards to overlook the strategic

²⁴¹ PWC op cit note 235 at 9.

²⁴² IoDSA, The King IV Code (2016) Part 5.3, Principle 10, Recommended Practice 78.

²⁴³ PWC op cit note 235 at 11.

²⁴⁴ IoDSA, The King IV Code (2016) Part 5.3, Principle 10, Recommended Practice 77.

²⁴⁵ PWC op cit note 235 at 11.

²⁴⁶ PWC op cit note 235 at 40.

²⁴⁷ PWC op cit note 235 at 42.

²⁴⁸ Chartered Governance Institute of South Africa, ‘The Governance Professional’, available at https://www.chartsec.co.za/index.php?option=com_content&view=article&id=10&Itemid=15, accessed on 11 November 2019; IoDSA, ‘Company secretaries emerging as governance custodians’ (2018), IoDSA available at <https://www.iodsa.co.za/news/424920/Company-secretaries-emerging-as-governance-custodians.htm>, accessed on 12 December 2020.

²⁴⁹ Y Smit op cit note 37 at 56; IoDSA, ‘Key principles of risk oversight’ (2019), IoDSA available at <https://www.iodsa.co.za/news/452777/Key-principles-of-risk-oversight.htm>, accessed on 16 December 2020.

²⁵⁰ B Knopjes & L Konar ‘Changes in King IV: The impact on companies’ approach to risk’ (2017) available at <https://www.isometrix.com/blog/changes-in-king-iv-the-impact-on-companies-approach-to-risk>, accessed on 4 June 2019.

²⁵¹ IoDSA op cit note 32 at 5.

opportunities that may arise.²⁵² The Code deals with this by introducing the concept of risk and opportunity governance,²⁵³ which recommends directors to focus on the opportunity side of risk, by taking strategic risks for the growth and development of the company.²⁵⁴ This reinforces the need to enforce the Code, because directors need to demonstrate effective leadership by understanding the effects of uncertainty on their strategic objectives and capitalising on any opportunities.²⁵⁵

The Code recommends that directors be responsible for risk oversight and should approve risk policy²⁵⁶ in a process clearly linked to the business strategy.²⁵⁷ This would allow directors to identify opportunities in uncertainty and implement strategy.²⁵⁸ The critical need for directors to evaluate and challenge the company's risks, especially those that are not anticipated,²⁵⁹ further underlines the need for the enforcement of the Code.

Directors can delegate the oversight of risk governance to a board committee.²⁶⁰ However, the Code does not provide details on the functions of the risk committee, and such should be included.²⁶¹ These functions could include creating the risk policy, determining the company's risk tolerance, regular risk assessments and evaluating risk governance.²⁶² Further, the Code does not provide details for limiting the power of the committee; it should be limited to the power delegated

²⁵² Ibid 5; IoDSA, 'Key principles of risk oversight' (2019), IoDSA available at <https://www.iodsa.co.za/news/452777/Key-principles-of-risk-oversight.htm>, accessed on 16 December 2020.

²⁵³ IoDSA, The King IV Code (2016) Part 5.4, Principle 11, Recommended Practice 1; IoDSA, The King IV Code (2016) 30.

²⁵⁴ IoDSA op cit note 32 at 5.

²⁵⁵ IoDSA, The King IV Code (2016) 30.

²⁵⁶ IoDSA, The King IV Code (2016) Part 5.4, Principle 11, Recommended Practice 6; IoDSA, 'General Guidance Note, Summary of King IV Disclosure Requirements' (2016), 4 available at https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/49D62EF3-F749-403C-BE47-73C50F27F30F/General_Guidance_Note_on_Summary_of_King_IV_Disclosure_Requirements.pdf, accessed on 30 May 2020.

²⁵⁷ IoDSA, The King IV Code (2016) Part 5.4, Principle 11, Recommended Practice 4 – 6.

²⁵⁸ IoDSA, 'General Guidance Note, Summary of King IV Disclosure Requirements' (2016), 4 available at https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/49D62EF3-F749-403C-BE47-73C50F27F30F/General_Guidance_Note_on_Summary_of_King_IV_Disclosure_Requirements.pdf, accessed on 30 May 2020.

²⁵⁹ Ibid 4 – 5.

²⁶⁰ IoDSA, The King IV Code (2016) Part 5.3, Principle 8, Recommended Practice 62.

²⁶¹ IoDSA, The King IV Code (2016) Part 5.3, Principle 8, Recommended Practice 62; PWC op cit note 235 at 35.

²⁶² P Natesan & P Du Plessis 'Opinion: Risk committees' crucial oversight role' (2019), available at <https://www.iol.co.za/business-report/opinion/opinion-risk-committees-crucial-oversight-role-30108212>, accessed on 16 October 2019; Deloitte 'Risk Committee Resource Guide' (2014) 24 – 29 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/ZA_RiskCommitteeResourceGuideOnline2014_22052014.pdf, accessed on 11 November 2019.

by the board.²⁶³ The Code fails to provide details on the committee's right of access to company information and also fails to provide how much information can be accessed.²⁶⁴ Further, the Code affords the board responsibility for conducting an independent evaluation of the committee's performance.²⁶⁵ While the Code provides adequate guidance for risk oversight, the functions of the risk committee need to be expressly set out, since the committee plays a crucial role in the management of risk.²⁶⁶

(d) *Adequate information and technology governance*

Cyber security is becoming a formidable corporate governance challenge for boards of directors.²⁶⁷ In 2016, the annual global cost of cybercrime was \$575 billion,²⁶⁸ with the main targets being social networks, android devices and the cloud storage.²⁶⁹ Daily business operations therefore require proper protection, with emphasis on information storage and sharing.²⁷⁰ Moyo asserts that company boards are responsible for information technology governance.²⁷¹ The Code provides that directors must assume such responsibility and create policy to secure the information technology systems,²⁷² cognisant of the revolution in information technology that is transforming products and services²⁷³ and the dawn of the 4th industrial revolution with its attendant potential

²⁶³ IoDSA, 'Guidance for Boards, Remuneration Committee Terms of Reference' (2019), 7 – 8 available at [https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/49D62EF3-F749-403C-BE47-73C50F27F30F/Guidance for Boards - Remuneration Committee T.pdf](https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/49D62EF3-F749-403C-BE47-73C50F27F30F/Guidance%20for%20Boards%20-%20Remuneration%20Committee%20T.pdf), accessed on 7 February 2020.

²⁶⁴ Ibid 8.

²⁶⁵ Ibid.

²⁶⁶ P Natesan & P Du Plessis op cit note 262; Deloitte 'Risk Committee Resource Guide' (2014) 24 – 29 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/ZA_RiskCommitteeResourceGuideOnline2014_22052014.pdf, accessed on 11 November 2019.

²⁶⁷ IoDSA op cit note 32 at 3.

²⁶⁸ Ibid.

²⁶⁹ Ibid.

²⁷⁰ Ibid.

²⁷¹ A Moyo 'King IV places IT governance on the board table' (2017), available at <https://www.itweb.co.za/content/z5yONP7EZWMXWrba>, accessed on 30 May 2020; Deloitte 'King IV: Bolder Than Ever' (2016) 13 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/ZA_King_IV.pdf, accessed on 11 May 2018.

²⁷² IoDSA, The King IV Code (2016) Part 5.4, Principle 12, Recommended Practice 10 – 13; IoDSA, The King IV Code (2016) 30; IoDSA, 'General Guidance Note, Summary of King IV Disclosure Requirements' (2016), 5 available at [https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/49D62EF3-F749-403C-BE47-73C50F27F30F/General Guidance Note on Summary of King IV Disclosure Requirements.pdf](https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/49D62EF3-F749-403C-BE47-73C50F27F30F/General%20Guidance%20Note%20on%20Summary%20of%20King%20IV%20Disclosure%20Requirements.pdf), accessed on 30 May 2020.

²⁷³ IoDSA, The King IV Code (2016) 30.

for disruption and opportunities.²⁷⁴ These risks and opportunities in an era of globalisation demand that the Code be enforced.

While South Africa has strict data privacy laws with stiff penalties,²⁷⁵ data remains a key collateral risk for directors, since hackers often gain access to systems to expropriate corporate data on the dark web.²⁷⁶ An example was when financial services giant Liberty had client information breached by hackers who attempted to extort ‘millions’ from Liberty against release of the personal information of their clients.²⁷⁷ The hackers gained access to the data unnoticed²⁷⁸ until the hackers themselves informed Liberty.²⁷⁹ Liberty suffered major reputational damage as a result.²⁸⁰ The Code adequately addresses such a challenge by recommending that directors exercise continuous oversight of company information and to ensure that there is a framework to protect confidentiality, integrity and availability of information.²⁸¹ In particular, such oversight should ensure the protection of personal information by continuous monitoring.²⁸² This scenario underlines further the need to enforce the Code, since it recommends that directors are responsible for ensuring the protection of data.²⁸³

Directors must ensure they identify, keep up to date with and understand the types of technology needed by the company.²⁸⁴ Moodley asserts that directors must stay up to date with growing trends in technology because of the pervasiveness of technology.²⁸⁵ Damianides adds that technology creates business value by giving a company a competitive advantage over others.²⁸⁶

²⁷⁴ Ibid.

