

# THE CIPC AS THE REGULATOR OF STATE OWNED COMPANIES

## “Boards of SOCs”



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# Disclaimer

The information contained in this presentation is published by Companies and Intellectual Property Commission (CIPC) and is provided for presentation purposes only.

Accordingly, this presentation is intended to provide readers a broad understanding of the general principles being discussed that pertain to the topic.

# CIPC Functions

Promotion of  
education &  
awareness

Registration of  
Co(s), Co-ops, and  
IP rights

Sec 187

Disclosure of  
Information on  
registers

Enforcement of  
legislation

# CIPC -The Regulator Of State Owned Companies

- ❑ The CIPC has jurisdiction over state owned companies (“SOCs”) as defined in the Companies Act 2008.
- ❑ The CIPC is a juristic person established by Section 185
- ❑ To monitor proper compliance with the Act section 187(2)(b).
- ❑ Section 9 of the Act deals with modified application with respect to SOCs.

Section 9(1) states: *“Subject to sections 5(4) and (5), any provision of this Act that applies to a public company applies also to a state-owned company, except to the extent that the Minister has granted an exemption in terms of subsection(3)”*.

# State Owned Companies (SOCs)

*“Government needs to retain its ownership of state-owned companies to ensure economic growth and create employment for generations to come, said Public Enterprises Minister Lynne Brown.*

*In her budget speech for the 2016-17 financial year, Brown emphasised that South Africa’s parastatals, worth R908bn, are key strategic assets that need to be kept intact”*

**(Minister Lynne Brown, Fin 24 April 2016)**

# State Owned Companies (SOCs)

- ❑ State-owned companies (SOCs) exist in South Africa to drive economic development and improve service delivery to the large population.
- ❑ In order for SOCs to achieve their mandates, as set out by government through their shareholding department, financial assistance and general good support by the state is imperative.
- ❑ The boards of SOCs should have the necessary authority, competencies and objectivity to carry out their function of strategic guidance and monitoring of management.
- ❑ They should act with integrity and be held accountable for their actions.
- ❑ Thus the boards of SOCs should be suitably and competently composed so that they can exercise objective and independent judgement.

Are SOC boards really that different to private sector boards?



# SOCs vs. Private Company Boards

- ❑ SOC are different from the private sector because Corporate Governance includes both Government and Boards, with Government make final decisions concerning allocation of finance and the selection and retention of board members.
- ❑ Both groups are therefore involved with the process of governing companies.
- ❑ It is however important to remember that the quality of corporate governance depends on whether corporate governors have the capacity, knowledge, experience, expertise and integrity to make and carry out wise decisions in the interests of the shareholder, company and stakeholders including the public.



# SOCs vs. Private Company Boards

- ❑ However, South Africa's SOC's have proven time and time again they are not capable of running profitable operations.
- ❑ The guarantee exposure (which is a higher figure than the government guarantees) of prominent SOC's are listed below:

