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THE EXTENT TO WHICH THE FIDUCIARY DUTIES AND LIABILITIES OF DIRECTORS OF STATE-OWNED COMPANIES FACILITATE GOOD CORPORATE GOVERNANCE IN SOUTH AFRICA.

A mini-thesis submitted to the Faculty of Law at the University of the Western Cape in partial fulfilment of the requirements for the Degree of Master's in Law (LLM).

by

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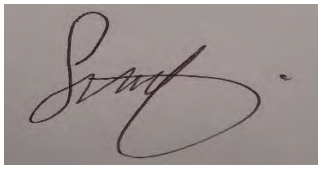
DECLARATION

I, **Stephany Theresa Terblanche**, hereby declare that "**The Extent to Which the Fiduciary Duties And Liabilities Of Directors Of State-Owned Companies Facilitate Good Corporate Governance In South Africa**", is my original work (except where acknowledgments indicate otherwise) and that neither the whole work nor any part of it has been, is being, or is to be submitted for another degree or examination in any other University or academic institution. All sources and materials used are duly acknowledged and properly referenced. I authorise the University of the Western Cape to reproduce for the purpose of research only, either the whole or any portion of the contents in any manner whatsoever.



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Dedication

I dedicate this thesis to God, my family and my friends. It is only by God's grace that I have found the strength to continue this journey. To my father, you taught me the spirit of perseverance, humility and delayed gratification. To my mother, you taught me the importance of hard-work, resilience, and the power of a woman. Your constant words of love and encouragement ring in my ears. To my sister, Grace, thank you for living up to your name, you are a constant reminder of God's love and favour.

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KEYWORDS AND PHRASES

Board of Directors

Business Judgement Rule

Common law

Companies Act 71 of 2008

Companies Act 61 of 1973

Corporate Governance

Denel

Department of Public Enterprises

Directors

Duty of Care and Skill

Eskom

Executive Authority

Fiduciary duty

Governance failures

King IV Report

Public Finance Management Act 1 of 1999

South African Airways

South African Broadcasting Corporation

Shareholder Representative

State Owned Companies

LIST OF ABBREVIATIONS

BJR	Business Judgement Rule
BE Framework	Board Evaluation Framework
CEO	Chief Executive Officer
CFO	Chief Financial Officer
DPE	Department of Public Enterprises
MBCA	Model Business Corporation Act
MOI	Memorandum of incorporation
PFMA	Public Finance Management, 1999 [No. 1 of 1999]
SAA	South African Airways
SABC	South African Broadcasting Corporation
SOC	State Owned Entity
The Act	The Companies Act, 2008 [No. 71 of 2008]
The Board	The Board of Directors

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CHAPTER ONE

1.1 INTRODUCTION

The legislative and policy framework governing the sector for State-Owned Entities (SOE's) in South Africa is criticised for being legally fragmented, in addition to other governance concerns in the sector, such as financial and operational concerns.[1] In recent years, South African State-Owned Companies (SOCs) have experienced a constant decline in their governance and delivery of public goods.[2] Efforts by these companies to effectively respond to the socio-economic development of the State remains constrained as a result of many factors, including the legal framework governing the sector.[3]

SOCs are defined as companies established by the state for the purpose of partaking in commercial activities on behalf of the government.[4] The Organisation for Economic Development (OECD), defines these entities as 'any corporate entity recognised by national law as an enterprise and in which the state exercises ownership.'[5] SOCs are founded in different statutes - and have various objectives, including socio-political, commercial, or dual objectives.[6] For the purpose of this paper, the term 'state-owned companies' (SOCs) will be used, as the paper reflects on corporate governance through the lens of the Companies Act 71 of 2008 (Companies Act).[7] SOCs are the principal drivers of the formal sector of the economy as they are the providers of the bulk of the State's economic growth.[8] They are the biggest employers in the economy, and they play a vital role in the provision of social services such as infrastructure, utilities, transport, energy, telecommunications, and finance.[9]

Most public entities in South Africa do not perform their public service functions effectively and efficiently, nor do they contribute strongly to the country's economic development.[10] Assessments of the performance of SOCs in South Africa indicate that many are vulnerable to detrimental factors such as debt burdens, underinvestment and corruption; thus undermining

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[1] Kanyane M & Sausi K 'Reviewing State-Owned Entities' Governance Landscape in South Africa' (2015) 9(1) *African Journal of Business Ethics* 28.
[2] Kanyane M and Sausi K (2015) 28.
[3] Kanyane M and Sausi K (2015) 28.
[4] De Visser J, Komote M & Muntingh L 'The Legal Framework for the Appointment and Dismissal of SOE Board Members' *DOI* 4 April 2019 8.
[5] Organisation for Economic Co-operation and Development *OECD Guidelines on Corporate Governance of State-Owned Enterprises* (2015).
[6] Thabane T *The Ownership and Control Architecture of South Africa's State-Owned Companies and its impact on Corporate Governance* (published LLM thesis, the University of Cape of Town, 2020) 1.
[7] The Companies Act 71 of 2008.
[8] Kanyane M & Sausi K (2015) 28.
[9] Thabane T (2020) 1.
[10] Kanyane M & Sausi K (2015) 28.

the state's objectives.[11] It is apparent as well, that some SOCs provide more political capital to politicians than others, fostering a political interest in their affairs.[12]

Despite the presidential review and recommendations on the sector in 2010, the financial performance of SOCs has faced a continual decline.[13] Policy framework agendas adopted since then with the goal of restructuring SOCs have been largely unachieved.[14] In 2014, the Public Protector published a report in which it found certain developments at the South African Broadcasting Corporation (SABC) to be 'symptomatic of pathological corporate governance deficiencies.'[15] The 'State of Capture' report published in 2016 raised further concerns on the governance of companies in this sector.[16] The report revealed that SOCs such as Eskom, South African Airways (SAA), Denel and the SABC, face severe financial difficulties, as well as allegations of fraud, mismanagement and state capture.[17] 'State capture' refers to a form of corruption in terms of which politicians and businesses conspire to affect and influence the country's decision-making process to advance their own interests.[18] In April 2017, following the State of Capture report, the rating agency Standard and Poor's downgraded South Africa to 'junk status.'[19] Standard and Poor's attributed the downgrade to the poor governance of SOCs, as it poses a risk to the country's fiscal outlook.[20] The agency proposed the need for governance reform within this sector.[21]

Against this background, this paper will discuss the study of corporate governance in SOCs in South Africa, particularly to assess whether the current framework providing the fiduciary duties and liabilities of the board of directors of such companies, facilitates good corporate governance in the sector.

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[11] Kanyane M & Sausi K (2015) 28.
[12] Kanyane M & Sausi K (2015) 28.
[13] Kanyane M & Sausi K (2015) 28.
[14] See Presidential Review Committee on State-Owned Entities (2013) Vol 1 – 8.
[15] Thabane T & Snyman-Van Deventer E 'Pathological Corporate Governance Deficiencies in South Africa's State-Owned Companies: A Critical Reflection' (2018) 21 *PER / PELJ* 2.
[16] 'State of Capture' A Report of the Public Protector Report No: 6 of 2016/17 (2016) available at *http://www.saflii.org/images/329756472-State-of-Capture.pdf* (accessed October 2022).
[17] A Report of the Public Protector South Africa (2016).
[18] Arun N 'State capture: Zuma, the Guptas, and the sale of South Africa' available at *https://www.bbc.com/news/world-africa-48980964* (accessed 19 February 2023).
[19] De Visser J et al (2019) 8 - The results from the rating agency were taken from a Business Live Article in 2017: "What the rating Agency said about SA" *Business Live* 4 April 2017 *https://www.businesslive.co.za/rdm/business/2017-04-04- what-the-rating-agency-said- about-sa/* (Accessed 5 May 2017).
[20] De Visser J et al (2019) 9.
[21] De Visser J et al (2019) 10.

1.2 PROBLEM STATEMENT

The efficient governance and management of state-owned companies is crucial for economic growth, particularly in developing economies such South Africa, as these entities play a critical role in society.[22] The decline in the performance and governance of SOCs, as indicated by allegations of fraud, mismanagement, state capture and severe financial difficulties, informs the increased scrutiny of the sector, and forms the basis of this enquiry. [23]

Considering the enormous contribution companies make to the economic and social well-being of our society, directors at large companies have received increasing scrutiny in recent years.[24] Mongalo argues that better managed companies yield benefits for all, emphasising why corporate governance is pivotal in the modern world.[25] Typically, governance is thought to be the exclusive domain of the board of directors.[26]

In 2010, the Presidential Review Committee (hereafter 'the PRC') found that there is a lack of clarity on the roles of the executive authority, the board of directors and the CEO, in terms of the operational management of SOCs.[27] In 2010, the PRC found the legislative framework for SOCs to be inadequate and corrupted by 'conflicting roles and duplications.'[28]

The regulatory framework governing SOCs in South Africa has been criticised for its complex, fragmented, and contradictory nature.[29] Mongalo argues that the connection between the legal enforcement framework and the conventional role of directorial duties does not accurately reflect the reality of modern business. [30] The current framework is thus said to be out of date.[31] For these reasons, it may be difficult for directors to determine the limits within which their power may be exercised.[32]

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[22] De Visser J et al (2019) 10.
[23] A Report of the Public Protector South Africa (2016).
[24] Mofokeng T 'Good corporate governance affirms the board (led by the chairperson) as the focal point of governance and the courts have no mandate to undermine this principle' (2020) 6(1) *Journal of Corporate and Commercial Law & Practice* 176.
[25] Mofokeng T (2020) 176.
[26] Mofokeng T (2020) 67.
[27] De Visser J et al (2019) 20.
[28] De Visser J et al (2019) 20.
[29] Thabane T (2020) 87.
[30] Mongalo T 'Supervision of the Use of Corporate Power as The Ultimate Purpose of Directorial Duties and The Advisability of Corporate Law Enforcement in The Public Interest' (2017) 3(1) *Journal of Corporate and Commercial Law & Practice* 19.
[31] Mongalo T (2017) 19.
[32] Mongalo T 'A 'Fair and Reasonable Proposal' by the Board May Still Amount to a Breach of Duty to Exercise Directors' Powers for a Proper Purpose' (2019) 5(2) *Journal of Corporate and Commercial Law & Practice.*

The public sector has fallen victim to an increasing number of corporate crimes, as reflected in the state of capture report (2016), as well as the financial conundrums SOCs find themselves in. 'Corporate crime,' according to Hendrikse and Hefer, refers to criminal acts that are a result of the 'deliberate decision making by those occupying structural positions within the organisation,' that are intended to benefit themselves at the expense of the corporation and its stakeholders.[33] Hendrikse and Hefer argue that corporate crimes are often, and far too conveniently, dismissed as "market failure" or merely as a product of poor corporate governance practices.[34] They argue that there is 'something more fundamentally wrong' relating to business ethics, a failure of government and professional communities to adequately monitor and control corporate activities.[35] While corruption and corporate crime is a world-wide phenomenon, in 2019, South Africa was rated 55th on a list rating 90 countries in terms of their level of corruption.[36]

Most forms of corporate misconduct and malpractice are the result of decisions made by those occupying high-level, structural positions within the organisation. In terms of understanding the causes of, and the prevention of corporate misconduct and malpractice, it is vital to assess the effectiveness of the current legal framework governing the board of directors at SOCs.

In light of the abovementioned concerns, particularly the lack of clarity of directorial duties for the boards at SOCs and the 'outdated' legislative framework governing the sector, this paper essentially seeks to assess the extent to which the fiduciary duties imposed on the board of directors of SOCs, in terms of the current legal framework, facilitates good corporate governance in the sector of SOCs.

1.3 SIGNIFICANCE OF THE STUDY

The study of corporate governance generally refers to the manner in which companies are directed and controlled. [37] In the absence of a standard definition of corporate governance, the United Kingdom's Cadbury Report views corporate governance as "the system by which companies are directed and controlled."[38]

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[33] Hendrikse JW & Hefer L *Corporate Governance Handbook: Principles and Practice* 3 ed (2019) 86.
[34] Hendrikse JW & Hefer L (2019) 86.
[35] Hendrikse JW & Hefer L (2019) 86.
[36] Hendrikse JW & Hefer L 86. The "list" referred to is the Transparency International Corruption Perceptions Index 2019.
[37] Mongalo T 'The Emergence of Corporate Governance as Fundamental Research Topic in South Africa.' (2003) *South African Law Journal* 120(1) 173.
[38] Thabane T & Snyman-Van Deventer E (2018) 3.