²⁷⁵ The Protection of Personal Information Act 4 of 2013; IoDSA, ‘City of Johannesburg ransomware attack a wake-up call for boards’ (2019), available at <https://www.iodsa.co.za/news/475603/City-of-Johannesburg-ransomware-attack-a-wake-up-call-for-boards-says-IoDSA.htm>, accessed on 6 November 2019.

²⁷⁶ IoDSA, ‘City of Johannesburg ransomware attack a wake-up call for boards’ (2019), available at <https://www.iodsa.co.za/news/475603/City-of-Johannesburg-ransomware-attack-a-wake-up-call-for-boards-says-IoDSA.htm>, accessed on 6 November 2019.

²⁷⁷ ITOO, ‘Liberty cyber breach: it could happen to you’ (2018) available at <https://www.itweb.co.za/content/KA3Ww7dl3mO7rydZ>, accessed on 23 August 2019.

²⁷⁸ Ibid.

²⁷⁹ Ibid.

²⁸⁰ Ibid.

²⁸¹ IoDSA, The King IV Code (2016) Part 5.4, Principle 12, Recommended Practice 14.

²⁸² Ibid.

²⁸³ IoDSA, The King IV Code (2016) Part 5.4, Principle 12, Recommended Practice 13.

²⁸⁴ IoDSA, ‘The King IV Report on Corporate Governance,’ (2016) 30.

²⁸⁵ IoDSA, ‘City of Johannesburg ransomware attack a wake-up call for boards’ (2019), available at <https://www.iodsa.co.za/news/475603/City-of-Johannesburg-ransomware-attack-a-wake-up-call-for-boards-says-IoDSA.htm>, accessed on 6 November 2019.

²⁸⁶ Damianides op cit note 36 at 77–78.

On the contrary, Botha argues that sudden changes in technology, along with growing customer expectations were associated with a lot of complexity and risk.²⁸⁷ This suggests that directors should seek guidance from experts and take a holistic view of the technological environment and its impact on operations and sensitive data.²⁸⁸ The Code recognises that the governance of information and technology are separate issues.²⁸⁹ In addition, directors must also ensure that information technology service providers are compliant with proper governance procedures,²⁹⁰ and that an intellectual property audit is conducted for the protection of intellectual property.²⁹¹ This also demands enforcement of the Code, since it includes practices to help the boards overcome the challenges of information and technology governance.²⁹²

(e) *Compliance monitoring*

Companies find it difficult to comply with corporate governance provisions because the cost of compliance is high;²⁹³ and the burden of over-regulation, results in tick-box compliance,²⁹⁴ essentially mindless compliance.²⁹⁵ The Code therefore recommends that directors create a compliance policy binding on stakeholders at every level of the company,²⁹⁶ combined with thoughtful implementation and reporting,²⁹⁷ ensuring that compliance moulds and strengthens the company in its strategic thinking.²⁹⁸ Such an approach further underlines the necessity to enforce the Code.²⁹⁹

²⁸⁷ E Botha *Information Technology Governance Frameworks in Higher Education in South Africa: A Paradigm Shift* (unpublished masters thesis, North West University, 2012) 1.

²⁸⁸ IoDSA, 'City of Johannesburg ransomware attack a wake-up call for boards' (2019), available at <https://www.iodsa.co.za/news/475603/City-of-Johannesburg-ransomware-attack-a-wake-up-call-for-boards-says-IoDSA.htm>, accessed on 6 November 2019.

²⁸⁹ IoDSA, 'The King IV Report on Corporate Governance,' (2016) 30.

²⁹⁰ S Kula 'Differences between King III and King IV' (2019) available at <https://www.michalsons.com/blog/difference-king-code-iii-iv-3-4/27132>, accessed on 30 May 2020.

²⁹¹ Ibid; Koornhof, PGJ *Bow to the King (IV)? A new era for IT governance in South Africa* (conference paper, Aston university, 2016) 170 – 17.

²⁹² IoDSA, 'The King IV Report on Corporate Governance,' (2016) 30; Koornhof, PGJ *Bow to the King (IV)? A new era for IT governance in South Africa* (conference paper, Aston university, 2016) 170 – 17.

²⁹³ Parry op cit note 3 at 42.

²⁹⁴ IoDSA op cit note 32 at 6.

²⁹⁵ Ibid.

²⁹⁶ IoDSA, The King IV Code (2016) Part 5.4, Principle 13, Recommended Practice 18 – 20; Kula op cit note 290.

²⁹⁷ IoDSA op cit note 32 at 6.

²⁹⁸ Steyn op cit note 177.

²⁹⁹ Ibid.

There is a growing demand for highly skilled professionals to manage compliance with the Code at a time when cost pressures are rising, causing reluctance to recruit external compliance professionals.³⁰⁰ Some companies deploy internal employees to compliance functions³⁰¹ in line with the Code's encouragement for directors to delegate the management of compliance,³⁰² subject to receiving independent assurances on the effectiveness of such compliance management.³⁰³ However, the cost of implementing the Code remains high, because companies need the assistance and advice of expert consultants.³⁰⁴ Therefore, directors should ensure that those tasked with the compliance function are adequately trained and possess the proper skills.³⁰⁵ However, the Code lacks detail on the role of those tasked with the compliance function, providing only a general guideline.³⁰⁶ Effective compliance requires regular assessments and monitoring, reporting compliance to regulators and maintaining a level of independence from management control.³⁰⁷ Therefore, the Code does not provide adequate guidance to those tasked with the compliance function.

Companies tend to create strong mechanisms on paper, but very weak controls in reality.³⁰⁸ Chakanika points out that the world is trying to hastily implement corporate governance structures in order to keep pace with international markets.³⁰⁹ However, there has been a failure to enforce rules, regulations and laws consistently.³¹⁰ Okpara states that this is contrary to the OECD principles, which assume that countries have an efficient regulatory system and its

³⁰⁰ Deloitte 'Targeting compliance: The changing role of compliance in the Financial Services Industry' (2016) 12 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/risk/ZA_Compliance_final_No_Crops_RA_190816.pdf, accessed on 31 October 2019.

³⁰¹ Ibid.

³⁰² IoDSA, The King IV Code (2016) Part 5.4, Principle 13, Recommended Practice 20.

³⁰³ Ibid.

³⁰⁴ D Anyango op cit note 181 at 78.

³⁰⁵ Deloitte 'Targeting compliance: The changing role of compliance in the Financial Services Industry' (2016) 12 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/risk/ZA_Compliance_final_No_Crops_RA_190816.pdf, accessed on 31 October 2019.

³⁰⁶ IoDSA, The King IV Code (2016) Part 5.4, Principle 13, Recommended Practice 20 – 23.

³⁰⁷ Deloitte 'Targeting compliance: The changing role of compliance in the Financial Services Industry' (2016) 12, available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/risk/ZA_Compliance_final_No_Crops_RA_190816.pdf, accessed on 31 October 2019.

³⁰⁸ Chakanika op cit note 77 at 45.

³⁰⁹ Chakanika op cit note 77 at 49.

³¹⁰ JO Okpara 'Corporate Governance in a Developing Economy: Barriers, Issues and Implications for Firms' (2011) 11(2) *Corporate Governance* 184 – 199.

courts have the resources and means to enforce it.³¹¹ For this reason, directors must ensure that regulation is on their agenda and management should report to the board on regulatory changes and their plans for response.³¹² Directors should engage with regulators, legislators, and industry associations over proposed rules and their impact. Further, directors must alert regulatory authorities to any unintended consequences that stem from a proposed rule change.³¹³ The Code adequately addresses this challenge, by recommending that director oversight results in continuous monitoring of the regulatory universe along with the appropriate response to any changes.³¹⁴ Further, the Code bolsters transparency by recommending that any regulatory penalties, sanctions or fines imposed on the company should be disclosed.³¹⁵

(f) *Adequate remuneration governance*

Remuneration of directors has become a popular topic in the corporate governance space.³¹⁶ In 2014, South Africa was ranked fourth by the Human Science Research Council as the most unequal society in the world, based on income, illustrating the inequality of income at different levels of employment.³¹⁷ Constant tension exists between shareholder challenges on the computation of remuneration levels of directors and the directors' appeal for privacy in their financial affairs.³¹⁸ The remuneration approved by boards of directors is also a matter of great concern in South Africa. The Code addresses this challenge, by recommending that boards be responsible for remuneration governance by approving policy to ensure fair, responsible, and transparent remuneration.³¹⁹ Therefore, the Code recommends that there should be fair remuneration of executive management.³²⁰

³¹¹ Ibid.