Eskom – **R170 billion**

Passenger Rail Agency of South Africa – **R53 billion**

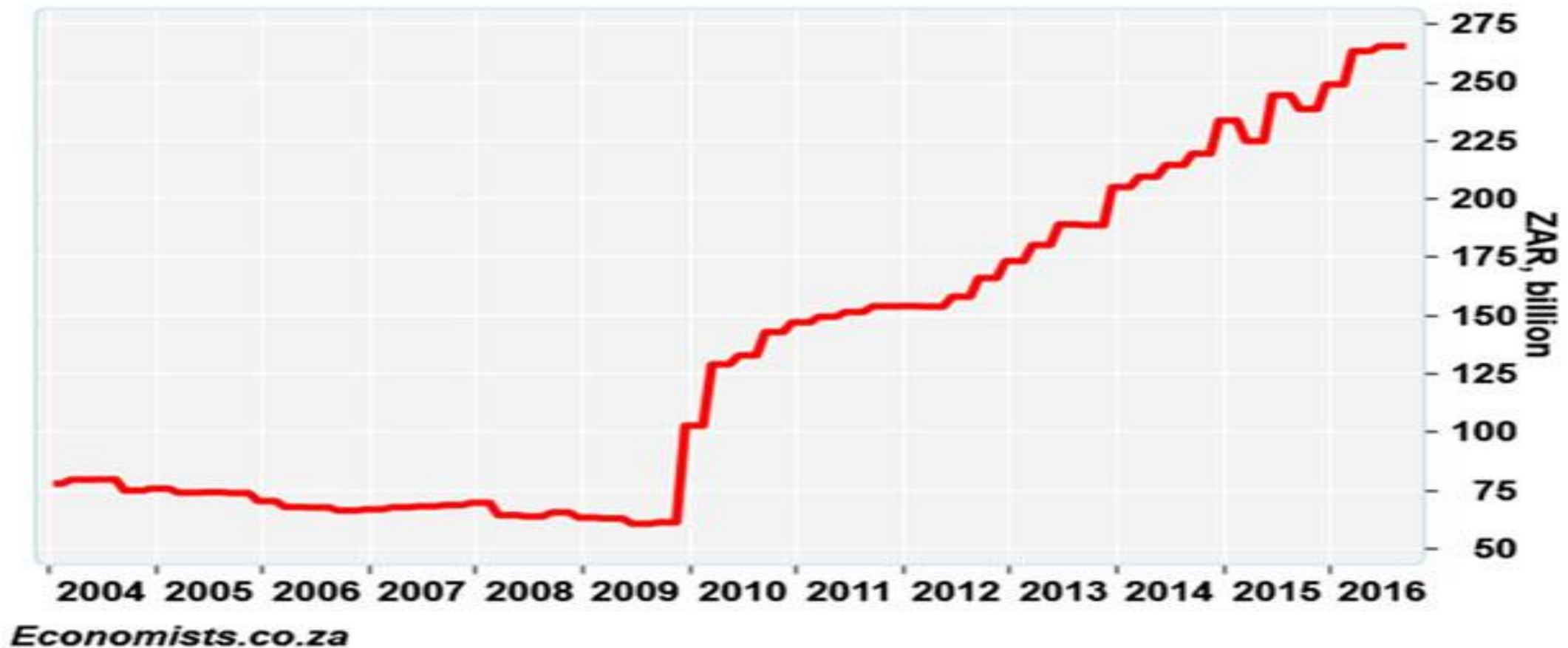
South African National Roads Agency Limited – **R35 billion**

South African Airways – **R19.1 billion**

South African Post Office – **R4.4 billion**

# Stats

**Government Guarantees to SOE's and agencies**



The graph below, courtesy of [Economists.co.za](http://Economists.co.za), shows the government guarantees to state-owned companies and agencies over the last 10 years

# Driving forces behind a SOC board as compared to private sector boards

The shareholder's expectations are vastly different to the private sector...

- private company is mostly only profit focussed and driven, high performance
- private company rarely has a political influence, or is politically charged
- SOC's are expected to last longer, whilst private companies may purposefully have a short market and exit strategy

# Demands placed on SOC boards

- A turbulent economy
- Qualified & experienced directors & employees
- Demands for greater company & employee performance
- Increasing awareness & need for good governance
- The role of ethics in public life is changing in all sectors of democratic society
- Boardroom challenges
- Remaining relevant whilst staying competitive
- Balancing the business against over prescriptive behaviour
- Integrated reporting
- Keeping it together as King IV enters the market

# Demands placed on SOC boards

## Gains

- People living with more than \$2 per day (up)
- Formal dwellings (up)
- Life expectancy (up)
- Black middle class (up)
- Board efficacy (up)
- Financial market stability (up)
- Audit systems (up)

## Worries

- Education (down)
- Labour relations (down)
- GDP (down)
- Social unrest (up)
- Employment (down)
- Political certainty (down)
- Regulatory over-reach (down)
- Country credit down-grading

# For what and to whom is the board accountable

## **1. Governing Body ('the board') sets organisation's strategic objectives & direction**

- board approves policy & planning
- board oversees & monitors
- board is ultimately accountable for organisational risk

## **2. Board supervises / monitors executive management performance**

- board evaluates executive management performance (e.g. CEO, CFO, CIO, HR)
- organisation's leaders are responsible to ensure that all activities driven by management lead toward success & not failure

## **3. Board is accountable to shareholders & stakeholders**

- organisations have evolved their understanding of importance from exclusive attention of shareholders to now also include stakeholders, namely employees, suppliers, general public, etc.
- board is subject to regular evaluation

# Companies Act on SOC boards

## BOARD RESPONSIBILITIES

### Going Concern

Solvency And Liquidity Test

Solvency – Financial Position

- Net Asset Value
- Market Values & Realisable Values

Liquidity

- Liquid Assets
- Short Term Obligations

Insolvency Audit

- Long Term Sustainability
- Short Term Liquidity Capacity
- Cash Flow From Operations