The significance of this study is to contribute to the available resources and knowledge on corporate governance of SOCs in South Africa, while focusing on the ways in which the current framework for director duties facilitates good corporate governance.

While academics like Van der Linde have contributed to the study of corporate governance, by writing on the various instances of liability for directors, this study will draw on her findings, to further demonstrate the link between the framework for director duties, and the outcome of good corporate governance.[39] Van der Linde further argued that very little attention is given to the study of the general duties of directors, before her study on the instances of liability for directors has been analysed.[40]

The increasing interest in corporate governance, has brought to light certain aspects of management, such as the role of shareholders and the duties and responsibilities of directors..[41] Corporate governance emphasises direction and control, because flaws in respect of these two aspects can easily lead to the devaluation of a company and its shares.[42] The study of directorial duties at SOCs thus proves a significant study, in the larger scheme of the economy.

Elaborating on contributions by writers and academics such as Thabane, this thesis discusses whether the purpose of SOCs to advance economic growth, development, and transformation, is achieved by SOCs. Furthermore, this thesis investigates the role of the board of directors in executing the constitutional mandates imposed on SOCs, and whether the existing regulatory framework allows for coherent and coordinated compliance. There is a general consensus that the entire sector of SOCs is experiencing poor governance.[43] However, from a legal perspective, Thabane writes that these questions have received little to no attention in legal and governance discourse. In essence, this thesis adds to the available research on SOCs.

This thesis expands on Thabane's contributions regarding the public interest mandate of state-owned companies. It seeks to rethink the legal and regulatory framework, re-evaluate, and expand on directors' duties.

[39] Van Der Linde K 'The Personal Liability of Directors for Corporate Fault - An Exploration' (2008) *20 S. Afr. Mercantile L.J.* 439
[40] Van Der Linde K (2008) 440.
[41] Mofokeng T (2020) 66.
[42] Mofokeng T (2020) 66.
[43] Thabane T (2020) 15.

1.4 RESEARCH QUESTION AND SUB-QUESTIONS

To what extent do the fiduciary duties of directors of state-owned companies facilitate good corporate governance in South Africa?

i. What is good corporate governance?
ii. To what extent has South African SOCs exhibited signs of poor corporate governance?
iii. What are the fiduciary duties applicable to directors of SOCs?
iv. What is the influence of state ownership and the role of shareholders in the governance of SOCs and the exercise of director duties?
v. What are the functions of the board of directors in ensuring board effectiveness?
vi. To what extent does the current framework of SOC director duties in South Africa facilitate good corporate governance of such entities?

1.5 CHAPTER OUTLINE

One: Introduction

The first chapter provides the relevant background information and introduction to the study. It will be comprised of an explanation and breakdown of the problem statement, the significance of the study as well as a literature review. Chapter One will also include the sub-chapter covering research methodology.

Two: What is good corporate governance for South African State-Owned Companies?

Chapter two investigates what 'good governance' entails at SOCs in South Africa. Firstly, the chapter discusses the rise of corporate governance in South Africa. This chapter provides an overview of the concept of corporate governance and draws on instances of companies displaying good corporate governance. It analyses what governance legislation considers good corporate governance, in terms of SOCs. This chapter will discuss the corporate governance framework, by discussing the regulations and instruments facilitating corporate governance in South Africa. Furthermore, this chapter draws on examples of corporate governance failures in South Africa and discusses governance challenges faced by SOCs such as Denel, Eskom, and the South African Airways (SAA). Lastly, this chapter discusses the role of the shareholder in South Africa, as well as the role of the Memorandum of Incorporation at SOCs.

Three: The Functions and Effectiveness of an SOC's Board of Directors

This chapter provides a discussion on the functions of the board of directors, and the effectiveness of the board. In this regard, this chapter analyses the composition of the board, the financial management of the board, as well as the directors' role of oversight and board effectiveness. It also provides a discussion on the directors' decision-making function. The sub-topics in chapter three provide insight on issues such as fraud and negligence, conflicts of interest, and accounting irregularities. This chapter provides a relevant entry point to the further topics of discussion in this study.

Four: The Legislative Framework Governing Directors' Duties at SOCs

Chapter Four specifically discusses and analyses the legal duties and responsibilities applicable to directors of SOCs, as provided for in the legislative framework. This chapter draws on relevant common law principles, such as the 'secret profit rule,' and the 'corporate opportunity rule'. This chapter discusses the duties and liabilities imposed on directors in terms of the Companies Act, and specifically discusses the duty to disclose personal financial interests, the fiduciary duty to act in the best interests of the company, the duty of care, skill, and diligence, as well as the business judgement rule. Furthermore, this chapter draws on the duties imposed on the board in terms of the PFMA, as well as the recommendations in terms of King IV. Chapter Four essentially analyses the fiduciary duties of directors of SOCs and assesses the effectiveness of the framework governing the sector. This chapter seeks to determine if the framework requires more development.

Five: Conclusions and Recommendations

The final chapter of this thesis encompasses a summary of all conclusions made in the abovementioned chapters.

1.6 LITERATURE REVIEW

According to Adams, Hermalin and Weisbach, a director's duties include the duties to serve as advisors to the chief executive officer (CEO) and top management, to set strategy, assess management performance, guide the appointment and retrenchment of executive managers and promote the interests of shareholders.[44] Corporate law accepts shareholders as the only corporate constituents with the power to access remedies, specifically through derivative actions.[45] Mongalo argues that as a result, shareholders often hold an expectation of directors

[44] Adams RB, Hermalin BE & Weisbach MS 'The Role of Boards of Directors in Corporate Governance: A Conceptual Framework and Survey' (2010) 48(1) *Journal of Economic Literature* 58 – 107.
[45] Mongalo T (2017) 20.

to pursue their (the shareholders) short term interests, in the promotion of the 'best interests of the company.'[46] In terms of traditional corporate governance, companies were enabled to embark on an exclusive approach, with the main focus being on the shareholders as the owners of equity.[47] Traditional corporate law emphasises the role of directors and shareholders in managing the company's business.[48] This shareholder dominance seemed a legitimate approach in terms of traditional corporate law.[49] With the emergence of corporate governance reforms in the 21st century, words such as "accountability" and "responsibilities" became the buzz of the 21st century, as companies realised that the need for profit cannot be the only bottom line in the operation of a company.[50] Companies shifted emphasis to providing services, and it became apparent that the 'inclusive approach' represents the future of any company.[51] This approach recognises that stakeholders such as the customers, employees, suppliers, the environment and the community at large all need to be considered when developing the strategy of the company.[52] This approach is particularly important and beneficial in South Africa, given the peculiar socio-economic situation of the country.[53]

Mupangavanhu has contributed literature on specific director duties in terms of the Companies Act.[54] Coetzee and Van Tonder contributed a publication on the advantages and disadvantages of partial codification of directors' duties in the South African Companies Act 71 of 2008.[55] They argued that the release of the policy document of 2004 titled 'South African Company Law for the 21st Century: Guidelines for Corporate Law Reform,' recognised the need to bring South African company law in line with international trends, to reflect and accommodate the changing environment for businesses locally and internationally.[56]

In terms of specific duties assigned to the board of directors, Mongalo has emphasised the importance of the proper purpose rule.[57] In terms of this rule, directors may still be found to be in breach of this duty if they act for a collateral or improper purpose, irrespective of whether it

[46] Mongalo T (2017) 20.
[47] Mongalo T (2003) 190.
[48] Mongalo T (2003) 190.
[49] Mongalo T (2003) 190.
[50] Mongalo T (2003) 191.
[51] Mongalo T (2003) 191.
[52] Mongalo T (2003) 191.
[53] Mongalo T (2003) 191.
[54] Mupangavanhu BM 'Fiduciary duty and duty of care under companies act 2008: Does South African Law Insist on the Two Duties Being Kept Separate' (2017) 28(1) *Stellenbosch Law Review* 152.
[55] Coetzee L & Van Tonder JL 'Advantages and Disadvantages of Partial Codification of Directors' Duties in the South African Companies Act 71 of 2008' (2016) 41(2) *Journal for Juridical Science* 10.
[56] Coetzee L & Van Tonder JL (2016) 10.
[57] Mongalo T (2019) 41.

is for the best interests of the company.[58] Although courts have never been confronted with the situation of possible breach of the duty to exercise directors powers for proper purposes, the duty remains part of the law as one of the recognised fiduciary duties.[59] Mongalo has emphasised the importance of this particular duty, and defines the current culture of corporate governance as "follow the leader" or of leaders surrounding themselves with 'yes men' and 'yes women' in the boardroom.[60] Mongalo has further argued that the subjective duty of skill might be "overkill" in the South African context, as it exposes directors with enhanced skills to the potential risk of personal liability.[61] The socio-economic climate of South Africa demands the attraction and retention of talented directors to spur the much-needed economic growth in the country.[62] Mongalo argues that the objective standard for the duty of care and diligence is improved from the subjective standard and is in line with international trends in corporate governance.[63] He argues that the impact of the expansive role of directorial duties, and the modern perception of the purpose of corporate constituencies, allows both shareholders and non-shareholder corporate constituencies to blame the mismanagement of corporate assets on the failure of directors to manage a corporation.[64] Mongalo has provided valuable research and insights on director duties in South Africa, providing insight on directors' standards of conduct in terms of the Companies Act.[65]

Mofokeng has cautiously argued that South Africa has made significant progress in ensuring that private and public entities are kept abreast of the potential risk of not implementing and consistently monitoring the practice of good governance.[66] He argues that the Memorandum of Incorporation (MOI), Public Finance Management Act 1 of 1999 (PFMA), King Codes and the Companies Act all entail that the courts have no mandate to undermine good corporate governance.[67] He further substantiates this argument by adding that both public and private companies are creature of statutes, and when all internal company processes of dispute resolution have been fully exhausted, and failed, the courts have a mandate to intervene as final

[58] Mongalo T (2019) 41.
[59] Mongalo T (2019) 43 - This duty has been codified in s76(3)(a) of the Companies Act 71 of 2008.
[60] Mongalo T (2019) 41.
[61] Mongalo T (2019) 41.
[62] Mongalo T (2019) 41.
[63] Mongalo T 'Directors' Standards of Conduct Under the South African Companies Act and the Possible Influence of Delaware Law' (2016) 2(1) *Journal of Corporate and Commercial Law & Practice* 12.
[64] Mongalo T (2016) 12.
[65] Mongalo T (2016) 12.
[66] Mofokeng T (2020) 78.
[67] Mofokeng T (2020) 79.

arbiters.[68] Mofokeng has made a significant contribution to the study of corporate governance and director duties. He emphasises the significance of the duty to act in good faith and for a proper purpose (s76(3)(a))[69], and the duty to act in the best interests of the company (s76(3)(b)).[70] He argues that if directors have proper appreciation of these two duties, it will be easier for them to avoid breach of their duties and of corporate governance.[71]

Thabane has contributed research to the discourse on SOCs, as he sought to determine whether the purpose of SOCs to advance economic growth, development, and transformation, while upholding the public interest mandate, is achieved by state-owned companies. Thabane has argued that there is a general consensus that the entire sector has been experiencing poor governance, attributable to various factors.[72] He has further observed that questions relating to the decline in corporate governance has received little to no attention in legal and governance discourse.[73] This thesis seeks to expand on Thabane's contributions regarding the public interest mandate of state-owned companies, to rethink the legal and regulatory framework, re-evaluate, and expand on directors' duties. Thabane and Snyman-van Deventer argue that one of the challenges faced by SOCs in South Africa is the boards' lack of appreciation of corporate governance rules.[74] They argued that another challenge facing SOCs is the role of government as a single or dominant shareholder, which has resulted in substantial political interference in the running of SOCs.[75]

Unlike other public or private companies, SOCs are subjected to further regulations under the PFMA.[76] Mofokeng argues that the responsibility rests on the board of directors, as the custodian of corporate governance, rather than the courts, to ensure that SOCs are managed according to the requirements of the PFMA, as well as their founding legislation.[77]

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[68] Mofokeng T (2020) 79.
[69] The Companies Act 71 of 2008 s 76(3)(*a*):
> '(3) Subject to subsections (4) and (5), a director of a company, when acting in that capacity, must exercise the powers and perform the functions of director— (a) in good faith and for a proper purpose.'

[70] Act 71 of 2008 s 76(3)(b):
> '(3) Subject to subsections (4) and (5), a director of a company, when acting in that capacity, must exercise the powers and perform the functions of director— in the best interests of the company.'