³¹² Deloitte 'Directors' Alert Through the eyes of the board: Key governance issues for 2015' (2015) 14 available at <https://www2.deloitte.com/content/dam/Deloitte/global/Documents/Risk/gx-gccg-directors-alert-2015.pdf>, accessed on 30 May 2020.

³¹³ Ibid.

³¹⁴ IoDSA, The King IV Code (2016) Part 5.4, Principle 13, Recommended Practice 21.

³¹⁵ IoDSA, The King IV Code (2016) Part 5.4, Principle 13, Recommended Practice 24.

³¹⁶ Deloitte 'Disclosure of remuneration – a hot topic' (2014) 2 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/ZA_DisclosureOfRemunerationAHotTopic_04042014.pdf, accessed on 31 May 2020.

³¹⁷ IoDSA op cit note 32 at 5.

³¹⁸ Deloitte 'Disclosure of remuneration – a hot topic' (2014) 2 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/ZA_DisclosureOfRemunerationAHotTopic_04042014.pdf, accessed on 31 May 2020.

³¹⁹ IoDSA, The King IV Code (2016) Part 5.4, Principle 14, Recommended Practice 26 – 27.

³²⁰ IoDSA, The King IV Code (2016) Part 5.4, Principle 14, Recommended Practice 29 and 34.

It is necessary to enforce the Code to prevent over-remuneration of directors and to ensure that remuneration creates value in a sustainable manner.³²¹ The Code recommends that the board establishes a remuneration committee,³²² composed of competent and skilled members to manage remuneration policies,³²³ including preparation of a remuneration report.³²⁴ Directors and the remuneration committee must agree on the information to be disclosed in the remuneration report, which includes the remuneration for each member of the executive.³²⁵

However, the Code does not provide detailed instructions for the remuneration committee, such as measurement of the performance of the CEO.³²⁶ It also fails to provide details regarding its access to independent professional advice.³²⁷ While the Code adequately addresses remuneration governance, it fails to specify the functions of the remuneration committee.³²⁸

(g) *Adequate stakeholder communication*

Most directors still perceive the company as an organism and not a social system interdependent on the support of society.³²⁹ The Code assumes an ‘interdependent relationship’ between the company and its stakeholders.³³⁰ While directors should ensure there is continuous oversight of

³²¹ Deloitte ‘King IV Remuneration Governance’ (2017) 4 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/za_Deloitte_KingIV_Remuneration_Governance_01032017.pdf, accessed on 3 May 2020

³²² IoDSA, The King IV Code (2016) Part 5.3, Principle 10, Recommended Practice 65.

³²³ IoDSA, The King IV Code (2016) Part 5.3, Principle 10, Recommended Practice 66 and 79; IoDSA, The King IV Code (2016) Part 5.3, Principle 7, Recommended Practice 36.

³²⁴ IoDSA, ‘General Guidance Note, Summary of King IV Disclosure Requirements’ (2016), 6 available at https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/49D62EF3-F749-403C-BE47-73C50F27F30F/General_Guidance_Note_on_Summary_of_King_IV_Disclosure_Requirements.pdf, accessed on 30 May 2020.

³²⁵ IoDSA, The King IV Code (2016) Part 5.4, Principle 14, Recommended Practice 35; IoDSA, ‘General Guidance Note, Summary of King IV Disclosure Requirements’ (2016), 6 available at https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/49D62EF3-F749-403C-BE47-73C50F27F30F/General_Guidance_Note_on_Summary_of_King_IV_Disclosure_Requirements.pdf, accessed on 30 May 2020.

³²⁶ IoDSA, ‘Guidance for Boards, Remuneration Committee Terms of Reference’ (2019), 7 available at https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/49D62EF3-F749-403C-BE47-73C50F27F30F/Guidance_for_Boards_-_Remuneration_Committee_T.pdf, accessed on 7 February 2020.

³²⁷ Ibid 11.

³²⁸ P Natesan & P Du Plessis op cit note 262; Deloitte ‘Risk Committee Resource Guide’ (2014) 24 – 29 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/ZA_RiskCommitteeResourceGuideOnline2014_22052014.pdf, accessed on 11 November 2019.

³²⁹ JB Leuner *A Change in Focus to Stakeholder Engagement and Reputation Management Aligned to King III recommendations* (unpublished masters thesis, University of Pretoria, 2010) 26; SM Bonini, LT Mendonca & JM Oppenheim ‘When Social issues become strategic’ 2006 *The McKinsey Quarterly* 31.

³³⁰ IoDSA, The King IV Code (2016) 25; PWC ‘King IV Code brings the role of ethical and effective leadership to the fore’, available at <https://www.pwc.co.za/en/press-room/king-four-draft.html>, accessed on 12 December 2020.

stakeholder relationships, they should also be mindful in particular of how the company's activities might affect these stakeholders.³³¹ Further, directors must manage stakeholder risk and stakeholder communication.³³² The Code addresses this challenge, by encouraging a stakeholder-inclusive approach to corporate governance, where directors must provide disclosure of the performance of the board of directors, the board committees, the CEO, risk management, technology and information, compliance and other stakeholder relationships.³³³

Many companies curb their business by conducting components of the business in separate 'silos'. The Code promotes a move from 'silo reporting' to 'integrated reporting',³³⁴ providing a holistic view of the company's efforts to preserve long-term sustainability without sacrificing short-term performance.³³⁵ For this reason, information on the company's strategy, risk and governance procedures must be communicated to stakeholders by virtue of an integrated report.³³⁶ It is suggested that directors refer to the International Integrated Reporting Council (IIRC) requirements to improve the overall quality of integrated reporting.³³⁷ However, integrated reporting is costly, because it creates a need to adjust management systems³³⁸ for the gathering, determining and measuring of data.³³⁹ Consequently, smaller companies, which often lack adequate reporting systems, may not have the financial capital to create formal governance structures to enable compliance.³⁴⁰ However and in general, the Code addresses the challenge of stakeholder communication by encouraging integrated thinking through integrated reporting which ensures adequate stakeholder communication, value creation and performance (Figure 8).³⁴¹ Figure 8 illustrates the process of integrated thinking which influences how the organisation will react and respond to external risks and opportunities and the needs of stakeholders.

³³¹ IoDSA, The King IV Code (2016) Part 5.5, Principle 16, Recommended Practice 4.

³³² IoDSA, The King IV Code (2016) Part 5.5, Principle 16, Recommended Practice 4.

³³³ F Myburgh & A De Costa op cit note 216.

³³⁴ SAICA 'Integrated thinking – an exploratory survey' (2014), 20 – 21 available at <https://www.saica.co.za/Portals/0/Technical/Sustainability/SAICAIntegratedThinkingLandscape.pdf>, accessed on 30 May 2020.

³³⁵ Deloitte 'The governance of reporting and the reporting of governance' (2014) 2 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/ZA_TheGovernanceOfReportingAndTheReportingOfGovernance_04042014.pdf, accessed on 30 May 2020.

³³⁶ Ibid.

³³⁷ Grant Thornton South Africa op cit note 179 at 4.

³³⁸ D Anyango op cit note 181 at 42.

³³⁹ Ibid.

³⁴⁰ Ibid.

³⁴¹ IoDSA, The King IV Code (2016) Part 5.2, Principle 5, Recommended Practice 12.



Figure 8 – The process of integrated thinking³⁴²

III. CONCLUSION

The Code provides a compass for directors in relation to corporate governance by providing direction and practical guidance to overcome corporate governance challenges.³⁴³ The Code governs all the critical sectors of a company; since it influences the manner a company normally conducts business and provides guidance to most of the non-negotiable governance areas of companies.³⁴⁴ However, it lacks guidance on the core functions performed by the CEO,³⁴⁵ the corporate governance professional, the risk committee and compliance professionals all of whom serve important roles in corporate governance.³⁴⁶ Further, it lacks adequate detail on ethics management.³⁴⁷

South Africa will not attract investor funds if it does not implement consistent and reliable corporate governance rules.³⁴⁸ Since directors are accountable for governance standards,³⁴⁹ ignorance is no excuse for non-compliance,³⁵⁰ especially as directors are privy to all issues within the

³⁴² SAICA op cit note 334 at 8.

³⁴³ Wiese op cit note 79 at 22.

³⁴⁴ P Natesan & P Du Plessis op cit note 50.

³⁴⁵ PWC op cit note 235 at 11.

³⁴⁶ IoDSA, The King IV Code (2016) 29.

³⁴⁷ The Ethics Institute op cit note 202.

³⁴⁸ Harris op cit note 3 at 23.

³⁴⁹ Ibid.