# Companies Act on SOC boards

## DIRECTOR RESPONSIBILITIES - CORE DUTIES SEC 76

- Disclose any conflict of interest
- Use position and information for company's benefit
- Disclosure of information
- Perform duties:
  - In good faith
  - In best interest of the company
  - With care, skill and diligence



# Companies Act on SOC boards

## DIRECTOR RESPONSIBILITIES: STRATEGY AND CORPORATE STRUCTURE

- duty to comply with the act in relation to different types of companies (section 8)
- duty to comply with the company's memorandum of incorporation (section 13)
- duty to manage the business affairs at the company (section 66(1))
- duty to carry on the business without trading recklessly or under insolvent conditions (section 22)

# Companies Act on SOC boards

## DIRECTOR RESPONSIBILITIES: BOARD STRUCTURE AND CORPORATE ADMINISTRATION

- Duty to appoint board committees (section 72)
- Duty to appoint an audit committee (section 94)
- Duty to appoint a company secretary (section 84 & 86)
- Duty to call and convene a shareholder's meeting (section 61)

# Companies Act on SOC boards

## DIRECTOR RESPONSIBILITIES: ACCOUNTABILITY AND ASSURANCE

- duty to keep company records (section 24)
- duty to keep accounting records (section 28)
- duty to comply with chapter 3 of the act (section 34(1) & 94)
- duty to pay directors remuneration in terms of memorandum of incorporation and get it approved by shareholders by special resolution (section 66(8) & 66(9))
- duty to appoint auditors (section 90 & 92)

# Companies Act on SOC boards

## LIABILITIES OF DIRECTORS

- breach of duties
- breach of accountability (section 213 & section 214)
- reckless trading
- prospectus liability
- Insolvency act( section 424)

# Challenges directors face in a board



# General boardroom challenges

- boards not entirely independently run, great influence by Minister, labour unions, civic groups, etc.
- political interference
- board composition not always ideal
- board members not suitably qualified
- board members lack skill & experience
- SOC boards not nimble, in spite of their market domination and state mechanisms (SAA, PRASA,)
- employees of SOCs motivated differently to private sector & not as sharp with relatively no fear of retrenchment
- budgetary constraints & massive red tape
- perception of corrupt officials / employees (R30bn pa in procurement)

# Composition & balancing of boards

## Board effectiveness, evaluation & rotation

### **What makes a balanced board of directors?**

- In essence, a board is a decision-making body, with responsibility for oversight and which delegates authority (but not responsibility) to management.
- To be effective, boards must be a working group of members who trust and understand one another.

# The Board as the focal point

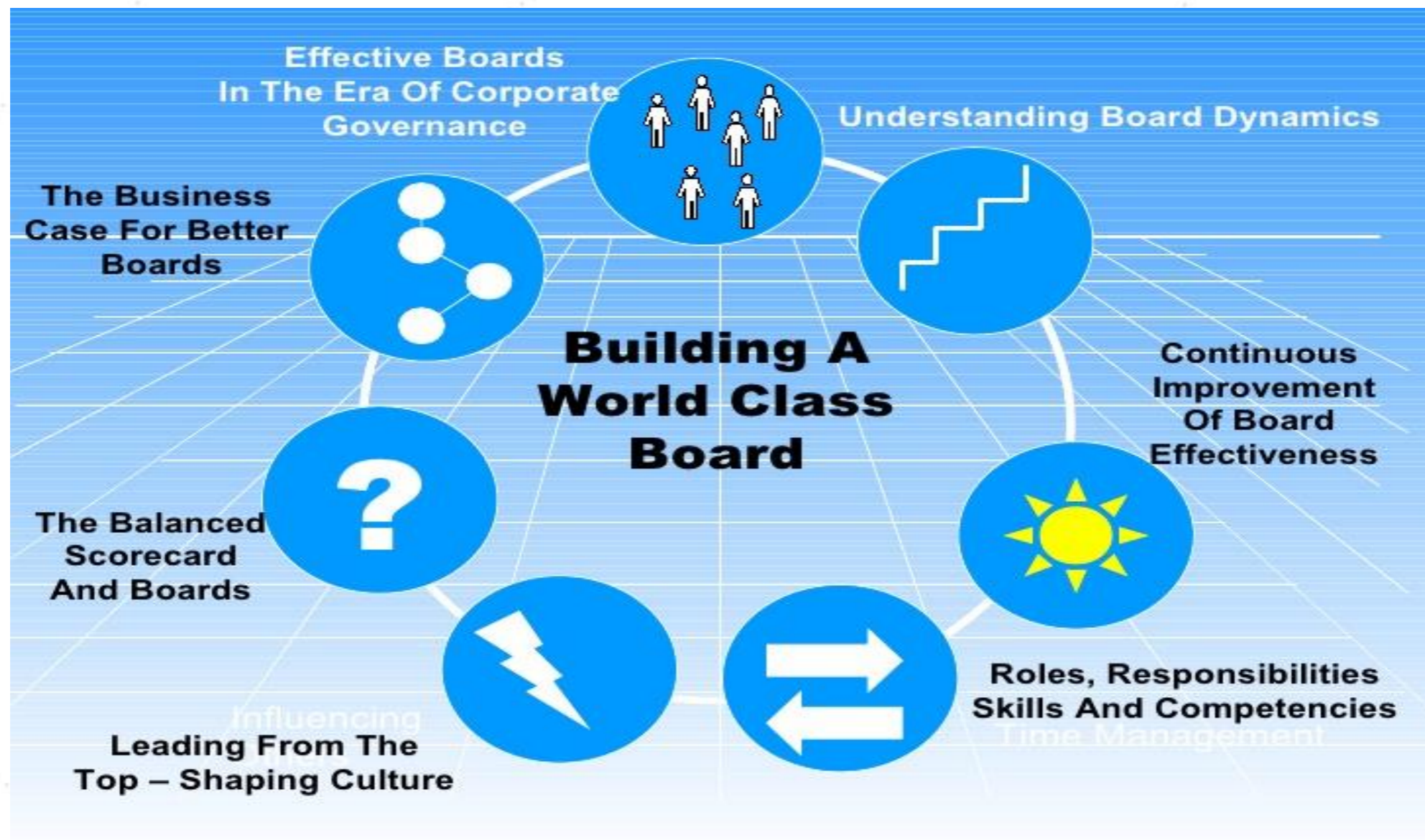
Role of the Governing Body ( board )