[71] Mofokeng T (2020) 73.
[72] Thabane T (2020) 15.
[73] Thabane T (2020) 15.
[74] Thabane T & Snyman-Van Deventer E (2018) 21.
[75] Thabane T & Snyman-Van Deventer E (2018) 21.
[76] Mofokeng T (2020) 75.
[77] Mofokeng T (2020) 75.

In terms of the liability of the board of directors, Van der Linde argues that a systematic study on the nature and scope of directors liability for corporate conduct, has not yet been conducted.[78] Her article on the liability of directors sought to explore the different areas and bases of liability applicable to company directors in South Africa.[79] Her study is relevant to this thesis, as it informs the link between the legal duties of directors, and the consequences of those duties not being fulfilled. Van Der Linde argues that directors owe their companies a duty of good faith, duties of care and skill, even though these duties are not listed in statute.[80] Although compliance with the Codes are not legally enforceable, certain recommendations are binding on companies listed on the JSE, Van der Linde argues.[81] Van der Linde further observes that it appears that South African law has no problem attributing the same conduct to a company as to its directors.[82] For example, in some instances, a company may be held liable for wrongful conduct, however, proceedings may be instituted against directors independently.[83] However, strict liability is imposed sparingly.[84] In terms of the Companies Act, directors may face criminal liability.[85] Directors may also be held liable in terms of common law, civil or delictual liability. For example, in *Jowell v Bramwell-Jones & Others*[86] directors of the company were sued for economic loss incurred by their negligent conduct in performing the company's contractual obligations to the third party.[87] It was held that the question is rather whether the director owed the injured party a duty of care.[88] Most cases of liability for pure economic loss demands a restrictive approach.[89] 'A fear of limitless liability demands a restrictive approach,' Van der Linde proposes.[90] Directors also face other forms of liability such as environmental liability, tax liability, as well as liabilities in terms of social security law.[91]

This thesis seeks to contribute to the available literature and discourse on corporate governance in South Africa. While extensive research and literature has been conducted on this topic, this

[78] Van Der Linde K (2008) 439.
[79] Van Der Linde K (2008) 439.
[80] Van Der Linde K (2008) 440.
[81] Van Der Linde K (2008) 440.
[82] Van Der Linde K (2008) 442
[83] Van Der Linde K (2008) 442
[84] Van Der Linde K (2008) 442.
[85] Van Der Linde K (2008) 449.
[86] Van Der Linde K (2008) 449 - *Jowell v Branwell-Jones & Others* 1998 (1) SA 836 (W), on appeal at 2000 (3) SA 274 (SCA).
[87] Van Der Linde K (2008) 451.
[88] Van Der Linde K (2008) 451.
[89] Van Der Linde K (2008) 451.
[90] Van Der Linde K (2008) 451.
[91] Van Der Linde K (2008) 451.

thesis provides a focused study on the roles and responsibilities of the board of directors at state-owned companies. This thesis provides a study on the regulatory framework governing the duties of directors, to determine the extent to which this framework facilitates good corporate governance in SOCs.

Although extensive research on the topic of director duties in south Africa has been conducted and published, this thesis seeks to provide a reflection on the state of corporate governance at state owned companies. While various publications focus on certain aspects of director duties, such as the liability of directors, influences from international trends, and specific duties imposed on directors, this thesis takes a holistic approach to the duties imposed on the board of directors at SOCs, and seeks to determine the extent to which the legal framework in this regard facilitates 'good corporate governance' at state-owned entities. With current events unfolding in South Africa, this thesis seeks to reflect on current discourse on the topic of SOCs and provides a legal perspective on the current regulatory framework governing the sector.

1.7 RESEARCH METHODOLOGY

This paper will be theoretically based and will analyse both primary and secondary works. Legislation, case law, corporate governance codes and regulations make up the primary works. Journal articles, news articles, theses and books make up the secondary works used. These sources provide the legislative framework governing state entities and provides insight from other academics in the field which informs this study.

CHAPTER TWO

WHAT IS 'GOOD' CORPORATE GOVERNANCE FOR SOUTH AFRICAN STATE-OWNED COMPANIES?

2.1 INTRODUCTION

The board of directors is the custodian of corporate governance in a company.[1] In order to understand the extent to which directors, and the fiduciary duties imposed on directors, facilitates good corporate governance at state-owned companies, one must first develop a thorough understanding of the concept of corporate governance.

This chapter seeks to provide insight on what corporate governance entails, particularly within state-owned companies. This chapter describes the history of the development of corporate governance as a global concept and discusses the ways in which it has been implemented in South Africa. Considering the unique socio-economic dynamics in South Africa, as well the history of economic exclusionary practices, the application of corporate governance in South Africa has to be tailored to the South African economy and corporate sphere.

Thus, this chapter discusses the regulations and instruments in place to facilitate corporate governance in South Africa, particularly the King Codes and relevant legislation. This chapter discusses the development of various instruments established to facilitate good corporate governance at South African corporations over the years. It identifies codes that have been developed but never encoded and provides an overview of the 'hybrid' system of governance in South Africa's corporate world.[2]

Furthermore, this chapter briefly assesses the ways in which corporate governance principles are implemented and upheld in South African state-owned companies. It draws on past instances in which SOCs have displayed poor corporate governance practices, which have resulted in serious consequences including seeking financial bailouts from National Treasury or threatening that salaries would not be able to be paid due to financial strife.

[1] Mofokeng T 'Good Corporate Governance Affirms the Board (Led by the Chairperson) as the Focal Point of Governance and the Courts Have no Mandate to Undermine this Principle' (2020) 6(1) *Journal of Corporate and Commercial Law & Practice* 75.
[2] King ME 'The Synergies and Interaction Between King III and the Companies Act 71 of 2008' (2010) *Acta Juridica* 447.

The influence of SOCs on the economy at large, is emphasised in this chapter. For this reason, since the emergence of corporate governance as a concept, it has been emphasised that large corporations should be 'good corporate citizens.'[3]

This is why understanding the concept of corporate governance lays the foundation for further discussion within this thesis. Understanding that the board of directors is the custodian for corporate governance at a corporation, ties in with the fundamental question posed by this thesis, which seeks to determine the extent to which the duties of the directors of SOCs actually facilitates good corporate governance.

2.2 THE RISE OF CORPORATE GOVERNANCE IN SOUTH AFRICA

It has been argued that corporate governance has been practiced for 'as long there have been corporate entities,' however the study of the subject is less than half a century old.[4] The construct of corporate governance was for the first time institutionalised in South Africa in 1994, with the publication of the King Report on Corporate Governance.[5]

In the 1980s, the main emphasis in corporate governance was on companies enhancing the return on capital, as stakeholder concerns were overshadowed by market-driven and growth-orientated attitudes.[6] During this time, the responsibility to increase shareholder value was emphasised, while safeguards against the abuse of power by directors were still lax.[7] The shortcomings of the traditional corporate governance system became exposed at the end of the 1980s, as irregular and unjustified payments to directors ensued.[8] After a series of corporate scandals in the United Kingdom (UK), the London Stock Exchange established the Cadbury Commission and released 'The Report of the Committee on the Financial Aspects of Corporate Governance' in 1992.[9] The 'Cadbury Report' emphasised the importance of independent, non-executive directors on the board, as well as the implementation of board committees such as nomination and remuneration committees for effective corporate governance.[10] The Cadbury

[3] Mofokeng T (2020) 67.
[4] Mongalo T 'The Emergence of Corporate Governance as Fundamental Research Topic in South Africa.' (2003) 120(1) *South African Law Journal* 178.
[5] Mofokeng T (2020) 67.
[6] Mongalo T (2003) 186.
[7] Mongalo T (2003) 186.
[8] Mongalo T (2003) 187. The case that sparked the corporate governance debate was that of *Guinness Plc v Saunders,* in which the board of directors of Guinness agreed to pay £5.2 million to one director for his services in connection to one transaction. It later transpired that the director had a financial interest in the transaction and the company claimed recovery of the money received.
[9] Mongalo T (2003) 188.
[10] Cadbury, A. *Report of the Committee on the Financial Aspects of Corporate Governance* (1992).

Report was the first of its kind in the world, and became significant in influencing thinking worldwide. In fact, South Africa followed the model of the Cadbury Report.[11] As a result of the Cadbury Report and developments in the corporate world, the Institute of Directors in Southern Africa (IoDSA) was influenced to form the King Committee.[12] The Committee was established to review governance in the corporate world, and make recommendations to improve the standard of corporate governance.[13] This led to the Code of Corporate Practices and Conduct issued by the King Committee.[14] The King Committee sought to make recommendations to the Johannesburg Stock Exchange (JSE), which the JSE has implemented and now form part of the JSE's Listing Requirements.[15]

Before 1994, all aspects of socio-economic and political life were governed by discriminatory laws, including the corporate sphere of economic activity.[16] With the aim of redressing past inequities, the new South African democratic government of 1994, undertook to establish programmes aimed at giving marginalised citizens access to means of production and to the economy, such as the Reconstruction and Development Programme (RDP).[17] However, since the inception of democracy in South Africa, the new government had inherited underperforming SOCs from the previous administration.[18]

At the time of the negotiations for a democratic South Africa, corporate governance reforms around the world were in their 'embryonic stage,' according to Mongalo, following the recommendations of the Cadbury Report of 1992.[19] Those charged with the responsibility of reviewing corporate governance following changes to the corporate sphere, realised they could not turn a blind eye to the political developments in South Africa.[20] Subsequently, the 1994 King Report dedicated a whole chapter to affirmative action.[21] The first King Reports considered the implementation of affirmative action as a practice of good corporate governance.[22] According to Mofokeng, the King Reports codified the behavior expected from

[11] Mofokeng T (2020) 67.
[12] Mofokeng T (2020) 67.
[13] Mongalo T (2003) 120.
[14] Mongalo T (2003) 175.
[15] Mongalo T (2003) 175. See schedule 22 of the JSE Listing Requirements.
[16] Mongalo T (2003) 189.
[17] Mongalo T (2003) 189.
[18] Thabane T & Snyman-Van Deventer E 'Pathological Corporate Governance Deficiencies in South Africa's State-Owned Companies: A Critical Reflection' (2018) 21 *PER / PELJ* 3.
[19] Mongalo T (2003) 189. Mongalo refers to the Cadbury report once again: Cadbury, A. *Report of the Committee on the Financial Aspects of Corporate Governance* (1992).
[20] Mongalo T (2003) 189.
[21] Mongalo T (2003) 189.
[22] Mongalo T (2003) 189.

companies, being to protect and enhance shareholder value, and signaled a new era in governance.[23] The first governance codes focused on the form rather than the function of a corporation, particularly emphasising the importance of independent non-executive directors, the separation of the role of the chairperson and the chief executive officer (CEO), and the importance of dedicated committees of non-executive directors to deal with auditing and remuneration matters.[24] A revised King Report was published in 2002, known as the King II.[25] King III was released in 2009, and King IV in November 2016.[26] Mofokeng highlights the 'groundbreaking' impact of the King IV, arguing that it confirmed South Africa as a global leader in governance thinking, at the forefront of other nations adopting superior governance standards.[27] Subsequent voluntary mechanisms were established and enforced to further facilitate good corporate governance in South Africa, such as the Protocol on Corporate Governance in the Public Sector (the 'Protocol').[28] Governance codes have evolved over time, for example the King III placed emphasis on the growing public awareness of sustainability issues, which has further gained international importance since its publication.[29] The King IV emphasises the necessity of corporate governance for all organisations, including non-profit companies, private companies, as well as all public companies, listed or not, state-owned companies, municipalities and retirement funds.[30]

2.3 REGULATIONS AND INSTRUMENTS FACILITATING CORPORATE GOVERNANCE IN SOUTH AFRICA

Corporate governance lies at the heart of a corporate entity, guiding relationships between shareholders, directors, management, employees and other stakeholders, and is not a merely business tool.[31] Implementing good corporate governance practices has become increasingly important as a result of globalisation and the need to level the international playing field by implementing international rules governing business.[32] This is particularly important in terms of international accounting and reporting standards, as one of the constituents of corporate

[23] Mofokeng T (2020) 67.
[24] Mofokeng T (2020) 67.
[25] Mofokeng T (2020) 67.
[26] Mofokeng T (2020) 67.
[27] Mofokeng T (2020) 67.
[28] Thabane T & Snyman-Van Deventer E (2018) 11 – The 'Protocol' refers to the Department of Public Enterprises Protocol on Corporate Governance (2002).
[29] King ME (2010) 451.
[30] Hendrikse JW & Hefer L (2019) 126.
[31] Hendrikse JW & Hefer L (2019) 107.
[32] Hendrikse JW & Hefer L (2019) 107.

governance.[33] As a result, certain mechanisms are put in place to ensure and assist in facilitating corporate governance in South Africa.