³⁵⁰ Steyn op cit note 177.

company.³⁵¹ The ‘apply and explain’ disclosure regime of the Code is a method of enforcement because it forces directors to disclose how they manage the company and move it closer to achieving the goals enshrined in its 17 principles.³⁵² This offers a good reason for the enforcement of the Code, as a proper application of the Code could assist directors to reap the benefits of good corporate governance.

The Act, the listing requirements of the JSE and the Code itself spell out the scope of liability of a director to a company. There are many instances where the Code has become mandatory through usage, such as the business judgement rule, the listing requirements of the JSE and the Act.

³⁵¹ Ibid.

³⁵² P Natesan & P Du Plessis op cit note 50.

CHAPTER 4

MECHANISMS FOR ENFORCEMENT OF THE KING IV CODE ON THE BOARD OF DIRECTORS

I. INTRODUCTION

The focus of this study is to analyse the role of the board of directors in terms of the Code. Directors often challenge the enforceability of the Code on the ground that compliance is voluntary, suggesting that the Code does not create any legally binding obligations and is simply a guideline.³⁵³ The objective of this chapter is to indicate how compliance with the Code can be enforced on boards of directors. Although the Code is voluntary, evidence indicates that its practice has become mandatory since JSE-listed companies are obliged to comply with the Code through its listing requirements and the business judgement rule, which is grounded in the Act. Further, it is necessary to analyse the synergy between the Act and the Code since elements of the Code and previous King Codes have been enacted in law and therefore rendered enforceable.

II. ENFORCING THE KING IV CODE THROUGH THE BUSINESS JUDGEMENT RULE

As custodians of corporate governance, directors must be able to make decisions that steer the company in a proper direction. However, a director may be held liable for an unsound decision, unless it can be proved that he/she acted within the scope of the business judgement rule.³⁵⁴

(a) The business judgement rule protects directors from liability to the company

According to Ncube, the business judgement rule is contained in section 76(4)(a) of the Act in terms of which a director must prove he/she exercised good business judgement by taking the following into consideration:

³⁵³ Visser op cit note 57 at 1.

³⁵⁴ L Muswaka 'Directors' Duties and the Business Judgment Rule in South African Company Law: An Analysis' (2013) 3(7) *International Journal of Humanities & Social Science* 91.

1. 'The director must prove he/she has taken reasonably diligent steps to become informed about the matter.'³⁵⁵
2. 'He/She had no material personal financial interest in the matter and did not have a reasonable basis to know that any other related person had a personal financial interest in the subject matter.'³⁵⁶
3. 'Where the director has made a decision or supported a decision of a committee and had a rational basis for believing that the decision was in the best interests of the company.'³⁵⁷

Upon proof of the above, the business judgement rule will protect the director from liability.³⁵⁸

According to Section 76 (3) of the Act, directors have a fiduciary duty to act in good faith and for proper purpose; in the best interests of the company and with the degree of care, skill and diligence reasonably expected of a similar director acting in the position of that director.³⁵⁹ In the case of *Bristol and West Building Society v Mothew* Millett LJ held that the distinguishing obligation of a fiduciary is the obligation of loyalty. The principal is entitled to single minded loyalty from a fiduciary. A fiduciary must act in good faith, not make a profit out of his trust, not place himself in a conflict of interest situation and may not act for his own benefit without the informed consent of his principal.³⁶⁰ In *Howard v Herrigel* the court held as that even at common law, once a person accepts an appointment as director, he becomes fiduciary in relation to the company and is obliged to display the utmost good faith towards the company and in his dealings on its behalf.³⁶¹ Further, the fiduciary duty extends even after a director's tenure has ended.³⁶² If found that a director failed in their statutory obligation of duty of care then the business judgement rule will apply. It serves as a defence for directors from liability for actions taken bona fide and in the best interests of the company.³⁶³

³⁵⁵ S 76(4)(a)(i) of the Companies Act 71 of 2008; CB Ncube 'Transparency and accountability under the new company law' (2010) *Acta Juridica* 69.

³⁵⁶ S 76(4)(a)(ii) (aa) of the Companies Act 71 of 2008; CB Ncube op cit note 355 at 69.

³⁵⁷ S 76(4)(a)(iii) of the Companies Act 71 of 2008; CB Ncube op cit note 355 at 69.

³⁵⁸ S 76(4) of the Companies Act 71 of 2008; Leach op cit 27 at 20 – 21.

³⁵⁹ Naidoo R, *An essential Guide for South African Companies*, 3rd ed, 2016, 203.; Visser op cit note 57 at 3.

³⁶⁰ 1996 4 ALL ER 698(CA), 711.

³⁶¹ 1991 2 SA 679 (A) 678

³⁶² *Atlas Organic Fertilizers (Pty) Ltd v Pikkewyn Ghwano (Pty) Ltd* 1981 2 SA 173 (T) 198d-h; *Da Silva v CH Chemicals (Pty) Ltd* 2008 6 SA 620 (SCA) 628F-G.

³⁶³ Institute of directors Southern Africa, *The Business Judgement Rule*, 2013, 6.

The business judgement rule is supported by the reliance rule in section 76(4)(b) and (5) of the Act, in terms of which a director can rely on information provided to him/her in exercising his/her functions as a director.³⁶⁴ 'Reliance' depends on the director reasonably believing that the advisers who provided the information were adequately informed or qualified.³⁶⁵ According to Ncube, directors are entitled to rely on any information, including recommendations and reports provided by professionals and employees.³⁶⁶ However, even in large companies, a director cannot be expected to be perpetually involved in all aspects of management³⁶⁷ and should delegate, but not abdicate their responsibility.³⁶⁸

Since business is about taking risk for rewards, directors must exercise proper judgement to ensure the best decisions are made. However, when an incorrect decision is made there must be a proper assessment of the appropriateness of the process leading to the decision.³⁶⁹ Naidoo asserts that directors can defend themselves from liability even if they did not comply with their statutory/fiduciary duties in the Act.³⁷⁰ However, the business judgement rule is not an impenetrable fortress for directors; they may still be liable for a breach of their statutory/fiduciary duties by acting with intentional dishonesty or irrationality.³⁷¹ Therefore, the business judgement rule guides directors to make informed decisions in the performance of all his/her duties.³⁷²

(b) *Applying the King IV Code assists directors in exercising good judgement*

The Code expressly acknowledges that the business judgement rule assists directors to exercise good business judgement, as follows:³⁷³

³⁶⁴ Cliffe Dekker Hofmeyr 'Corporate Governance a Guide for Directors' (2019) 9 available at <https://www.cliffedekkerhofmeyr.com/export/sites/cdh/en/sectors/downloads/Corporate-governance-A-directors-guide.pdf>, accessed on 20 November 2019.

³⁶⁵ Ibid.

³⁶⁶ S 76(4)(b) and s 76(5) of the Companies Act 71 of 2008; CB Ncube op cit note 355 at 69.

³⁶⁷ Cliffe Dekker Hofmeyr op cit note 364 at 9.

³⁶⁸ Ibid.

³⁶⁹ IoDSA, 'The Business Judgement Rule,' (2013), 3 available at https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/05E93ACB-10BE-4507-9601-307A66F34BD8/IoD_Business_JudgementEmail.pdf, accessed on 18 October 2018.

³⁷⁰ Naidoo op cit note 33 at 212.

³⁷¹ S 76(3)(b) - (c) of the Companies Act 71 of 2008; L Muswaka 'Shielding Directors against Liability Imputations: The Business Judgment Rule and Good Corporate Governance' (2013) 27 (1) *Speculum Juris* 27.

³⁷² IoDSA, 'The Business Judgement Rule,' (2013), 3 available at https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/05E93ACB-10BE-4507-9601-307A66F34BD8/IoD_Business_JudgementEmail.pdf, accessed on 18 October 2018.

³⁷³ IoDSA, 'The King IV Code on Corporate Governance', 2016, 35.

‘The more widely certain recommended practices in codes of governance are adopted, the more likely it is that a court would regard conduct that conforms to these practices as meeting the required standard of care For directors of companies, adopting good corporate governance practices will be especially important if they were to rely on the protection afforded by the business judgement rule as provided for in the Companies Act in the course of litigation. In the absence of robust and sound governance structures and processes, it will be difficult, if not impossible, for a director to show that reasonably diligent steps have been taken to become informed; that material financial interests were absent or dealt with appropriately; and that there was a rational basis for believing – and that the director did believe – that a decision was in the best interests of the company.’³⁷⁴

The first principle of the Code asserts moral duties that reflect the requirements of the business judgement rule in the Act. Adherence to these moral duties will enable directors to exercise good business judgement in terms of the rule. According to the Code, directors should demonstrate the following characteristics in their conduct.³⁷⁵

(i) *Integrity*

A director who fails to act in the best interest of the company or acts with a conflict of interest will not receive protection through the business judgement rule.³⁷⁶ The Code provides that directors should act in good faith and avoid a conflict of interest. The business judgement rule is embedded in the Code;³⁷⁷ directors must act ethically and ‘set the tone for creating an ethical culture’.³⁷⁸

(ii) *Competence*

A defence that the director lacked the knowledge or skills to perform the function undertaken will not avail the director.³⁷⁹ In the case of *Fisheries Development Corp of SA Ltd v Jorgensen*, it was held that directors cannot blindly rely on information presented by professionals or other officers of the company. The court held that a director need not exhibit a greater degree of skill than may reasonably be expected from a person of his/her knowledge and experience and will not be held liable for mere errors of judgement. Further, the court held that a director could rely on the

³⁷⁴ Ibid.