King IV Principle 3.1: The GB should serve as the focal point and custodian of corporate governance in the organisation



# Board composition & effectiveness

The Governing Body ('the board') needs to be fully functional - this is where the strategy is set . . .



# Board Composition

- Who's sitting in your boardroom?
- Do your directors bring the right mix of skills, experiences and expertise to best oversee your company?
- Are they a diverse group, or a group with common backgrounds and outlooks?
- Can they help see into the future and how your industry is likely to take shape?
- And are some of your directors serving on your board as well as those in other industries?

# Board Composition

Board composition is “the” issue for investors in 2017- *Investors want to know who is sitting in the boardroom and whether they are the best people for the job.*

King IV emphasises race and gender representation on the governing body – Chapter 2.71

Principle 3.2: The GB should ensure that in its composition it comprises a balance of the skills, experience, diversity, independence and knowledge needed to discharge its role and responsibilities

Time to refresh the board :-

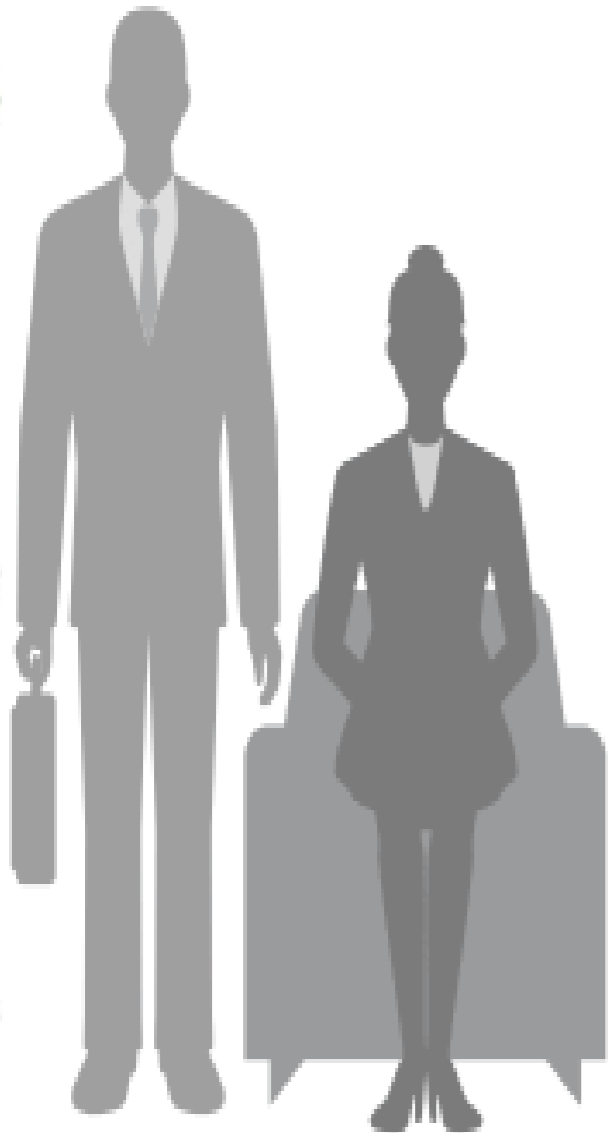
- ✓ Board Diversity ( gender, race, ethnicity, skills, experience, expertise, age and even geography. It’s about diversity of thought and perspective.)
- ✓ Evaluate their leadership structure and split the chair and CEO role