The Constitution of South Africa serves as a fundamental instrument facilitating corporate governance in SOCs in South Africa.[34] In terms of section 55(2) of the Constitution, the National Assembly is required to provide a mechanism to ensure that all national executives are accountable to it, and to maintain oversight over national executive authorities.[35] As a result, the National Assembly maintains oversight over 35 national departments and over 200 state-owned companies.[36] Portfolio committees are established to assist the National Assembly with this enormous task of oversight.[37] The Standing Committee on Public Accounts (SCOPA) is established to audit the reports submitted by the Auditor General (AG), whereas Portfolio Committees review the non-financial annual reports of the departments and SOCs.[38]

The Companies Act 71 of 2008 ('the Act') for the first time incorporates issues of corporate governance into South African legislation.[39] King defines the system of governance in South Africa as a hybrid system, partly legislated and partly voluntary.[40] However, he maintains that the law and the practice of how companies are directed and managed should never be looked at separately.[41] The Act sets the framework in which the company operates and the recommended practices in the King codes are a guide for directors as to how they should direct the business of the company and make decisions on behalf of the company.[42] King further points out that the Act and the King codes complement each other.[43]

[33] Hendrikse JW & Hefer L (2019) 107.
[34] Constitution of the Republic of South Africa, 1996.
[35] De Visser J, Komote M & Muntingh L 'The Legal Framework for the Appointment and Dismissal of SOE Board Members' *DOI* 4 April 2019 5.
Constitution of the Republic of South Africa, No. 108 of 1996 s55(2) reads: 'The National Assembly must provide for mechanisms-
(a) to ensure that all executive organs of state in the national sphere of government are accountable to it; and
(b) to maintain oversight of-
(i) the exercise of national executive authority, including the implementation of legislation; and (ii) any organ of state.'
[36] De Visser et al (2018) 5.
[37] De Visser et al (2018) 5.
[38] De Visser et al (2018) 5.
[39] King ME (2010) 446 – 'the Act' refers to the Companies Act 71 of 2008.
[40] King ME (2010) 447.
[41] King ME (2010) 447.
[42] King ME (2010) 447.
[43] King ME (2010) 447.

SOCs are creatures of statute, falling within the ambit of the Companies Act.[44] SOCs are also run according to the Public Finance Management Act (The Public Finance Management Act 1 of 1999).[45] In addition, SOCs have their own founding legislation, determining their specific public mandates.[46] These companies are also required to comply with the Protocol on Corporate Governance in the Public Sector,[47] as public-sector corporations themselves.[48] In terms of the Companies Act, an SOC must have a board that is responsible for exercising all the powers conferred on it, and perform the functions of the company, except where limited by the Act itself or by the company's Memorandum of Incorporation (MOI).[49] Thabane and Snyman van Deventer emphasise the importance of this provision in light of the 'political meddling' experienced in many SOCs, from their shareholding Ministers.[50] The Companies Act further provides for "accountability and transparency," which entails that every public company and state-owned company must have a company secretary and an audit committee, as well as an external auditor.[51] Most SOCs are audited by the Auditor-General of South Africa. However, at section 84(3)(*b*) the Act states that state-owned companies are not required to appoint an auditor for any financial year to conduct an audit of that enterprise.[52] In terms of the Companies Act, SOC directors are required to act in good faith and for proper purpose, in the best interests of the company, with the degree of care, skill and diligence that is expected of them.[53] Nonetheless, Thabane and Snyman van Deventer maintain that it is arguable whether

[44] Thabane T & Snyman-Van Deventer E (2018) 3.
[45] Thabane T & Snyman-Van Deventer E (2018) 3.
[46] Thabane T & Snyman-Van Deventer E (2018) 3.
[47] Thabane T & Snyman-Van Deventer E (2018). 9.
[48] Thabane T & Snyman-Van Deventer E (2018) 9.
[49] Memorandum of Incorporation is defined in the Companies Act (71 of 2008), as 'the document, as amended from time to time that sets out rights, duties and responsibilities of shareholders, directors and others within and in relation to a company, and other matters as contemplated in section 15…'
[50] Thabane T & Snyman-Van Deventer E (2018) 9.
[51] In addition to the 'Transparency, accountability and integrity' rules (from section 23 to 34) of the Companies Act (71 of 2008), State-Owned Companies are obliged to comply with the extended accountability requirements set out in Chapter Three of the Act.
[52] Section 84 (3)(b), however, states:
'That despite the provisions of this Chapter (Three), the state-owned company is not required to appoint an auditor for any financial year in respect of which the Auditor-General has elected, in terms of the Public Audit Act, 2004 (Act No. 25 of 2004), to conduct an audit of that enterprise.'
[53] Section 76(3) states:
'A director of a company, when acting in that capacity, must exercise the powers and perform the functions of director-
a) In good faith and for a proper purpose;
b) In the best interests of the company; and
c) With the degree of care, skill and diligence that may reasonably be expected of a person –
i) Carrying out the same functions in relation to the company as those carried out by that director; and
ii) Having the general knowledge, skill, and experience of that director.

these crucial provisions are observed, given the laxity displayed by some directors of SOCs in the recent past.[54]

As previously mentioned, SOCs are further subject to their founding legislation, which is entity-specific and allows for their establishment, control, powers, and function.[55] For example, the SABC is established in terms of the Broadcasting Act, and the South African Airways (SAA) by the SAA Act.[56]

Voluntary codes which aid in facilitating corporate governance in companies, include the Protocol on Corporate Governance in the Public Sector (The Protocol).[57] The Protocol was first established in 1999 to instil good corporate governance in SOCs, as part of the overall strategic vision to restructure SOCs.[58] The Protocol was revised in 2002 to include the principles in the King II report, and was adopted by Cabinet in 2003.[59] The Protocol has not been enacted or updated since then, but remains an applicable code of best practice for all public entities listed in the PFMA.[60] The Protocol provides guidance to various entities, including SOCs, and takes into account the unique mandate for SOCs, which includes government's socio-economic objectives.[61] Whereas the King Code makes for general application, the Protocol was specifically developed to cover governance issues specific to the public sector.[62] However, the two should be read together as the Protocol merely seeks to amplify the King Code, rather than to supersede or contradict it.[63] The Protocol remains cognisant of the financial, reputational, political and operational risks that SOCs face, as well as the high standards of corporate governance they must adhere to.[64] The Protocol further acknowledges that an SOCs performance is dependent on its board's capabilities and performance, and recommends that the shareholder should ensure that the board is properly constituted with individuals who possess integrity and accountability.[65] As a fundamental basis of corporate governance, the

[54] Thabane T & Snyman-Van Deventer E (2018) 9.
[55] Thabane T & Snyman-Van Deventer E (2018) 11.
[56] Broadcasting Act 4 of 1999 and South African Airways Act 5 of 2007; Thabane T & Snyman-Van Deventer E (2018) 11.
[57] De Visser et al (2018) 8.
[58] De Visser et al (2018) 8.
[59] De Visser et al (2018) 9.
[60] De Visser et al (2018) 9.
[61] Thabane T & Snyman-Van Deventer E (2018) 13.
[62] Thabane T & Snyman-Van Deventer E (2018) 13.
[63] Thabane T & Snyman-Van Deventer E (2018) 13.
[64] Thabane T & Snyman-Van Deventer E (2018) 14.
[65] Thabane T & Snyman-Van Deventer E (2018) 14.

Protocol provides that the board must effectively and efficiently control and head the corporation.[66]

The King Codes facilitate corporate governance by providing a detailed guideline to companies and other entities.[67] However, the King Codes are voluntary in nature and only binding on companies listed on the Johannesburg Stock Exchange (JSE).[68] The King IV replaced the King III in its entirety, in April 2017 when it became effective.[69] King IV includes a specific sector supplement for the governance of SOCs.[70] According to Hendrikse and Hefer, King IV serves as the benchmark for corporate governance in South Africa.[71] One of the most important innovations in the King IV, according to De Visser et al, is the formal recognition of the fact that different types of enterprises may require different governance frameworks, and thus recognises that certain aspects of the King IV are more relevant to specific sectors than others.[72] While the King IV highlights the importance of government as stakeholders in SOCs, it also highlights the 'triplicate stakeholder role' of government, as one of the most problematic aspects of the governance of SOCs. [73]

Legislation supersedes the guidelines provided in the form of instruments such as the King Codes.[74] While legislation remains supreme, De Visser et al note the lack of a uniform regulation of national SOCs in South Africa.[75] They argue that the lack of a uniform regulation of national SOCs causes uncertainty as a result of overlapping and conflicting legislative regimes.[76] This uncertainty is partly evident in the current state of state-owned companies in South Africa.

It is evident that the system facilitating corporate governance in South Africa is extensive, ranging from hard regulation in the form of various legislation to soft regulation in the form of voluntary applicable codes. "Good corporate governance" in essence would be companies putting into practice the instruments available to facilitate their governance. Instances of company failures attributed to corporate governance failures indicate that these instruments are

[66] Thabane T & Snyman-Van Deventer E (2018) 14.
[67] De Visser et al (2018) 9.
[68] De Visser et al (2018) 9.
[69] De Visser et al (2018) 9.
[70] De Visser et al (2018) 9.
[71] Hendrikse JW & Hefer L *(*2019) 120.
[72] De Visser et al (2018) 27.
[73] De Visser et al (2018) 27.
[74] De Visser et al (2018) 9.
[75] De Visser et al (2018) 31.
[76] De Visser et al (2018) 9.

either ineffective in facilitating good corporate governance, or do not provide sufficient tools to ensure accountability for irregular business activities. The concept of good corporate governance is further discussed in the following sub-chapter.

2.4 WHAT IS GOOD CORPORATE GOVERNANCE?

Corporate governance is understood to be the way in which companies are directed and controlled.[77] According to Mofokeng, direction and control is particularly important: he argues that governance flaws in this respect can lead to the devaluation of a company and by extension, its shares.[78] In a broader sense, he adds that corporate governance is used to define the structure, relationships, control mechanisms and corporate objectives of a corporation.[79] Mofokeng stresses 'ethical behavior' in corporate governance, arguing that financial institutions, and even suppliers, would prefer to engage with organisations that display a strong ethical approach.[80] Structure and control mechanisms of a corporation must be in place, and well understood, by everyone in the company, to display said ethical approach.[81]

The purpose behind corporate governance regulation is to ensure that companies are managed like good corporate citizens, and simultaneously to ensure that shareholders' investments are protected.[82] Notwithstanding the main objectives of a firm to attract capital, deliver efficient performance, comply with the law and remain profitable for the benefit of shareholders, companies remain creatures of statute, and the governing body must always ensure that the board complies with regulatory requirements to enforce good corporate governance.[83]

Thabane and Snyman van Deventer weigh in on the discourse on corporate governance, particularly in terms of state-owned companies. They draw on the definition of corporate governance, posed by Du Plessis et al in 2011, which reads:

> '(Corporate governance is) The process of controlling management and of balancing the interests of all internal stakeholders and other parties who can be affected by the corporation's

[77] Mofokeng T (2020) 66. This is the most well-known definition of corporate governance, deriving from the Cadbury Committee, which was set up in the United Kingdom in 1991: Cadbury, A. *Report of the Committee on the Financial Aspects of Corporate Governance* (1992).
[78] Mofokeng T (2020) 66.
[79] Mofokeng T (2020) 66.
[80] Mofokeng T (2020) 67.
[81] Mofokeng T (2020) 67.
[82] Mofokeng T (2020) 67.
[83] Mofokeng T (2020) 67.

conduct in order to ensure responsible behaviour by corporations and to achieve the maximum level of efficiency and profitability for a corporation.'[84]

In terms of SOCs, corporate governance refers to the process of governing the company with the same control of management as profit-seeking companies, although they have social or public goals, which other companies potentially may not have.[85]

According to Mongalo, a regulated corporate sphere is justified considering that corporations, especially those listed on the Johannesburg Stock Exchange (JSE), predominantly make up the business structure that dominates economic life in South Africa.[86] King has argued that companies are far greater agents for change than governments, and thus have a responsibility to their stakeholders to act and be seen as good corporate citizens.[87] This is a good point because, given the context of the socio-economic history of South Africa, these corporations should be effectively utilised to effect societal change. I agree that corporations should take on their responsibility as 'agents for change,' by behaving as good corporate citizens. This responsibility rests heavier on state-owned companies, in consideration of the impact of these companies on the economy, service delivery, and creation of employment. Mofokeng argues that the amount of capital and resources that these companies contribute to the economy, constitutes a great proportion of the country's gross domestic product.[88] Thus, further emphasising the need for a regulated corporate sphere, particularly at state-owned companies.