³⁷⁵ IoDSA, The King IV Code (2016) Part 5.1, Principle 1, Recommended Practice 1.

³⁷⁶ Muswaka op cit note 371 at 36 – 37.

³⁷⁷ Ibid.

³⁷⁸ IoDSA, The King IV Code (2016) Part 5.1, Principle 1, Recommended Practice 1.

³⁷⁹ Muswaka op cit note 371 at 37 – 38.

guidance of officials or experts in the performance of his/her duties.³⁸⁰ However, if a director relied on expert advice in good faith to make a decision not in the best interests of the company, he/she may escape personal liability by virtue of the reliance theory.³⁸¹ The Code expressly recommends that directors act with ‘due care, skill and diligence, and take reasonably diligent steps to become informed before a decision is made’.³⁸² In addition, directors must practise continuous professional development of their skills to keep up to date with company affairs, laws and codes applicable to the company.³⁸³ Further, directors must keep a record of expert advice received.³⁸⁴

(iii) Responsibility

A director who ignores or avoids responsibility may be liable for negligence.³⁸⁵ According to the Code, directors should assume collective responsibility for steering the company, approving policy, overseeing management and shoulder accountability for company performance.³⁸⁶ Directors should exhibit courage in their responsibilities and act in the best interests of the company.³⁸⁷ Further, directors should devote enough time to prepare for and attend board meetings.³⁸⁸ In the case of *Fisheries Development Corp of SA Ltd v Jorgensen*, it was held that the non-executive director does not need to attend all meetings, but can attend whenever he/she is reasonably able to do so. Further, a distinction was made between executive directors who are under a contract with the company and owe a higher duty of care, skill and diligence as opposed to a non-executive director whose duties are of an intermittent nature.³⁸⁹ However, recent cases suggest that non-executive directors have more responsibility;³⁹⁰ he/she cannot turn a blind eye to the company affairs and at the same time state that he had exercised good business judgement.³⁹¹

³⁸⁰ *Fisheries Development Corporation of SA Ltd v Jorgensen: Fisheries Development Corp of SA Ltd v AWJ Investments (Pty) Ltd* 1980 (4) SA 156 (W) 165.

³⁸¹ Muswaka op cit note 371 at 37 – 38.

³⁸² IoDSA, The King IV Code (2016) Part 5.1, Principle 1, Recommended Practice 1.

³⁸³ Ibid.

³⁸⁴ Muswaka op cit note 371 at 37.

³⁸⁵ Ibid.

³⁸⁶ IoDSA, The King IV Code (2016) Part 5.1, Principle 1, Recommended Practice 1.

³⁸⁷ Ibid.

³⁸⁸ Ibid.

³⁸⁹ *Fisheries Development Corporation of SA Ltd v Jorgensen: Fisheries Development Corp of SA Ltd v AWJ Investments (Pty) Ltd* 1980 (4) SA 156 (W) 165H; Muswaka op cit note 371 at 37 – 38.

³⁹⁰ Muswaka op cit note 371 at 37 – 38.

³⁹¹ Ibid.

(iv) *Transparency and accountability*

Director accountability has become a subject of international interest.³⁹² The Code asserts that directors should exercise their governance responsibilities in a transparent manner³⁹³ and remain accountable even when responsibility is delegated.³⁹⁴ The Code promotes transparency and accountability³⁹⁵ in the same way as section 7(b)(iii) of the Act encourages ‘transparency and high standards of corporate governance’.³⁹⁶ The Act also sets minimum standards for transparent and accountable³⁹⁷ disclosure of information;³⁹⁸ information should be accurate, complete and readily accessible to the public,³⁹⁹ and any failure to adhere to such standards will attract criminal liability (a fine or imprisonment for up to 10 years).⁴⁰⁰

(v) *Fairness*

Directors should not only consider the interests of shareholders;⁴⁰¹ they need to act in a fair manner and adopt a stakeholder-inclusive approach as mandated by the Code.⁴⁰² Further, directors must not cause harm to the natural environment, society or future generations.⁴⁰³ However, Leach points out that there are factors unique to South Africa,⁴⁰⁴ particularly black economic empowerment partnerships in which racial considerations form part of corporate and social responsibility.⁴⁰⁵ Consequently, Leach argues that the profitability of a company may suffer if directors focus on corporate responsibility policies, which may lead to shareholder discontent and a contravention of section 76(3)(b)-(c) of the Act.⁴⁰⁶ This is balanced with the business judgement rule that

³⁹² Muswaka op cit note 371 at 26.

³⁹³ IoDSA, The King IV Code (2016) Part 5.1, Principle 1, Recommended Practice 1.

³⁹⁴ Ibid.

³⁹⁵ IoDSA, ‘Understanding King IV and what it is intended to achieve’(2018), available at <https://www.iodsa.co.za/news/389613/Understanding-King-IV-and-what-it-is-intended-to-achieve.htm>, accessed on 20 December 2019.

³⁹⁶ Muswaka op cit note 371 at 35.

³⁹⁷ Ch Two, Part C of the Companies Act 71 of 2008; CB Ncube op cit note 355 at 45 – 46.

³⁹⁸ S 216(a) of the Companies Act 71 of 2008; CB Ncube op cit note 355 at 45 – 46.

³⁹⁹ Ibid.

⁴⁰⁰ Ibid.

⁴⁰¹ Leach op cit 27 at 51.

⁴⁰² IoDSA, The King IV Code (2016) Part 5.1, Principle 1, Recommended Practice 1; IoDSA, The King IV Code (2016) Part 5.5, Principle 16; Leach op cit 27 at 51.

⁴⁰³ IoDSA, The King IV Code (2016) Part 5.1, Principle 1, Recommended Practice 1.

⁴⁰⁴ Leach op cit 27 at 51.

⁴⁰⁵ Ibid.

⁴⁰⁶ Ibid.

encourages directors to seize studied operational risks.⁴⁰⁷ Good judgement ensures that they act in a fair manner that recognises the interests of all stakeholders as required by the Code.

(c) *The business judgement rule as a mechanism for enforcing the King IV Code*

When determining if the requirements of the business judgement rule are satisfied, courts will consider whether a director has complied with good corporate governance practices, such as those mentioned in the Code.⁴⁰⁸ Further, according to section 7(b)(iii) of the Act, one of the purposes of the Act is to:

‘Promote the development of the South African economy by encouraging transparency and high standards of corporate governance as appropriate, given the significant role of enterprises within the social and economic life of the nation.’⁴⁰⁹

Section 5(1) of the Act must be interpreted to give effect to the purposes set out in section 7 of the Act.⁴¹⁰ Section 5(1) and section 7(b)(iii) provides a basis for the courts to demand reliance on corporate governance codes (such as the Code), because it demands principles and practices that ‘encourage transparency and high standards of corporate governance’.⁴¹¹

A director who complies with the business judgement rule is not liable to the company, shareholders or stakeholders.⁴¹² Section 76(4) of the Act requires the director to take reasonable steps to become informed and rely on ‘any relevant information, recommendations or reports provided in performance of his/her duties’.⁴¹³ Figure 9 illustrates that directors who comply with the King IV Code also comply with the business judgement rule and the requirements of the Act. Visser asserts that a director must apply the principles and practices of the Code to establish compliance with the Act and the business judgement rule⁴¹⁴ (Figure 9). Further, Visser states that a director who does not obtain relevant information as prescribed by the Code does not comply with his/her statutory/fiduciary obligation and the business judgement rule and, to this extent the

⁴⁰⁷ S7(b)(iii) of the Companies Act 71 of 2008; Muswaka op cit note 371 at 39.

⁴⁰⁸ L Muswaka ‘Directors’ Duties and the Business Judgment Rule in South African Company Law: An Analysis’ (2013) 3(7) *International Journal of Humanities & Social Science* 95; IoDSA, The King IV Code (2016) 35.

⁴⁰⁹ Muswaka op cit note 371 at 35.

⁴¹⁰ Ibid.

⁴¹¹ Ibid.

⁴¹² Naidoo op cit note 33 at 213.