King IV - The chairman of the board should be independent and free of conflicts of interest at appointment – Chapter 2.38

King IV - The board should appoint the chief executive officer and establish a framework for the delegation of authority – Principle 2.17

# Stats from PWC on Boards

## The importance of diversity on the board<sup>1</sup>

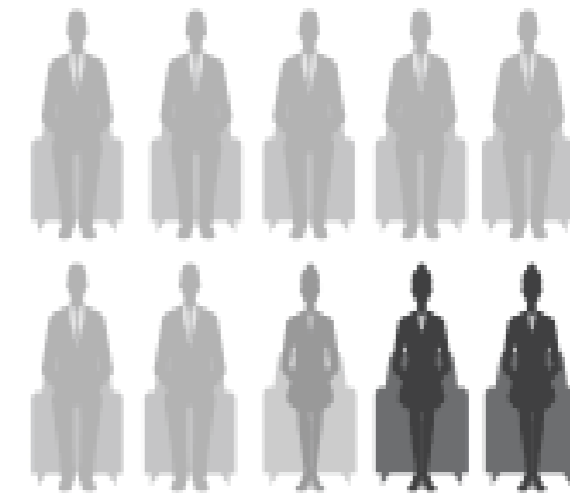


**91%**

..... of directors say diversity enhances board effectiveness

**84%**

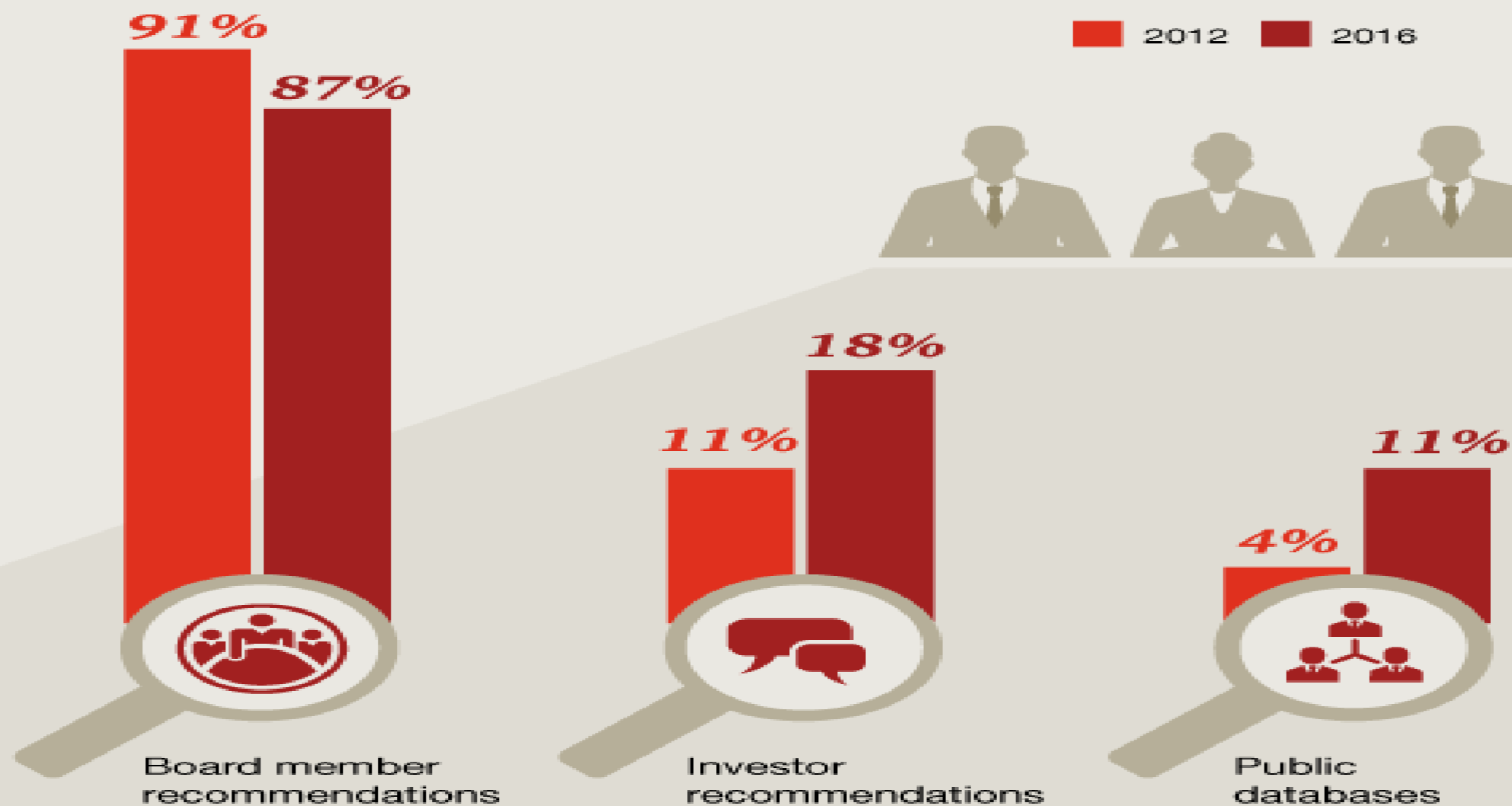
..... of directors say the same leads to enhanced company performance