Evidently, governance is delegated by law, the company's owners including its shareholders, and shared by the boards and in some measure with the company's management.[89] However, governance is generally thought to be the domain of the board of directors.[90] Mofokeng refers to the governing body of a company as the 'heartbeat' of good corporate governance, arguing that the collapse of governance at board level will inevitably impact the entire organisation.[91] He thus argues that the governing body should exercise and implement its leadership role by setting strategic direction, approving policy, overseeing and monitoring the execution by

[84]Thabane T & Snyman-Van Deventer E 'Pathological Corporate Governance Deficiencies in South Africa's State-Owned Companies: A Critical Reflection' (2018) 21 *PER / PELJ* 3, citing Du Plessis JJ, Hargovan A & Bagaric M *Principles of Contemporary Corporate Governance* 2nd ed (2011).
[85] Thabane T & Snyman-Van Deventer E (2018) 3.
[86] Mongalo T (2003) 175.
[87] King ME (2010) 449.
[88] Mongalo T (2003) 175.
[89] Mofokeng T (2020) 68.
[90] Mofokeng T (2020) 68.
[91] Mofokeng T (2020) 68.

management, and further ensuring accountability for organisational performance through reporting and disclosure.[92]

The board of directors is tasked with ensuring that the main principles of the King IV are implemented throughout the company.[93] Mongalo agrees that emphasis is placed on the role played by directors in terms of incorporating the standards of corporate governance.[94] The reason for the emphasis on and scrutiny of the board of directors, is the enormous contributions by these companies to the economic and social wellbeing of our society.[95] According to Mongalo, better managed companies yield benefits for all, which is why corporate governance is undeniably pivotal in the modern world.[96]

Hendrikse and Hefer affirm these arguments, as they contend that the purpose of corporate governance is to match business behaviour and management conduct with the company's intentions, mission and objectives.[97] They admit that corporate failure in businesses caused by fraud, accounting irregularities and dishonest management, amongst other causes, is a global reality.[98] They propose that corporate governance is the global solution to such corporate crimes, and further argue that this may require an adaptation to the unique circumstances of different countries, economies and business models.[99]

Corporate governance affects every aspect of a company, including the structure, relationships, and objectives of the company. Since direction and control are the foundations of corporate governance, a company displays good corporate governance when it operates successfully under the direction and control of the custodian who emphasises and implements ethical practices. The notion that corporate governance ensures that companies are managed like good corporate citizens, further captures the essence of good corporate governance. A company should aim to maintain a balance between protecting shareholders' interests by remaining profitable and conducting business in an ethical manner as good corporate citizens. As mentioned earlier, companies are great agents for change, given their large contributions to society. If companies remain cognisant of their corporate responsibility, while practically and

[92] Mofokeng T (2020) 68.
[93] Mofokeng T (2020) 68.
[94] Mongalo T (2003) 176.
[95] Mongalo T (2003) 176.
[96] Mongalo T (2003) 176.
[97] Hendrikse JW & Hefer L *Corporate Governance Handbook* 3 ed (2019) 121.
[98] Hendrikse JW & Hefer L *(*2019) 121.
[99] Hendrikse JW & Hefer L *(*2019) 121.

in good faith complying with the mechanisms in place to facilitate corporate governance, 'good corporate governance' would ensue.

In most cases, where companies have displayed unethical behaviour, as well as poor direction and control mechanisms, corporate failures have ensued. The following sub chapter describes cases of corporate governance failures in South Africa.

2.5 CORPORATE GOVERNANCE FAILURES IN SOUTH AFRICA

In light of the abovementioned mechanisms facilitating corporate governance in companies, it is imperative for this study to discuss the state of corporate governance among SOCs in South Africa. This section of the study draws on cases of corporate governance failures in South Africa, both in the private sector as well as in state owned companies.

As a starting point, given recent discourse in the country, and developments within the company, the state of governance at Eskom SOC Ltd (Eskom) will first be discussed. Eskom has a history of corruption and irregular expenditure, as former Chief Executive Officer (CEO) Andre de Ruyter reported that the parastatal was losing about R1-billion a month due to corruption and theft.[100] To further illustrate critical governance issues at the parastatal, over the last ten years, Eskom has had ten different CEOs or acting CEOs - indicating a fundamental governance instability issue at the company.[101] According to Bowman, the crisis at Eskom has simultaneously been an operational, financial and political crisis.[102]

The most prominent crisis at Eskom is the widespread power outages (known as 'load-shedding') in 2008, 2014 to 2015, and 2018 to 2023.[103] Loadshedding has resulted in far-reaching disruptions to economic activity.[104] Further to the operational and financial crisis, Eskom has been at the centre of political conflicts over procurement spending, the control of Eskom's board, as well as the 'state capture' controversies.[105] Bowman believes that these factors collectively have destabilised Eskom's corporate governance.[106] Bowman further

[100] Patel O 'The State of Disaster that is Eskom' *Mail and Guardian* 11 April 2023 available at *https://mg.co.za/thoughtleader/opinion/2023-04-11-the-state-of-disaster-that-is-eskom/* (accessed 20 April 2023).
[101] De Visser J, Komote M & Muntingh L 'The Legal Framework Governing the Appointment and Dismissal of Board Members and Executives of Eskom, Prasa and the SABC' *DOI* 4 July 2019 (hereafter *Appointment and Dismissal of Board Members)* 19.
[102] Bowman, A. 'Parastatals and Economic Transformation in South Africa: The Political Economy of the Eskom Crisis' (2020) 119 *African Affairs* 396.
[103] Bowman A (2020) 396. Bowman's article was published in 2020, and thus he records loadshedding up until 2020, although it has continued on until 2023.
[104] Bowman A (2020) 396.
[105] Bowman A (2020) 396.
[106] Bowman A (2020) 396.

captures the extent of the effect of corporate governance failure at an SOC such as Eskom, by arguing that the mounting debt burden at the company has hindered fiscal capacity in the context of economic stagnation, and that the cost and unreliability of electricity has damaged the competitiveness of South Africa's pivotal energy manufacturing and mining industries.[107] Bowman defines the crisis at Eskom as 'extreme dysfunctionality,' derived from long-running contestation of the company.[108]

According to Skae, Eskom's board, chairperson and the responsible Minister have failed in their duties to serve Eskom, and they have failed the country.[109] Skae argues that corporate governance rules designed to manage conflicts of interest, were simply disregarded.[110] He highlights the provision in the Companies Act that prescribes what a director may or may not do if they have a personal financial interest in a matter, arguing that this provision was also disregarded.[111] De Visser et al argue that the 'governance fiasco' at Eskom serves as evidence of the problems that can arise from the convoluted arrangement between government and the board.[112] They argue that governance problems arise where government is the shareholder, policy maker and regulator.[113] Skae agrees that there is too much interference from outsiders at Eskom, and argues that this interference is for nefarious reasons.[114] He argues that interference undermines the way the business should be run, erodes confidence and serves as fertile ground for conflicts of interest to grow.[115]

At the South African Broadcasting Corporation (SABC), governance instability is also evident in the high turnover rate of chief accounting officers and other executive members.[116] The corporation has received several cash injections from its shareholder in order to continue delivering services, due to underperformance at the company.[117] The main trends of institutional weaknesses found at the SABC include the mismanagement of funds, the lack of accountability mechanisms and controls, the lack of skilled personnel in strategic positions, as

[107] Bowman A (2020) 396.
[108] Bowman A (2020) 396.
[109] Skae O 'Eskom: So many red flags it's hard to know where to start' available at *https://www.ru.ac.za/perspective/2017archives/eskomsomanyredflagsitshardtoknowwheretostart.html* (accessed 20 April 2023) (hereafter *Eskom: So Many Red Flags)*
[110] Skae O *Eskom: So Many Red Flags* (2017).
[111] Skae O *Eskom: So Many Red Flags* (2017).
[112] De Visser et al (2018) 19.
[113] De Visser et al (2018) 20.
[114] Skae O *Eskom: So Many Red Flags* (2017).
[115] Skae O *Eskom: So Many Red Flags* (2017).
[116] Thabane T & Snyman-Van Deventer E (2018) 4.
[117] Thabane T & Snyman-Van Deventer E (2018) 4.

well as a lack of determination by management to follow up on findings and decisions made.[118] In 2020, the Daily Maverick reported that senior and middle management constitute 30 percent of the staff, but their salaries made up 44% of the compensation, with many employees at the SABC earning more than R1million per year.[119] Majozi observed that conflict between the board and the shareholder representative indicates weak oversight and a lack of leadership, which leaves the company in a constant state of uncertainty.[120] Financial statements from 2014/15 reported a loss of roughly R395 million, while at the same time the Chief Operating Officer (COO) received a salary increase from R2.8 million to R3.7 million.[121] One pivotal incident indicating the state of corporate governance at the SABC, was in 2015 when the former Minister of Communications amended the SABC's Memorandum of Incorporation (MOI), conferring on herself the authority to appoint, suspend or even dismiss the CEO, Chief Financial Officer (CFO) and COO.[122] This raised the question of the division of power between the SABC board and the shareholder.[123] Mofokeng argues that a lack of legitimacy at the SABC has negatively impacted on the company's corporate governance.[124] These incidents indicate governance instability at board level.

The Passenger Rail Agency of South Africa (PRASA) is another example of a South African SOC suffering from poor governance practices, as the company has been subject to a number of corruption investigations.[125] In November 2017, then Minister of Transport, Joe Maswanganyi, said these investigations are so many, that government cannot even keep track of them.[126] By September 2018, the annual report for PRASA indicated that the company was on the brink of financial collapse.[127] De Visser et al argue that the levels of underperformance at PRASA could be attributed to years of governance instability.[128] Interim CEO of the corporation, Sibusiso Sithole, confirmed De Visser's contention, as he ascribed the corporation's challenges to governance issues and dysfunctional internal controls.[129] To

[118] Maphetshana B *Corporate Governance Compliance at the South African Broadcasting Corporation (SABC)* (Unpublished Master of Management thesis, University of the Witwatersrand, 2016) 7.
[119] Majozi Z 'SABC Crisis: The Public Broadcaster is sitting on its Solutions' *Daily Maverick* 24 January 2021 available at *https://www.dailymaverick.co.za/opinionista/2021-01-24-sabc-crisis-the-public-broadcaster-is-sitting-on-its-solutions/* (accessed 20 April 2023).
[120] Majozi Z *Daily Maverick* (2021).
[121] Thabane T & Snyman-Van Deventer E (2018) 4.
[122] Thabane T &Snyman-Van Deventer E (2018) 5.
[123] Thabane T & Snyman-Van Deventer E (2018) 5.
[124] Mofokeng T (2020) 69.
[125] De Visser et al (2018) 15.
[126] De Visser et al (2018) 15.
[127] De Visser et al (2018) 15.
[128] De Visser et al (2018) 15.
[129] De Visser et al (2018) 15.

illustrate the extent of the instability at PRASA, the company had eight interim boards between August 2014 and April 2018, with seven acting CEOs between 2014 and June 2018.[130]

For a more holistic perspective on corporate governance failures in South Africa, as it pertains to the private sector, the 'Steinhoff saga' provides great insight into what may transpire when a company neglects to observe proper corporate governance systems. The Steinhoff saga has been one of the biggest cases of corporate fraud in South African business history, according to De Klerk et al.[131] De Klerk et al argue that much can be learned from business success stories, but sometimes business failures are even more revealing.[132] They argue that the Steinhoff cases reminds us that corruption is not only to be found in government and the public sector, but is commonplace in the private sector as well.[133] Following a series of large-scale business acquisitions, both nationally and internationally, Steinhoff had managed to climb to the JSE Top 40 index.[134] The empire however saw a major collapse on the eve of 5 December 2017 when the Steinhoff CEO, Markus Jooste, stepped down from his position with immediate effect, with the board announcing that the company had become aware of 'accounting irregularities.'[135] Following the initial announcements by the company, the company's share price dropped by 85 percent.[136] In terms of compliance, De Klerk et al found that Steinhoff appeared to comply with all legal and listing requirements in its various jurisdictions, however this created a false sense of security for investors and other stakeholders.[137] They argue that this points to the risks associated with a tick-box compliance system, that is not underpinned by an ethical commitment to respect and abide by regulations.[138] De Klerk et al reflect on whether or not there may have been a transparency problem at the company. The Steinhoff saga caused De Klerk et al to ponder whether ethical behaviour can be legislated.[139]

In light of these governance issues, Hendrikse and Hefer have identified that in most cases of 'corporate collapse', the root cause is a conflict between the objectives of the company and the custodians of the company's assets and undertaking, i.e. the directors and senior executives.[140]

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[130] De Visser et al (2018) 15.
[131] De Klerk M, Hamilton B and Malan D 'Business Perspectives on the Steinhoff Saga' 2018 *University of Stellenbosch Business School* 3.
[132] De Klerk et al (2018) 3.
[133] De Klerk et al (2018) 3.
[134] De Klerk et al (2018) 5
[135] De Klerk et al (2018) 5
[136] De Klerk et al (2018) 5
[137] De Klerk et al (2018) 16
[138] De Klerk et al (2018) 17.
[139] De Klerk et al (2018) 5.
[140] Hendrikse JW & Hefer L (2019) 86.