⁴¹³ S 76(4) of the Companies Act 71 of 2008.

⁴¹⁴ Visser op cit note 57 at 4.

Code would be enforceable against the director.⁴¹⁵ Thereby, the Code satisfies the requirement that a director obtains information relevant to exercising good business judgement.

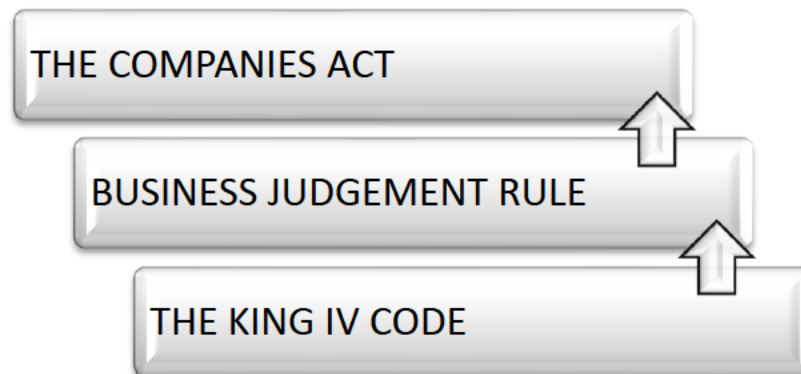


Figure 9 – The enforceability of the King IV Code

III. ENFORCEMENT OF THE KING IV CODE THROUGH THE JSE LISTING REQUIREMENTS

The Code should be enforced through the JSE, which is licensed as an exchange under the Securities Services Act.⁴¹⁶ According to Bhika institutional investors practise governance initiatives that will enhance the market value of client portfolios.⁴¹⁷ Further, investors have adopted a hands-on role in the corporate management and business of their investee companies to safeguard their interests.⁴¹⁸ In addition, increased institutional investor ownership and its influence thereof, has the effect of better monitoring and improving corporate governance.⁴¹⁹ It is evident that all listed companies must comply with the listing requirements of the JSE, which are ‘amended from time to time’.⁴²⁰ Therefore, it is in the interest of listed companies to comply with the listing requirements of the JSE and the Code to attract better investors who will assist in ensuring the company practises good corporate governance.

⁴¹⁵ Ibid.

⁴¹⁶ Act 36 of 2004.

⁴¹⁷ V Bhika op cit note 59 at 7.

⁴¹⁸ V Bhika op cit note 59 at 6 – 7.

⁴¹⁹ V Bhika op cit note 59 at 7.

⁴²⁰ JSE Listing Requirements 1.2 and 3.62; Wiese op cit note 8 at 23; Parry op cit note 3 at 24.

(a) *The JSE makes the King IV Code mandatory*

The definition of ‘King Code’ in the JSE listing requirements refers to ‘the King Code on corporate governance as amended or replaced from time to time’. This suggests that the Code and future evolution of the King Codes continue to impact the governance of companies.⁴²¹ For instance, the listing requirements of the JSE emphatically state that ‘the effect of incorporating certain practices from the King Code in the listing requirements is to make their implementation mandatory’.⁴²² Further, according to Dlamini, although the application of the Code is generally voluntary, listed companies cannot choose to ignore its practices, since the disclosure regime was amended to ‘apply and explain’.⁴²³ Therefore, it is conclusive that all directors of listed companies must comply with the listing requirements, and the King Codes as ‘amended from time to time’.⁴²⁴

(b) *Listing compulsory*

Listed companies must comply with the Code and state in their annual reports how it applied the principles of the Code and the reasons for any non-compliance.⁴²⁵ The listing requirements of the JSE make the Code enforceable in the areas relating to board committees,⁴²⁶ the company secretary⁴²⁷ and for the promotion of gender⁴²⁸ and race diversity⁴²⁹ at board level. In addition, directors of JSE listed companies must create a remuneration policy⁴³⁰ and a policy that ensures a balance of power⁴³¹ at board level. In addition to the Code, listed companies must disclose the compliance of other specific corporate governance requirements in their annual reports.⁴³²

⁴²¹ Wiese op cit note 79 at 23.

⁴²² JSE Listing Requirements 3.84; Dlamini op cit note 50.

⁴²³ Dlamini op cit note 50.

⁴²⁴ JSE Listing Requirements 3.62; Parry op cit note 3 at 24; Wiese op cit note 8 at 23.

⁴²⁵ JSE Listing Requirements 8.63(a)(ii); Parry op cit note 3 at 25.

⁴²⁶ JSE Listing Requirements 3.84 (c).

⁴²⁷ JSE Listing Requirements 3.84 (h).

⁴²⁸ JSE Listing Requirements 3.84 (i).

⁴²⁹ JSE Listing Requirements 3.84 (j).

⁴³⁰ JSE Listing Requirements 3.84 (k).

⁴³¹ JSE Listing Requirements 3.84 (a).

⁴³² JSE Listing Requirements 3.84; Parry op cit note 3 at 24.

IV. ENFORCING THE KING IV CODE THROUGH SPECIFIC PROVISIONS OF THE COMPANIES ACT 71 OF 2008

There are many instances where the provisions of the Act overlap with the Code and many recommendations of the Code that strengthen the provisions of the Act. Directors need to understand how the recommendations of the Code overlap with the Act, because the Act forms part of the South African regulatory framework for corporate governance.⁴³³ Since the Code is to be a best-practice recommendation, it should be looked at holistically to ascertain which sections are in alignment with legislation. While the Code is not mandatory, a ‘hawk eye’ interpretation of the Act actually highlights substantial mechanisms for the enforcement of the recommendations of the Code.⁴³⁴ However, certain corporate governance recommendations of the Code are not covered by the Act and should be enacted in legislation. The Code and the Act overlap as follows:

(a) Ethical leadership and the responsibility of corporate governance

The Code recommends that directors are responsible for corporate governance and must lead ethically and effectively.⁴³⁵ This is reflected in section 66 of the Act which states that ‘the business affairs of the company are under the direction of the board of directors who have the power to appoint a social and ethics committee’.⁴³⁶ In addition, section 72(8) of the Act states that ‘directors are required to make public disclosures on the ethical status of the company’.⁴³⁷ Therefore, the Code is in line with the Act, since directors control the strategic direction of the company and are required to appoint a social and ethics committee to assist with ethical issues and ethical leadership.⁴³⁸

⁴³³ Naidoo op cit note 33 at 42.

⁴³⁴ Visser op cit note 57 at 2.

⁴³⁵ IoDSA, The King IV Code (2016) Part 5.1, Principle 1 – 3; IoDSA, The King IV Code (2016) Part 5.3, Principle 6.

⁴³⁶ S 66 of the Companies Act 71 of 2008.

⁴³⁷ S 72(8) of the Companies Act 71 of 2008; Harris op cit note 3 at 15.

⁴³⁸ IoDSA, The King IV Code (2016) Part 5.3, Principle 8, Recommended practices 68 – 70; Deloitte, ‘King IV: Bolder Than Ever’ (2016) 5 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/ZA_King_IV.pdf, accessed on 11 May 2018.

(b) *Delegation of power to board committees*

The Code reflects section 72(1) of the Act, in regards to the appointment of and delegation of authority to board committees.⁴³⁹ However, this delegation of authority does not absolve the director from his/her own duty as a director.⁴⁴⁰ Therefore, the Code serves to strengthen the provision in the Act by providing more guidance for directors on the structure, composition and responsibilities of such board committees.⁴⁴¹

(c) *Composition of the board of directors*

The Code strengthens the composition of the board of directors by proposing the appointment of independent non-executive directors.⁴⁴² In the case of *Fisheries Development Corporation of SA Ltd v Jorgensen and Fisheries Development Corporation of SA Ltd v AWJ Investment (Pty) Ltd*⁴⁴³ the court held that non-executive directors were not obliged to provide continuous attention to company affairs; their presence was to ensure independence and objectivity⁴⁴⁴ in terms of global best practice, by avoiding a situation where a single person has unfettered control over the entity. In this way the Code's recommendations for the composition of the board of directors strengthens the provisions of the Act by providing a balance of authority.⁴⁴⁵

(d) *Governance of information and technology*

While the Act incorporates provisions that compel the use of information technology, it lacks in governance provisions.⁴⁴⁶ Section 6(10) of the Act states that 'it is sufficient for a notice to be electronically transmitted to another person as long as it is printed within a reasonable time'.⁴⁴⁷ Despite recognising information technology, the Act needs to be amended to set out issues of

⁴³⁹ S 72 of the Companies Act 71 of 2008; WJL Calkoen *The Corporate Governance Review* (2011) 277; Moore Stephens 'Companies Act Guide' (2018), available at <https://southafrica.moorestephens.com/MediaLibsAndFiles/media/southafricaweb.moorestephens.com/Guides-2018/MS-Companies-Act-Guide.pdf>, accessed on 30 May 2020.