women make up 21% of S&P 500 company boards

# Stats from PWC on Boards

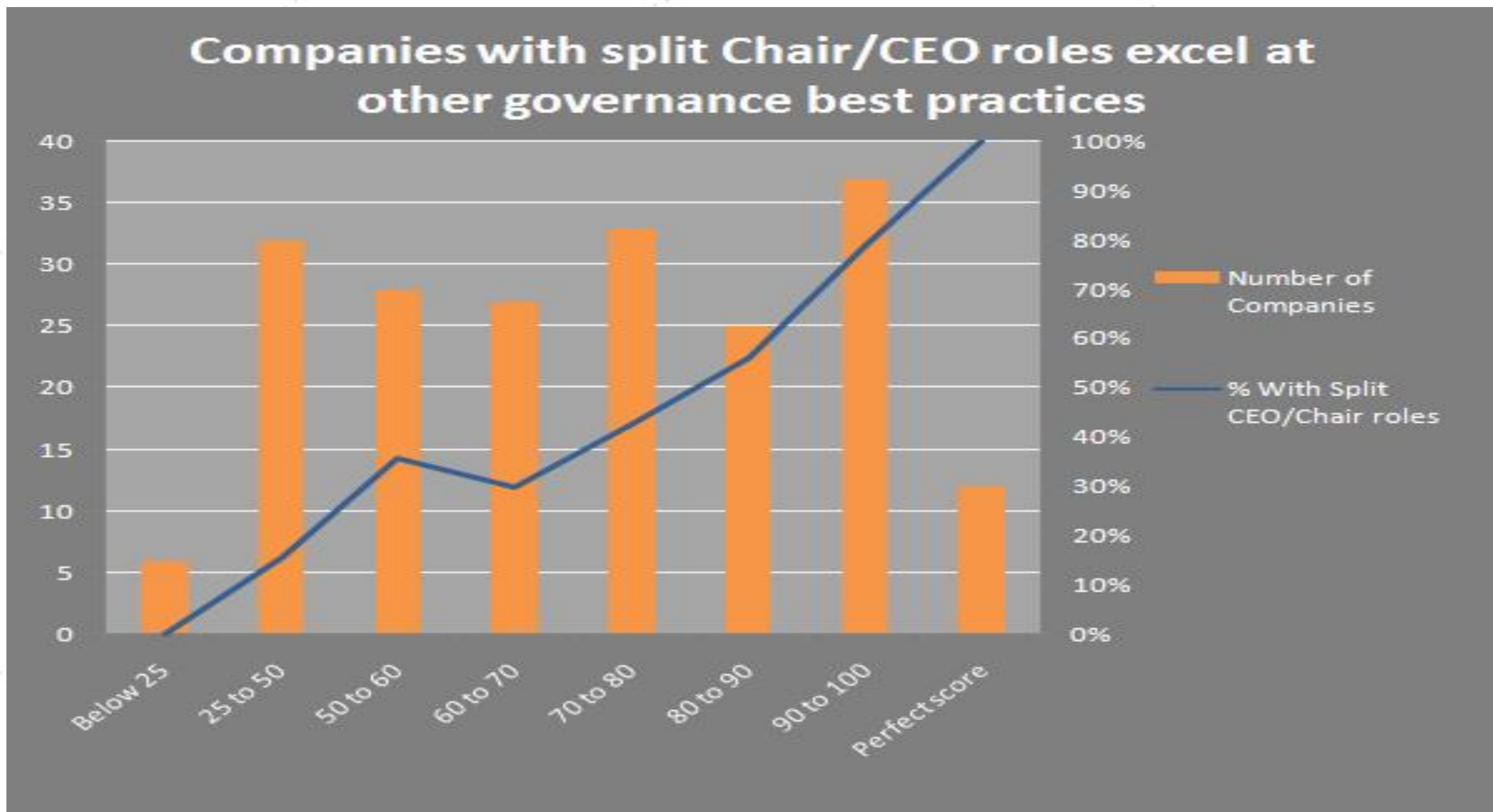
**Thinking outside the boardroom box:  
More boards are listening to investors  
when looking for new blood**