This has resulted in corporate crimes in various forms, including falsification of financial statements, excessive payments of remuneration, and a crisis of confidence within global equity markets.[141] They argue that in most cases of corporate crime, something is more fundamentally wrong.[142] This includes issues concerning business ethics, and perhaps the failure of government and professional communities to adequately monitor and control corporate activities.[143] Mofokeng echoes Hendrikse and Hefer's argument, stating that effective control entails having systems and structures in place that ensure a business is able to reach the desired objectives with the minimum expenditure of time, money, waste and effect.[144] Mofokeng believes that legitimacy will be achieved by doing the right thing, for the right reasons, consistently and continually, both internally and externally.[145] He believes that trust, good reputation and legitimacy can be rekindled by taking responsibility and embracing the ownership of one's obligations or liability to correct things, meaningfully and swiftly.[146] Mofokeng's sentiments highlight the imperative nature of business ethics, and how it ties into effective corporate governance. Having a thorough legal framework requires ethical business practices in order for it to be really effective.

2.6 CHALLENGES FACED BY SOCS IN SOUTH AFRICA

The Office of Public Enterprises (OPE) was established in 1995, to direct the restructuring of SOCs in South Africa, and to ensure they are economically impactful on society.[147] To accelerate the restructuring, the executive in 1999 upgraded and redesignated the OPE as the Department of Public Enterprises (DPE), to be a national government department.[148]

The DPE is the primary interface between government and SOCs, as the department is the shareholder representative for government, and is mandated by the Executive to oversee a number of SOCs.[149] The DPE thus plays a key role in the economic growth and stability of South Africa.[150]

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[141] Hendrikse JW & Hefer L *(*2019) 86.
[142] Hendrikse JW & Hefer L *(*2019) 86.
[143] Hendrikse JW & Hefer L *(*2019) 86.
[144] Hendrikse JW & Hefer L *(*2019) 86.
[145] Mofokeng T (2020) 69.
[146] Mofokeng T (2020) 69.
[147] Department of Public Enterprises *Strategic Plan 2020/2021 – 2024/2025* (2020) 13 (hereafter *Strategic Plan).*
[148] DPE *Strategic Plan* (2020) 13.
[149] DPE *Strategic Plan* (2020) 13.
[150] DPE *Strategic Plan* (2020) 14.

The DPE's 5-year strategic plan identifies certain challenges that may be prevalent at SOCs in the 2020-2025 period. One of these challenges is the declining growth in the world's larger economies, as a result of trade tensions between the United States of America (USA) and China.[151] Ultimately, this has a global effect on trade and foreign investment.[152] The DPE further highlights the impact of the coronavirus pandemic on the world's economy, and anticipates a new world order to emerge after the pandemic.[153] Due to an increase in competition from imports, the DPE warns that South African manufacturers may face an increasingly challenging export environment.[154]

Most SOCs have been under pressure as they face a wide array of issues ranging from operational to monetary difficulties, as SOCs are still recovering from years of systemic corruption.[155] In performing its oversight function, the DPE utilises a number of instruments prescribed by the PFMA and Companies Act. These instruments include the Strategic Intent Statement (SIS), the Shareholder Compact (SHC), the Corporate Plan (CP), the Quarterly and Monthly Reports (QR and MR), as well as the Annual Report (AR).[156] However the effectiveness of these instruments, and their legal status in ensuring proper governance and management of SOCs, remains an area of concern for the department.[157] The Minister has placed a strong emphasis on the strengthening of SOC boards by ensuring they are composed of credible and capable individuals.[158] Nonetheless, challenges faced by some SOCs in South Africa, as identified by the department, are discussed below.

2.6.1 Denel

Denel was established in 1992 as a private company in terms of the Companies Act of 1973, with the government as its sole shareholder. [159] The company operates in the military aerospace and landward defence industry, providing strategic equipment to the defence force. [160] For the 2020-2025 period, the company is focussed on restructuring, which entails optimising its cost structure, and reviewing the company's business model to improve global competitiveness.[161]

[151] DPE *Strategic Plan* (2020) 14.
[152] DPE *Strategic Plan* (2020) 14.
[153] DPE *Strategic Plan* (2020) 14.
[154] DPE *Strategic Plan* (2020) 14.
[155] DPE *Strategic Plan* (2020) 35.
[156] DPE *Strategic Plan* (2020) 35.
[157] DPE *Strategic Plan* (2020) 35.
[158] DPE *Strategic Plan* (2020) 35.
[159] Companies Act 61 of 1973.
[160] DPE *Strategic Plan* (2020) 36.
[161] DPE *Strategic Plan* (2020) 36.

In 2020, the company posted a loss of R1.5billion, and the company has been insolvent ever since.[162] As a result, the company had been unable to pay employee pension funds or taxes. This necessitated an emergency government loan guarantee of R580 million, in order to pay salaries and suppliers.[163] As a result, the company experienced high turnover of specialised staff, which in turn affected manufacturing.[164] In the 2021-22 financial year, a R3.6billion bailout from Treasury assisted the company in repaying debts.[165] According to the acting chief financial officer (CFO), Thandeka Sabela, the company failed to address its fundamental operational challenges, *despite* the bailout.[166] In 2023, certain operational problems were addressed through the sale of non-core assets, the unbundling of the Denel Medical Benefits Trust (DMBT), and the recapitalisation of funding received in March 2023.[167]

The challenges facing Denel, as identified by the DPE, are mostly related to financial management at the company.[168] The DPE also acknowledges that Denel has felt the impact of the regulatory environment on exports and market retention.[169] Despite an improvement in the financial management at the company in 2023, SCOPA (Standing Committee on Public Accounts) members still expressed concern over the number of interim/acting positions at the company.[170]

2.6.2 Eskom

Eskom is governed by the Eskom Conversion Act,[171] in terms of which it is mandated to generate and distribute electricity to residential, industrial, commercial, municipal, mining and agricultural customers and redistributors.[172] In 2019/2020, Eskom was reportedly responsible for generating 95 per cent of the electricity used in South Africa, and 45 per cent of the electricity used in Africa.[173] However, the conglomerate has battled with financial, operational and structural challenges for many years.[174]

[162] DPE *Strategic Plan* (2020) 36.
[163] Erasmus D 'Denel posts R390 million profit' *Mail & Guardian* 14 June 2023 available at *https://mg.co.za/news/2023-06-14-denel-posts-r390-million-profit/* (accessed 12 July 2023).
[164] Erasmus D *Mail & Guadian* (2023).
[165] Erasmus D *Mail & Guadian* (2023).
[166] Erasmus D *Mail & Guadian* (2023).
[167] Erasmus D *Mail & Guadian* (2023).
[168] DPE *Strategic Plan* (2020) 36.
[169] DPE *Strategic Plan* (2020) 36.
[170] Erasmus D *Mail & Guadian* (2023).
[171] Eskom Conversion Act 13 of 2001.
[172] DPE *Strategic Plan* (2020) 36.
[173] DPE *Strategic Plan* (2020) 36.
[174] DPE *Strategic Plan* (2020) 36.

The most pressing challenge faced by Eskom, as identified by the DPE, is the aging and unreliable power stations impacting the security of electricity supply and causing significant deterioration of the generation fleet.[175] As a result of the severe capacity shortages at Eskom, the country has faced unprecedented loadshedding signals, or electric blackouts.[176] Loadshedding occurs when a power station cannot meet the demand for electricity, and power is switched off to preserve power generating assets.[177] The situation is exacerbated by Eskom's inability to collect outstanding debt from municipalities, and its inability to address low payment levels in municipalities and residential areas.[178] One of Eskom's greatest challenges is the soaring debt of almost half a trillion Rand, as at the end of March 2019.[179]

South Africa has experienced almost daily loadshedding in 2023, meaning most companies and households have been cut off for up to eight hours a day.[180] The power crisis which emerged in 2022 is a culmination of almost two decades of deficient policymaking, political interference, inefficient management, weak spending controls and embedded crime and corruption at the SOC.[181]

On 6 March 2023, the President created a new ministerial position in the presidency to oversee the implementation of crisis measures and appointed the new Minister of Electricity.[182] President Cyril Ramaphosa decided to appoint a Minister of Electricity, Kgosientsho Ramakgopa, to aid in solving the problems at Eskom, which the two Ministers responsible for the power sector could not do.[183] Due to the deterioration in Eskom's performance, and delays in producing new power, government has turned towards more executive, and even presidential crisis interventions.[184] As a result, the President announced a 'state of disaster' in the power

[175]DPE *Strategic Plan* (2020) 36.
[176] DPE *Strategic Plan* (2020) 36.
[177] 'Loadshedding explained' available at *https://sympower.net/load-shedding-explained/* (accessed 31 August 2023).
[178] DPE *Strategic Plan* (2020) 36.
[179] DPE *Strategic Plan* (2020) 36.
[180] Economist Intelligence Unit 'South Africa's underpowered economy faces severe challenges' *EIU* 1 June 2023 available at *https://country.eiu.com/article.aspx?articleid=933281076&Country=South+Africa&topic=Economy* (accessed 12 July 2023).
[181] Economist Intelligence Unit (2023).
[182] Godinho C 'The Eskom crisis update: Where we are now' *Energy Growth Hub* March 2023 available at *https://energyforgrowth.org/wp-content/uploads/2023/03/The-Eskom-crisis-update_-Where-we-are-now-2-2.pdf* (accessed 12 July 2023).
[183] The two ministers responsible for the power sector, namely Minister of Public Enterprises Pravin Gordhan, and Minister of Mineral Resources and Energy Gwede Mantashe, failed to solve the problems at Eskom, resulting in the new office for the Minister of Electricity. Godinho C (2023).
[184] Godinho C (2023).

sector, enabling more executive level interventions.[185] In terms of the Disaster Management Regulations published early in 2023, Cabinet members are empowered to exercise additional executive authority.[186]

2.6.3 South African Airways

South African Airways (SAA) operates as the country's national air carrier, operating in the international, regional, and domestic markets.[187] According to the DPE, the company has been undercapitalised since the transfer from Transnet in 2007.[188] The SAA has thus battled financial issues spanning over ten years, and has relied on debt to survive.[189]

In February 2019, the company was recapitalised with R5billion, which included working capital, to assist the airline to repay its matured government guaranteed debt.[190] However, despite the recapitalisation, the situation at SAA remained precarious, and the airline was placed under business rescue on 5 December 2019.[191] The coronavirus crisis has crippled aviation globally, and as a result, the SAA ceased operations entirely by September 2020.[192] However, by March 2023, SAA CEO John Lamola announced that the airline will be re-opened, and would be ready to sell flights.[193]

According to the DPE, challenges at the SAA include a lack of leadership, poor productivity and efficiencies, and a continued reliance on government funding.[194] Furthermore, the DPE added that the deteriorating financial performance of the company, and the lack of implementation of the turn-around plans, add to the challenges faced by the company.

[185] Godinho C (2023).
[186] National Disaster Management Act 57 of 2002 in GN R3096 *GG* 48152 of 27 February 2023. Regulation 5(1) empowers Cabinet members to issue Directives.
[187] DPE *Strategic Plan* (2020) 38.
[188] South African Airways Act 5 of 2007, Long title states: 'To provide for the transfer of the shares of Transnet Limited in South African Airways (Proprietary) Limited to the State; to provide for the conversion of South African Airways (Proprietary) Limited into a public company having a share capital incorporated in terms of the Companies Act, 1973; and to provide for matters connected therewith.'
[189] DPE *Strategic Plan* (2020) 38.
[190] DPE *Strategic Plan* (2020) 38.
[191] DPE *Strategic Plan* (2020) 36. In terms of s128(1)(b) 'Business rescue' refers to the procedure of facilitating the rehabilitation of a company in financial distress.
[192] Spaeth A 'SAA charts new international flightpath' *Airline Ratings* 16 March 2023 available at *https://www.airlineratings.com/news/saa-charts-new-international-flightpath/#:~:text=After%20a%20year%2C%20a%20%E2%80%9Cnew,ranging%20from%20Accra%20to%20Mauritius* (accessed 13 July 2023).
[193] Spaeth A *Airline Ratings* (2023).
[194] DPE *Strategic Plan* (2020) 36.