⁴⁴⁰ Calkoen op cit note 439 at 277.

⁴⁴¹ IoDSA, The King IV Code (2016) Part 5.3, Principle 8.

⁴⁴² Harris op cit note 3 at 16.

⁴⁴³ 1980 (4) SA156 (W) 165.

⁴⁴⁴ Harris op cit note 3 at 16.

⁴⁴⁵ IoDSA, The King IV Code (2016) Part 5.3, Principle 7, Recommended Practice 6; Ernst & Young op cit note 31 at 14.

⁴⁴⁶ Harris op cit note 3 at 20.

⁴⁴⁷ S 6(10) of the Companies Act 71 of 2008; Harris op cit note 3 at 20.

governance. The Code, however, recognises technology as the company's intellectual property,⁴⁴⁸ and that directors should govern the asset so as to assist the company in defining a core purpose and achieve its strategic objectives.⁴⁴⁹ The Code also recognises information as being separate from technology, strengthening the provisions of the Act with practice recommendations.⁴⁵⁰

(e) *Integrating a stakeholder relationship*

In Chapter II, the importance of stakeholders was underlined to the extent that they could affect the operations, objectives, and reputation of the company in various ways. Contrary to the Act, the Code recognises stakeholder interests.⁴⁵¹ Muswaka points out that while directors are legally required to act in the best interests of the company, the Act does not oblige them to consider stakeholder interests.⁴⁵² Stakeholder interests are tangentially considered in the Act through the business judgement rule and the requirement to appoint a social and ethics committee.⁴⁵³ In the absence of any specific mention of stakeholder interests,⁴⁵⁴ sections 26 and 31(3) of the Act only recognise the rights of stakeholders to company records⁴⁵⁵ and financial statements.⁴⁵⁶ The Code adopts the stakeholder-inclusive model,⁴⁵⁷ which dictates that expectations, interests and needs of stakeholders are not dependent on shareholder interests.⁴⁵⁸ For instance, directors must balance the interests of all stakeholders by creating an effective communication plan.⁴⁵⁹ For this reason, the Act should be amended to include the recognition of stakeholder interests.

⁴⁴⁸ IoDSA, The King IV Code (2016) Part 5.4, Principle 12, Recommended Practice 13 and 14; Meyer op cit note 49; Deloitte, 'King IV: Bolder Than Ever'(2016) 5 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/ZA_King_IV.pdf, accessed on 11 May 2018.

⁴⁴⁹ Ibid.

⁴⁵⁰ IoDSA, The King IV Code (2016) Part 5.4, Principle 12, Recommended Practice 12.

⁴⁵¹ L Muswaka 'A Critical Analysis of the Protection of Stakeholders' Interests under the South African Companies Act: (Part 2) (2014) 5(3) *Mediterranean Journal of Social Sciences* 70 – 71.

⁴⁵² Ibid.

⁴⁵³ L Muswaka 'A Critical Analysis of the Protection of Stakeholders' Interests under the South African Companies Act: (Part 2) (2014) 5(3) *Mediterranean Journal of Social Sciences* 66.

⁴⁵⁴ Ibid.

⁴⁵⁵ S 26 of the Companies Act 71 of 2008.

⁴⁵⁶ S 31(3) of the Companies Act 71 of 2008.

⁴⁵⁷ IoDSA, The King IV Code (2016) Part 5.5, Principle 16.

⁴⁵⁸ Deloitte 'King IV: Bolder Than Ever'(2016) 8 available at https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/ZA_King_IV.pdf, accessed on 11 May 2018.

⁴⁵⁹ IoDSA, The King IV Code (2016) Part 5.5, Principle 16, Recommended Practice 4.

V. CONCLUSION

While directors are not expected to be experts on relevant subject matter, they are responsible to take reasonably diligent steps to actively seek out information rather than being passively ignorant.⁴⁶⁰ While the company secretary should update directors of regulatory and industry developments,⁴⁶¹ a director should not simply accept information at face value, but evaluate such information.⁴⁶² The Code recognises the importance of the business judgement rule because it ensures that boards demonstrate integrity, competence, responsibility, transparency, accountability and fairness. Therefore, for directors to receive protection afforded by section 76(4)(a) of the Act they need to apply the Code.

Directors who ignore or do not comply with the Code in making decisions could be liable to the company, shareholders, or stakeholders.⁴⁶³ Therefore, directors need to follow the recommendations of the Code to avoid liability. This means that the Code can be enforced through the business judgement rule because it demands the standard of care required to comply with the Act.⁴⁶⁴

The role of the boards of directors with regards to corporate governance is consistent with the legal duties prescribed in the listing requirements of the JSE and the Act; and applying the Code would lead to compliance with the Act. This suggests that directors who are non-compliant with the Code may become non-compliant with the Act. Compliance is assessed by the CIPC.⁴⁶⁵ If there is non-compliance with the Act, the CIPC can issue a compliance notice,⁴⁶⁶ and failure to comply with such notice can result in a fine of up to R1 million being imposed by a court or an investigation by the National Prosecuting Authority.⁴⁶⁷ However, it remains necessary for the legislature to amend the Act to make explicit provision for the governance in the field of information and technology and to put pressure on the director to consider the interests of

⁴⁶⁰ IoDSA, 'The Business Judgement Rule,' (2013), 3 – 4 available at https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/05E93ACB-10BE-4507-9601-307A66F34BD8/IoD_Business_JudgementEmail.pdf, accessed on 18 October 2018.

⁴⁶¹ Ibid.

⁴⁶² Ibid.

⁴⁶³ Visser op cit note 57 at 4.

⁴⁶⁴ Ibid.

⁴⁶⁵ S 185, 186, & 187 of the Companies Act 71 of 2008.

⁴⁶⁶ S 171 of the Companies Act 71 of 2008.

⁴⁶⁷ S 171(7) of the Companies Act 71 of 2008.

stakeholders rather than adopting an ‘enlightened shareholder approach’.⁴⁶⁸ Therefore, the Code reflects and even strengthens various provisions of the Act that relate to the board’s role in corporate governance.

⁴⁶⁸ Harris op cit note 3 at 26.

CHAPTER 5

CONCLUSION AND RECOMMENDATIONS

I. CONCLUSION

The primary objective of this study was to evaluate whether there was sufficient evidence to indicate that the Code can be enforced on boards of directors in respect of corporate governance in South Africa. This chapter will argue that there is a need to enforce the Code based on compelling evidence. The recommendations will address the effect and enforceability of the Code on board governance. The Act is important legislation, which could ensure regulation of the Code. This chapter will describe the training that directors and other company officers can receive to achieve sufficient working knowledge of the Code and corporate governance in general. This study will provide a basis for future studies and make a valuable contribution to the realm of corporate governance in South Africa.

Corporate governance provides an important moral compass for directors. This can be achieved by creating strong CGF's and ensuring they are correctly enforced, leading to the attainment of corporate governance benefits.⁴⁶⁹

Proper application of the Code would facilitate well-informed judgements within the scope and protection of the business judgement rule. The 'apply and explain' disclosure regime of the Code can be considered as a method by which directors will inevitably comply with the business judgement rule in the Act. Applying the Code will ensure an appropriate composition of boards, oversight of risk management, information and technology governance, prevention of over-remuneration of directors and ensure that the 'tick-box' approach to compliance is curtailed. In addition, the Code requires the use of integrated reporting as a method of stakeholder communication to build trust between shareholders and stakeholders.⁴⁷⁰ Moreover, a director who complies with the Code's moral strictures will probably receive the protection afforded by the business judgement rule against a claim for personal liability.⁴⁷¹ It follows that the Code can be

⁴⁶⁹ Kondlo op cit note 12 at 61 – 62.

⁴⁷⁰ IoDSA, The King IV Code (2016)13.

⁴⁷¹ Muswaka op cit note 371 at 39.

enforced through the business judgement rule, facilitating good judgement and proper decision-making.

Directors need to be compelled to follow the precepts of the Code, because South Africa has a hybrid system of corporate governance, in which there is a link between the Code and the law.⁴⁷² The Code is directly enforceable in terms of the JSE listing requirements, since the requirements make it mandatory for listed companies to comply with the ‘apply and explain’ disclosure regime of the Code or face termination of their listing on the JSE.⁴⁷³ Since many principles of the Code are linked to the listing requirements of the JSE and integrated within the Act, compliance with the Code leads to compliance with the Act, the Code can be enforced to a certain extent through the Act.⁴⁷⁴ For instance the Code adds weight to the provisions of the Act and provides a regulatory guideline for compliance with the Act. Non-compliance with the Act can result in a penalty, which amounts to tangential enforcement of the Code through the Act.⁴⁷⁵

Therefore, as stated in the Code:

‘In South Africa, as in many jurisdictions around the world, a hybrid system of corporate governance has developed as, over time, some practices of good governance have been legislated in parallel with the voluntary King Codes of governance.’⁴⁷⁶

The King Codes have evolved over time and in the process significantly developed corporate governance to a position of eminence, elevating the moral and ethical basis of business for the overall benefit of honest and effective business in South Africa.