Q. What sources do you use to recruit new board members?  
Base: 884  
Source: PwC, 2016 Annual Corporate Directors Survey, October 2016.

# Stats on spilt role of CEO and Chair

[Rotman School of Management - University of Toronto](#)



# Rotation of the Board

Rotation of board members should be structured so as to retain valuable skills, maintain continuity of knowledge and experience and introduce people with new ideas.

King IV [Chapter 2.74 to 76]

# Board types

There are various types of boards; each are unique to the environment in which they operate . . .

- **Will it be a unitary board or a two-tiered board?**

- **What structure, composition & behaviour might the board follow?**

  - Ceremonial board

  - Liberated board

  - Progressive board

- **Boards may undergo various phases - as the board becomes more evolved, so the functions between its members become more developed**



# Board types (Cont.)

- ❑ **With mounting pressures & demands *vis-à-vis* board performance so comes an obligation for directors to reach beyond fiduciary duties & technicalities**
  
- ❑ **Mindful boards & their directors:-**
  - master the explicit and implicit ways of working to unrestricted group leadership & efficacy
  
  - operate at a level where they are not pre-occupied with their own preconceived thoughts, ideas & biases (conscious & unconscious)
  
  - are not blinded, neither captured by their own history
  
  - are collaborative in approach & solutions, where ‘disruptive thinking’ to enhance strategy is encouraged

# Qualities of directors

Directors require a strong mix of interpersonal & market skill sets ...

## Personal attributes

- strong interpersonal & communications skills
- energetic / tenacious
- independent mind
- strategic / lateral thinker
- analytical / cautious
- ethical / diligent
- probes matters for further understanding
- listens attentively

## Market skills

- business skills / international exposure
- industry expertise
- financial knowledge
- understanding of regional, national & international changes viz; business,

# Dysfunctional Board

## Top Ten Signs of a Dysfunctional Board of Directors

**Lack of Confidentiality**

**Non - participants**

**Conflicting Agendas**

**Dominating Members**

**Lack of Respect**

**Lack of Trust**

**Lack of Order**

**Hostile Environment**

**Personal and Political  
Agendas**

# CEO - fat cat pay cheques

South Africa has one of the biggest pay gaps in the world, where CEOs get paid on average 500 times more than the average employee.

South Africa ranked seventh when counting CEO salaries around the world, according to a *Bloomberg survey of executive paychecks* around in the world's 25 largest economies.



# Why SA's chief executives are coining it

## SA CEOs are paid many times more than workers

Companies with the biggest pay gaps: The number of times the chief executive's annual pay exceeds that of the lowest paid worker  
JSE listed companies, 2013