2.7 THE ROLE OF THE SHAREHOLDER IN SOUTH AFRICAN SOCs

Understanding the role of shareholders in SOCs is imperative to the understanding of the governance structure of these entities. In South Africa, political involvement of the shareholders in SOCs has been a hotly debated topic. Given the large contribution of SOCs to the economy, Kgobe and Chauke argue that where politicians are not responsible, societies are likely to suffer maladministration of public services, demonstrate fraudulent patterns and face growth challenges. [195] Considering the current state of SOCs in South Africa, most SOCs display these consequences Kgobe and Chauke warned of, thus depicting a society of 'irresponsible politicians.'

PricewaterhouseCoopers (PwC), the Institute of Directors in Southern Africa (IodDSA) and the Development Bank of Southern Africa (DBSA) has published a position paper on SOCs, reflecting on governance responsibility and accountability.[196] The paper indicates that the levels of responsibility and accountability in the governance structures of SOCs often overlap, which negatively affects good governance at these companies.[197] The paper essentially proposes a more effective government-shareholder management model to improve the performance of SOCs, better protect the assets of government, and address governance issues such as poor operational and financial performance of SOCs.[198]

The National Assembly and the National Council of Provinces (NCOP), along with their portfolio committees, public accounts committees and joint committees, are charged with the responsibility of oversight of the performance of SOCs.[199] According to the PwC working group, Parliament faces the problem of needing to improve the capacity of these policy or parliamentary committees, to hold departments and SOCs accountable for their performance.[200] Cabinet, which is made up of the various Ministers, also holds the authority to direct policy.[201] The Department of Public Service and Administration (DPSA) and National Treasury, as well

[195] Kgobe F & Chauke K 'Ethical Leadership and Public Accountability: Problematiques of South Africa's State-Owned Enterprises.' (2021) 26 *Technium Social Sciences Journal* 48.
[196] 'State-Owned Enterprises: Governance responsibility and accountability' Public Sector Working Group: Position Paper 3 (Published by PricewaterhouseCoopers, the Institute of Directors in Southern Africa, and the Development Bank of Southern Africa) 2011.
[197] PwC, IoDSA & DBSA (2011) 7.
[198] PwC, IoDSA & DBSA (2011) 6.
[199] PwC, IoDSA & DBSA (2011) 7.
[200] PwC, IoDSA & DBSA (2011) 7.
[201] PwC, IoDSA & DBSA (2011) 7.

as various regulators, provide support in monitoring policy implementation, through respective financial, public service and regulatory mandates.[202]

In terms of the PFMA, the Executive Authority refers to the Cabinet member who is accountable to Parliament for that specific SOC.[203] Ultimately, the Executive Authority is the line Minister concerned with a return on investments and ensuring the financial viability of the SOC.[204] He is also responsible for the effective and efficient provision of service delivery requirements.[205] The PwC study argued that Parliament and its committees lack the capacity to effectively scrutinise the strategic, financial, budgetary and delivery plans and reports of departments and SOCs, and thus cannot effectively monitor the performance of government departments and SOCs.[206] Oversight on SOC performance rests with Parliament, the line Minister and the boards of SOCs.[207] The working paper argued that the perception that the responsibility to resolve poor performance rests with the Executive Authority undermines the board's role.[208] The PwC working group emphasised that role-players in SOCs should clarify their respective roles through formal means, as either shareholder, policy maker, or regulator.[209] The paper further argued that oversight lines are often blurred, hence the proposal that various levels of oversight be clarified and codified in formal terms, and that measures of independent oversight are implemented.[210] This practice will align with the principle of "cooperative governance," as enshrined in the Constitution.[211] The PwC working group encourages transparency between stakeholders, to promote continual accountability and provide a platform for Ministers to face scrutiny for their actions.[212]

Kgobe and Chauke provide their understanding of the complexity in the operation of SOCs and apply the 'Agency theory' to do so.[213] According to these authors, the agency theory questions the vigilance of directing and overseeing SOCs by board members.[214] In terms of this theory, the managers of the company are considered the 'agents' and the shareholders are considered the 'principal'. The theory suggests that conflict occurs when the interests and objectives of

[202] PwC, IoDSA & DBSA (2011) 7.
[203] PwC, IoDSA & DBSA (2011) 9.
[204] PwC, IoDSA & DBSA (2011) 7.
[205] PwC, IoDSA & DBSA (2011) 7.
[206] PwC, IoDSA & DBSA (2011) 9.
[207] PwC, IoDSA & DBSA (2011) 9.
[208] PwC, IoDSA & DBSA (2011) 9.
[209] PwC, IoDSA & DBSA (2011) 13.
[210] PwC, IoDSA & DBSA (2011) 13.
[211] PwC, IoDSA & DBSA (2011) 13.
[212] PwC, IoDSA & DBSA (2011) 14.
[213] Kgobe F & Chauke K (2021) 46.
[214] Kgobe F & Chauke K (2021) 46.

the managers and shareholders differ, when there is a separation of ownership and control.[215] For example, shareholders may be interested in maximising shareholder value, whereas managers may have different objectives such as maximising salaries, growth of market share or an attachment to a certain investment project.[216] Kgobe and Chauke argue that the 'agency dilemma' occurs when the institution's agents, being the directors, seek to maximise their benefits through actions beneficial to themselves but damaging to the interests of the shareholders.[217] In terms of the Companies Act,[218] however, directors have a duty not to set themselves on a position of conflict between their personal interests and those of the company.[219] Furthermore, directors have the duty not to exceed their powers, and may not perform beyond their capacity.[220] The King IV further entails that all members of the governing body, whether executive, non-executive or independent, are expected by law to act with the independence of mind, in the best interests of the company.[221] However, SOCs still face problems such as political intervention, competing agendas, incompetence, and the agency problem.[222]

Researchers have become increasingly attentive to the problems regarding the relationship between politicians and SOCs.[223] Kgobe and Chauke argue that underperformance of SOCs will impair productivity and growth, which will result in a fiscal burden and a fiscal risk to the state.[224] They predict that public services will become private resources for ruling politicians.[225] It has become apparent that politicians abuse government ownership of SOCs for personal enrichment, thus an important concern for policy makers and development professionals is to boost the efficiency of SOCs, by improving corporate governance.[226] Kgobe and Chauke argue that ideological differences inside and outside the ruling African National Congress (ANC), has further weakened the efficacy of the SOC reform.[227]

[215] Kgobe F & Chauke K (2021) 46.
[216] Kgobe F & Chauke K (2021) 46.
[217] Kgobe F & Chauke K (2021) 47.
[218] s75 of the Companies Act 61 of 2008.
[219] Kgobe F & Chauke K (2021) 47.
[220] Kgobe F & Chauke K (2021) 47.
[221] Kgobe F & Chauke K (2021) 47.
[222] Kgobe F & Chauke K (2021) 48.
[223] Kgobe F & Chauke K (2021) 48.
[224] Kgobe F & Chauke K (2021) 47.
[225] Kgobe F & Chauke K (2021) 48.
[226] Kgobe F & Chauke K (2021) 49.
[227] Kgobe F & Chauke K (2021) 49.

As previously alluded to by Thabane and Snyman van Deventer, SOCs play a very significant role in the South African economy.[228] Political involvement in SOCs, and the current state of affairs at most SOCs, feed the discourse on the privatisation of SOCs versus the nationalisation thereof.[229] Some may argue that South Africa will not become a fully developed state without strategic government intervention in the economy, while some may argue for the nationalisation of important companies to assist the poor, and others may call for the privatisation of non-performing SOCs.[230]

Political involvement in SOCs is a fundamental factor to see to transformation of the economy. However, political involvement in SOCs has caused many problems as well. Addressing the corporate structure and allowing for clarity in terms of the roles of each constituent making up the structure, would allow for more cohesion between parties' involvement.

Thabane and Snyman van Deventer argue that although renewed calls for the privatisation of SOCs have emerged, SOCs are likely to, and probably should, remain under state ownership for the foreseeable future.[231] They argue that as a result of the unique socio-political and economic dynamics of South Africa, government should run public corporations in order to improve labour relations, limit private and foreign control of the domestic economy, generate public funds for the fiscus, increase service delivery and encourage economic development and industrialisation.[232] However, it is questionable whether this is happening.

2.8 SOCS AND THE MEMORANDUM OF INCORPORATION

The Memorandum of Incorporation (MoI) between the executive authority and the accounting authority, is the founding document of the company, and is binding on the company.[233] The MoI sets out the rules against which the company is expected to operate, as it provides the powers of the company, as well as the rights and responsibilities of the directors and shareholders.[234]

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[228] Thabane T & Snyman-Van Deventer E (2018) 2.
[229] Thabane T & Snyman-Van Deventer E (2018) 2.
[230] Thabane T & Snyman-Van Deventer E (2018) 2.
[231] Thabane T & Snyman-Van Deventer E (2018) 4.
[232] Thabane T & Snyman-Van Deventer E (2018) 4.
[233] Section 15(6) of Act 71 of 2008. See also National Treasury 'Governance Oversight Role Over State Owned Entities (SOE's) 25 November 2005 available at *https://www.treasury.gov.za/publications/other/soe/governance%20oversight%20role.pdf* (accessed 23 July 2023) 13.
[234] Morajane T 'The Binding effect of the Constitutive Documents of the 1973 and 2008 Companies Acts of South Africa' (2010) *PER /PELJ* 179.

In terms of the Act, the MoI is binding between the company and each shareholder, each director or prescribed officer of the company, and any other person serving the company as a member of the audit committee or as a member of a committee of the board, in the exercise of their respective functions within the company.[235] Rules contained in the MoI that are inconsistent with the Act , are void in terms of section 15 of the Act.[236]

In terms of section 15(6) of the Act, the MoI is binding, although the Act does not state in which way it is binding.[237] Phiri and Nwafor argue that the Act must be interpreted and applied in a manner giving effect to its purpose.[238] One of the purposes of the Act is to promote the development of the South African economy through entrepreneurship and enterprise efficiency, by creating flexibility and simplicity in the formation of and maintenance of companies.[239] To determine the binding effect of the MoI, the courts are required to recognise common law principles, to give effect to the common law contractual binding effect of the memorandum and articles of association, as it applies to the legal nature of the MoI and the rules.[240] It remains to be seen how the courts will interpret the provisions of the constitutive documents under the 2008 Companies Act.[241]

Nonetheless, in terms of s15(6) of the Act, directors, prescribed officers and members of the audit committee are contractually bound to observe the provisions of the MoI.[242] Directors may be held bound to the rights and obligations contained in the MoI, if it has been handed to them in their official capacities as directors.[243] Morajane warns that drafters of the company's MoI must be wary not to draft documents that defeat the effect of prohibition of the Act[244] to avoid these provisions from being declared void by the courts.[245] The anti-avoidance section of the Act empowers the courts to declare certain provisions of the MoI void, upon application by the

[235] Act 71 of 2008 s 15(6) of Act 71 of 2008.
[236] s 15(1)(*b*). See also Morajane T (2010) 179-180.
[237] Morajane T (2010) 180.
[238] Phiri S & Mpofu K 'A consideration of the binding effect of section 15 (6) of the Companies Act 71/2008' (2020) 45(2) *Journal for Juridical Science* 154-167.
[239] Morajane T (2010) 180.
[240] Morajane T (2010) 181.
[241] Morajane T (2010) 186.
[242] Section 15(6) of Act 71 of 2008.
[243] Morajane T (2010) 186.
[244] See s6 of Act 71 of 2008.
[245] s 6(15) of Act 71 of 2008 reads: 'To the extent that the specific content, or a particular effect, of any provision of a company's Memorandum of Incorporation –

(a) Is required of the company by or in terms of any applicable public regulation, or by the listing requirements of an exchange; and
(b) Has the effect of negating, restricting, limiting, qualifying, extending, or otherwise altering the substance or effect of an unalterable provision of the Act, that provision of the company's Memorandum of Incorporation must not be construed as being contrary to section (1)(a).'