⁴⁷² Parry op cit note 3 at 28.

⁴⁷³ Ibid 40 – 41.

⁴⁷⁴ Ibid 40.

⁴⁷⁵ Ibid 22.

⁴⁷⁶ IoDSA, The King IV Code (2016) 35.

II. RECOMMENDATIONS

(a) Companies Amendment Bill enacts principles of the King IV Code

The draft Companies Amendment Bill (CAB) was published for public comment on 21 September 2018, strongly indicating that the Code principles were being adopted in legislation. The CAB reflects the Code by obliging directors to prepare and present a remuneration report containing specific details of their remuneration at the shareholder meeting.⁴⁷⁷ The CAB also echoes the Code by stating that the names of each director of the company must be disclosed in the report.⁴⁷⁸ The CAB also reflects the Code in stating that all public, and not only listed public companies and state-owned companies appoint social and ethics committees.⁴⁷⁹

The CAB proposes that ‘a person who does not hold or have a beneficial interest in securities issued by a profit company, or is not a member of a non-profit company, is entitled access to the company’s Memorandum of Incorporation (MOI), records relating to its directors and access to minutes of annual meetings’.⁴⁸⁰ Further, the CAB provides for access to the securities register of a profit company. This suggests that the CAB is analogous to the Code, because, when persons have access to company information, the transparency and disclosure requirement of the Code is applied. The CAB was published for comment at the time of this study, and it is yet to be seen whether the proposed amendments will take effect. If accepted, it will provide further evidence of the legislature’s intention to statutorily incorporate principles of the Code. Therefore, it is recommended that the proposed amendments be adopted as law in the interest of good corporate governance.

(b) Establishment of a corporate governance regulatory body

It is recommended that the IoDSA be afforded recognition as a regulatory body to strengthen compliance with the Code. The regulatory function should include an annual on-site inspection of whether the company’s CGF complies with the Code and the OECD principles. The inspection can probe steps taken to create an ethical culture within the company, whether a conflict of interest policy exists, and training programmes for board members regarding the Code and reporting

⁴⁷⁷ S 30(4) of The Companies Amendment Bill.

⁴⁷⁸ S 30(4) of The Companies Amendment Bill.

⁴⁷⁹ S 72 of The Companies Amendment Bill.

⁴⁸⁰ S 26 of The Companies Amendment Bill.

procedures in line with international reporting standards have been introduced.⁴⁸¹ Further, the inspection could assist in creating policies, guidelines and tools that might assist in ensuring compliance with the Code.

(c) *Continuous professional development of directors*

It is recommended that an obligation be placed on directors of small or medium-sized companies to record Continuous Professional Development (CPD) hours relating to their knowledge and application of the Code, by way of attending authenticated training programmes on the Code. Further, it is recommended that directors maintain a CPD register to track their competence and training on the Code and provide this information to the relevant regulatory body, upon request.

(d) *Establishment of corporate governance tribunals*

It is recommended that specialised corporate governance tribunals be created to adjudicate on claims for director liability and corporate governance matters.⁴⁸² Currently, the Companies tribunal adjudicates on company and directorship disputes in terms of the Act, and not the Code *per se*.⁴⁸³ Members of the IoDSA should serve as chairmen in these tribunals to ensure a proper application of the theory and concepts of the Code.⁴⁸⁴

(e) *Inclusion of stakeholder interests in the Act*

It is recommended that the Act be amended to include the recognition of stakeholder interests,⁴⁸⁵ making the Code mandatory and enforceable in that regard, since it encourages a stakeholder-inclusive approach to corporate governance.⁴⁸⁶

⁴⁸¹ Chartered Institute of Internal Auditors, 'Auditing corporate governance' (11 October 2019) available at <https://www.iaa.org.uk/resources/corporate-governance/auditing-corporate-governance/>, accessed on 19 January 2019.

⁴⁸² Chakanika op cit note 77 at 65 – 66.

⁴⁸³ Companies Tribunal 'About us' (2019) available at <https://www.companiestribunal.org.za/about-us/about-the-companies-tribunal/>, accessed on 03 December 2019.

⁴⁸⁴ Chakanika op cit note 77 at 65 – 66.

⁴⁸⁵ Parry op cit note 3 at 42.

⁴⁸⁶ IoDSA, 'The King IV Report on Corporate Governance,' (2016) 13; Radebe op cit note 39 at 274.

(f) *Inclusion of information and technology governance in the Act*

It is recommended that the legislature recognises information and technology governance in the Act. According to Natesan, the ransomware attack of Johannesburg in 2019 necessitates boards of directors to take a more holistic view of technology and the risk it poses.⁴⁸⁷ Although the Act allows for the use of information technology,⁴⁸⁸ it fails to present governance procedures, whereas the Code provides recommendations for information and technology governance, which includes training of staff and conducting an information and technology assessment of the company.⁴⁸⁹

(g) *Applying the King IV Code to directors of smaller companies*

It is recommended that directors of smaller companies not listed on the JSE comply with the business judgement rule to give effect to the recommendations of the Code. According to Anyango, this would give the Code legal status for smaller companies, which are presently not subject to the listing requirements of the JSE.⁴⁹⁰ This would ensure that directors of smaller companies do not ‘fall through the cracks’ when it comes to their responsibilities in terms of corporate governance.

(h) *Training for corporate governance professionals*

It is recommended that corporate governance professionals and company secretaries be required to attend corporate governance training programmes to facilitate the implementation of the Code in companies.⁴⁹¹ This would ensure that many corporate governance challenges are anticipated and avoided.⁴⁹²

⁴⁸⁷ IoDSA, ‘City of Johannesburg ransomware attack a wake-up call for boards’ (2019), available at <https://www.iodsa.co.za/news/475603/City-of-Johannesburg-ransomware-attack-a-wake-up-call-for-boards-says-IoDSA.htm>, accessed on 6 November 2019.

⁴⁸⁸ S 6(10), 6(11), 61(10), 63(2), and 73(3) of the Companies Act 71 of 2008.

⁴⁸⁹ IoDSA, The King IV Code (2016) Part 5.4, Principle 12, Recommended Practice 13; Kula op cit note 290.

⁴⁹⁰ D Anyango op cit note 181 at 75.

⁴⁹¹ Chakanika op cit note 77 at 65 – 66.

⁴⁹² Ibid.

III. FUTURE STUDIES

This study may constitute the basis for future studies, specifically in the realm of corporate governance and the Code. Future studies are necessary to validate the conclusions drawn in this study. While this research does not deal with every corporate governance challenge faced by directors, the study serves as an opportunity for future research on overlooked corporate governance challenges. Future research should evaluate whether the creation of corporate governance regulatory bodies, specialised tribunals and use of courts would reduce corporate governance challenges and adequately enforce the Code. While this study focuses more on law reform in the context of the Act, future research could explore whether the Code could influence the development of other relevant legislation.

IV. CONTRIBUTIONS OF THE STUDY

This is one of the few studies that provides a critical analysis of the effect and enforceability of the Code on the role of directors. Not only does this study indicate some of the corporate governance challenges that companies and directors face, but also the benefits they would obtain by applying the Code. It is also intended to create awareness of the need for law reform, the relevance of which cannot be more aptly conveyed than in the Code:

‘Good governance does not exist separately from the law, and a corporate governance code that applies on a voluntary basis may also trigger legal consequences.’⁴⁹³

⁴⁹³ IoDSA, The King IV Code (2016) 35.

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Mr Greshen Naidoo (209520647)
School Of Law
Howard College

Dear Mr Greshen Naidoo,

Protocol reference number: 00011801

Project title: The enforcement of the King IV Code with emphasis on the role of the board of directors for corporate governance in South Africa

Exemption from Ethics Review

In response to your application received on 6 April 2021, your school has indicated that the protocol has been granted **EXEMPTION FROM ETHICS REVIEW**.

Any alteration/s to the exempted research protocol, e.g., Title of the Project, Location of the Study, Research Approach and Methods must be reviewed and approved through an amendment/modification prior to its implementation. The original exemption number must be cited.

For any changes that could result in potential risk, an ethics application including the proposed amendments must be submitted to the relevant UKZN Research Ethics Committee. The original exemption number must be cited.

In case you have further queries, please quote the above reference number.

PLEASE NOTE:

Research data should be securely stored in the discipline/department for a period of 5 years.

I take this opportunity of wishing you everything of the best with your study.

Yours sincerely,



- PROF S BOSCH

**Academic Leader Research
School Of Law**

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