## ... by R3.69m on average a year

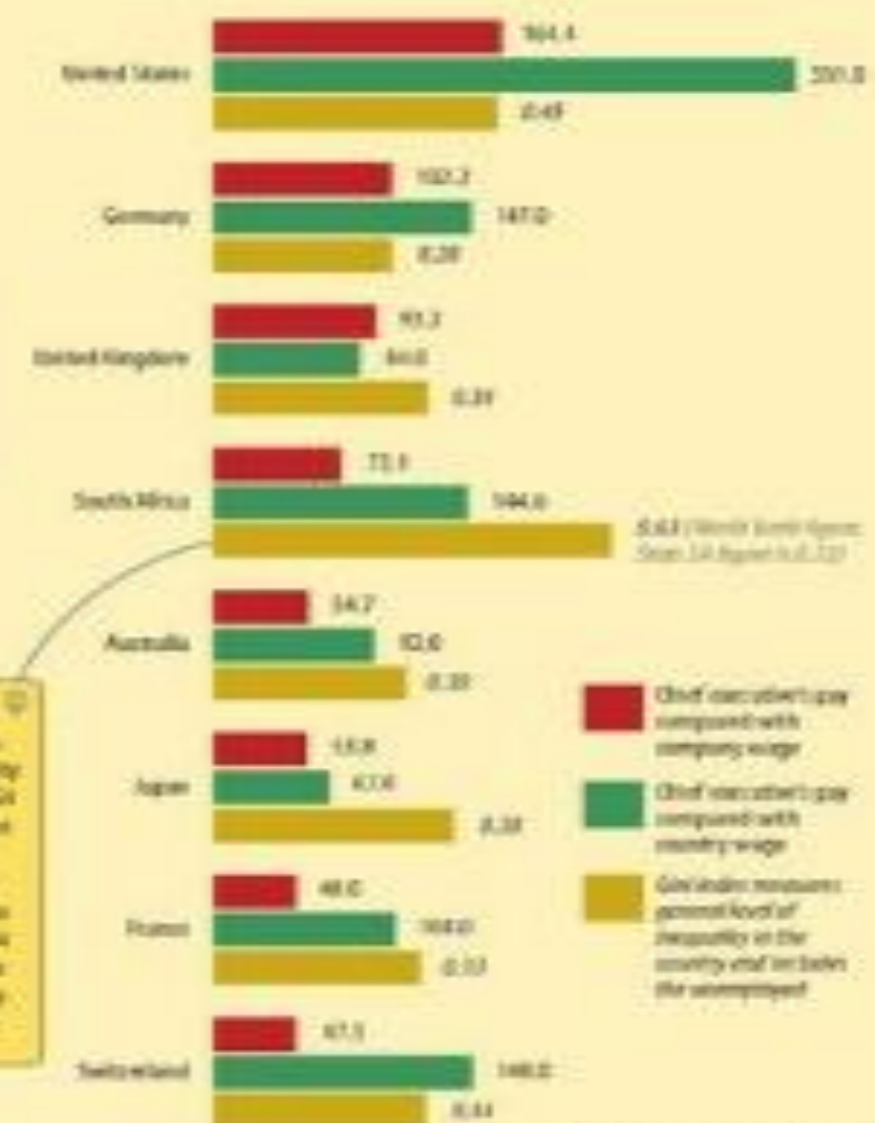
Average pay gap between chief executive and lowest paid worker in JSE listed companies  
2013



Demarcation researchers say SA's general Gini inequality level equated to 8.04 if the unemployment rate fell to 10%. The Gini index for employed earners in SA would not be 0.44 — still higher than the general average in many countries.

## ... and fare better than CEOs in Switzerland

Chief executives' average pay compared with average company wage, average country wage and Gini inequality index  
2013



Source: 2014 ILO Asia-Pacific Survey of Wages, MEMPHIS

# Regulation of SOCs

- There is no simple recipe for regulators: the laws, traditions, and historical performance by the SOC differ widely.
- The CIPC has identified State Owned Entities Oversight Units as critical stakeholders in promoting compliance with the Companies Act and would like to encourage these Oversight Units Contact the CIPC for
  - ❑ assistance on issues relating to the Companies Act for example concurrent jurisdiction, procedures to be followed in appointing and removing directors, the establishment of Social and Ethics Committees and relief from oppressive or prejudicial conduct or from abuse of separate juristic personality of company.

# Regulation of SOCs

- ❑ Strengthen the relationship with the Company Secretary's office of the respective SOCs as this is critical to track compliance with the Companies Act.
- ❑ Strengthen the relationship with the Auditor General's or Independent Auditor office, as the case may be, to identify issues relating to the Companies Act early



# CIPC action against SOC - SAA

- The SAA chairperson was found by the CIPC to have acted in a manner inconsistent with the duties of a director in relation to a 2013 aircraft deal.
- In 2013, the SAA board decided to lease 10 new planes from a financier, however SAA is reported to have only approved two planes
- SAA contravened the Companies Act 2008 by misrepresenting a board decision.
- Compliance notice was served to the SAA and the entity was afforded time to respond . Another option was to bring a delinquency application



**“A focused Board concentrates on strategy oversight and governance practices, to avoid getting lost in the forest.” (Pearl Zhu Digitizing Boardroom)**