CIPC, or the Takeover Regulation Panel, for defeating the effect of the prohibition as provided for in the Act.[246]

The infamous issue of former Minister of Communications, Faith Muthambi, seeking to revise the MoI for the SABC (South African Broadcasting Corporation), to provide her with the power to remove board members in terms of the Companies Act,[247] is relevant in this regard. An ad hoc committee established by the National Assembly found that the amended MoI was never registered with the CIPC and therefore was not valid, and that all actions taken before this was declared, was invalid.[248] It appears therefore that the rules concerning the registration of MoI's are clear and were fairly implemented. However, it begs the question, that had that amended MoI been registered, would the Minister have succeeded in affording herself the authority to remove board members? It appears that the legislature does not provide SOCs with sufficient protection from political meddling.

2.9 CONCLUSION

The essence of corporate governance is understood as the manner in which companies are directed and controlled.[249] Good corporate governance provides the foundation for well-managed, effective, and productive companies. Mofokeng emphasised 'direction and control' in corporate governance, arguing that flaws in this respect can lead to the devaluation of a company and by extension, the company's shares.[250] Ethical behaviour and social responsibility are recurring themes in the understanding of corporate governance.[251] In my opinion, the notion of running companies like good corporate citizens best encapsulates the concept of good corporate governance. Companies being 'good corporate citizens' is particularly relevant in the context of SOCs, given their social objectives, and their enormous contribution to the economy. In this respect, I agree with King that companies are greater agents for change than the government.[252]

The South African socio-political history justifies a regulated corporate sphere. Racial exclusionary practices in the economy and workforce were extensively addressed through

[246] s 6 of Act 71 of 2008, deals with 'Anit-avoidance, exemptions and substantial compliance.'
[247] Interim report of the ad hoc committee on the SABC board Inquiry into the fitness of the SABC board, dated 27 January 2017.
[248] Interim report of the ad hoc committee on the SABC board Inquiry into the fitness of the SABC board, dated 27 January 2017.
[249] Mofokeng T (2020) 66.
[250] Mofokeng T (2020) 66.
[251] Mofokeng T (2020) 67.
[252] King ME (2010) 446.

mechanisms facilitating good corporate governance, such as the King Codes and the Protocol. These instruments made way for transformation of the corporate sphere in terms of addressing past societal imbalances. When considering the history of corporate governance codes, at the very beginning, there was a lax approach to safeguarding against directors' abuse of power. Later, corporate governance codes emphasised the importance of independent, non-executive directors, as well as board committees. Just as corporate governance principles and codes have been developed in the past, to reflect issues in the market at that time, these principles should continuously be amended. For example, current issues in the sector of SOCs include the issue of extensive political involvement in the companies, a lax approach to the duties and responsibilities of the board of directors, and the issue of blurred lines of oversight. Collectively, these issues have manifested into poor service delivery, poor governance structures, labour-related concerns, as well as fraud and corruption. Corporate governance codes should be constantly evolving, especially when considering the rapid pace of technological advancements that need to be regulated, such as the development and integration of artificial intelligence in business. A pro-active approach to contemporary corporate misconduct should be developed.

While the Constitution remains a fundamental instrument facilitating corporate governance, it is clear that the codification of the Companies Act of 2008 was a particular milestone for corporate governance in South Africa. The corporate sphere in South Africa has moved towards a more integrated, inclusionary, and sophisticated governance system. Although some still argue for a uniform regulation to govern SOCs, I do not agree, as the regulatory framework governing the sector is thorough and extensive. I believe the problem is the practices that are implemented, or rather *not* implemented, as required by these regulatory mechanisms. The fact remains that, despite the sophisticated system governing the sector, the current state of affairs at most SOCs indicates a lack of cohesion between the practices implemented and the system of governance available. This is evident in the constant political meddling that often occurs from shareholding ministers. It is thus disputed whether crucial provisions in terms of the Companies Act. PFMA, or the codes, are observed at SOCs.

Ethical behaviour and practices form the foundation of good corporate governance. SOCs have social and public goals and responsibilities, which other private companies in most cases, do not. Ethical behaviours and practices, as a foundation for corporate governance, in some cases, would see to ordinary citizens having their basic needs being met. For example, with the correct ethical behaviour, and cohesion with the principles of corporate governance, Eskom would

theoretically be able to see to ordinary citizens having their basic need to electricity being met. The most concerning 'failed' SOC in South Africa, and the most discussed, is Eskom. This chapter has identified the challenges at Eskom as operational, financial, and political. However, the fundamental challenge at the parastatal is the governance instability. The challenges at Eskom has had far-reaching disruptions to economic activity in South Africa. The challenges identified at Eskom, and the effects of failed corporate governance at an SOC, captures the essence of this paper, which is the great impact these companies have on the economy at large, and the influence of implementing good corporate governance practices.

Corporate governance failures at South African SOCs highlight the problematic tripartite role of government, as shareholder, policy maker and regulator. In the private sector, the Steinhoff saga brought to light the issue with tick-box compliance systems. This further enunciates the importance of ethical practices, which has led De Klerk et al to question if it is possible to codify ethical practices.

However, further to the challenges of fraud, corruption, and political meddling at SOCs, this sector is further impacted by changes in the global economy. As identified by the Department of Public Enterprises, these challenges include the effects of trade tensions between the United States and China, the effects of the coronavirus pandemic on the global economy, as well as an increase in competition from imports. In light of this, good leadership, ethical business practices, and implementing good corporate governance standards at SOCs in South Africa, would assist these companies to remain sustainable and competitive in an ever-changing global economy.

This chapter has discussed the regulations and instruments facilitating corporate governance at SOCs. The Memorandum of Incorporation can be viewed as an instrument that facilitates corporate governance. However, the incident with a cabinet minister seeking to amend the MoI of an SOC to afford herself the power to appoint or dismiss board members, once again highlights the political meddling experienced at SOCs. It is thus questionable whether legislation adequately protects SOCs from political meddling.

Lastly, this chapter has discussed the role of shareholders in SOCs, and highlighted the political meddling that often takes place in these Companies. The role played by shareholders, particularly the role played by the Minister in charge of the entity, has been largely contested in South African discourse on the state of affairs at SOCs. However, to reiterate Mofokeng's earlier statements, governance is generally thought to be in the domain of the board of

directors.[253] It is clear that the governing body of a company is the heartbeat of corporate governance, which further fuels the intention of this study. With the emphasis placed on the governing body, and the board of directors as 'the custodian of corporate governance' within a corporation, it is worthwhile to analyse the extent to which the legal duties of a company's board of directors facilitates good corporate governance.

[253] Mofokeng T (2020) 68.

CHAPTER THREE

THE FUNCTIONS AND EFFECTIVENESS OF AN SOC's BOARD OF DIRECTORS

3.1 INTRODUCTION

As a legal entity separate from its management and shareholders, a company must act through its individuals,[1] particularly through its directors. Havenga has argued that a company's directorship is one of the most complex fiduciary offices.[2] The effective control of management is essential to the interests of the company and its stakeholders.[3] A balance should be struck between the directors' freedom to manage, directors' accountability and the interests of various stakeholders.[4] While directors must always remain cognisant of their duties as directors, and the limitations to their powers, they must have the freedom to exercise their own decision-making discretion in the interests of the company's growth.

This chapter provides an analysis on the composition and functions of the board of directors and discusses issues such as the financial management by the board, and board effectiveness. This chapter thus investigates whether the regulatory framework is effective in facilitating good corporate governance at State-Owned Companies (SOCs) in South Africa.

Furthermore, this chapter analyses the two broad functions of the board of directors, namely the decision-making function and the oversight function. This chapter briefly discusses the impact of international corporate law on the South African corporate legal framework, and its influences.

3.2 BOARD EFFECTIVENESS AND FUNCTIONS OF THE BOARD

As previously mentioned, the board of directors are the custodian of corporate governance within a company. However, the duty of corporate governance oversight in an SOC is vested in the board (or accounting authority), as well as the Parliament and the respective Executive Authorities.[5]

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[1] Havenga M 'The Company, the Constitution, and the Stakeholders' (1997) 5 *Juta's Business Law* 134.
[2] Havenga M (1997) 134.
[3] Havenga M (1997) 134.
[4] 'Stakeholders' refers to 'any group or individual who can affect or is affected by the achievement of the organisation's objective.' This definition is found in Abratt R, Benn S & O'leary B 'Defining and identifying stakeholders: Views from management and stakeholders' (2016) 47(2) *South African Journal of Business Management* 1 – 11. Havenga M *The company, the Constitution, and the stakeholders* (1997) 134.
[5] *DPE – SOC Board Evaluation Framework* (2021) 19.

The board of directors is fully accountable to their shareholders for meeting strategic objectives, while simultaneously achieving commercial objectives as agreed with the shareholding minister.[6] The board is further responsible for meeting the needs of other stakeholders, inter alia, the consumers of the company's goods and services, lenders, workers, as well as the general public.[7] Alongside responsibilities to the company, shareholders and other stakeholders, the board of an SOC must remain cognisant of, and uphold, the fiduciary duties imposed on them in terms of the Companies Act,[8] the Public Finance Management Act,[9] and common law.[10] The roles and responsibilities of the board, are ultimately found in these legislative statutes, common law, as well as the Protocol on Corporate Governance,[11] and the King IV report.[12]

3.2.1 Composition and Functions of the Board

The Act requires that a board of an SOC be comprised of at least three directors.[13] Section 72(4) of the Act, read with Regulation 43, however requires that the board of an SOC establish a social and ethics committee.[14] In terms of Regulation 43(4), a company's social and ethics committee must be comprised of at least three directors or prescribed officers.[15] Essentially, the intention is that the committee should include a 'non-executive director.'[16] Therefore in practice, more than three directors is required.

In terms of section 50 of the PFMA, the board of an SOC must:

1. Ensure reasonable protection of the assets and records of the SOC;[17]
2. Act with fidelity, honesty, integrity and in the best interests of the SOC in managing the financial affairs of the SOC;[18]

[6] *DPE – SOC Board Evaluation Framework* (2021) 21.
[7] *DPE – SOC Board Evaluation Framework* (2021) 21.
[8] Companies Act 71 of 2008.
[9] Public Finance Management Act 1 of 1999.
[10] *DPE – SOC Board Evaluation Framework* (2021) 21.
[11] The Department of Public Enterprise's Protocol on Corporate Governance (2002).
[12]The King IV Report on Corporate Governance for South Africa 2016, The Institute of Directors in Southern Africa (hereafter *King IV Report*).
[13] s 66(2)(b) of Act 71 of 2008.
[14] s 72(4)(b) of Act 71 of 2008 read with reg 43(1) of the Companies Act 71 of 2008, prescribes the categories of companies required to appoint a social and ethics committee (SEC).
[15] The Companies Act regulations in R351 *GG* 34239 of 26 April 2011, regulation 43(4).
[16] Havenga M 'The Social and Ethics Committee in South African Company Law' (2015) 78 *Tydskrif vir Hedendaagse Romeins-Hollandse Reg* 286.
[17] s 50(1)(a) of Act 1 of 1999.
[18] s 50(1)(b) of Act 1 of 1999.

3. Must disclose to the minister responsible for that SOC, upon request, all material facts which may influence the decisions or actions of the minister or legislature;[19] and
4. Seek to prevent any prejudice to the financial interests of the state, within the sphere of influence of that accounting authority.[20]

In terms of s66(1) of the Act, an SOC must have a board, which has the authority to exercise all powers and perform any of the functions of the SOC, except if limited by the Act or the company's Memorandum of Incorporation (MoI).[21] As the sole shareholder of an SOC, government has the responsibility of appointing an accounting authority, which constitutes the board of directors, in terms of the Companies Act.[22] The board is required to implement and monitor policies, and to evaluate the performance of those tasked with the implementation of certain performance objectives.[23] Part of the board's responsibility, aside from monitoring performance against set targets, includes taking corrective action on a timely basis.[24] The board is also responsible for establishing an environment of accountability and responsibility.[25] Failures by the board to uphold these responsibilities, has often resulted in government having to assist SOCs in order for them to remain sustainable.[26]

3.2.2 Financial Management by the Board

In terms of financial and risk management of the company, s51 of the PFMA provides that the SOC must have and maintain a transparent, effective, and efficient system of internal control.[27] This section requires that the SOC maintains a system of internal audit, under the control and direction of an audit committee, which serves as a subcommittee of the board of directors.[28]

The role and functions of the board in terms of the PFMA, include that the board takes appropriate steps to collect all revenue due to the company; prevent irregular, fruitless and wasteful expenditure; prevent losses resulting from criminal conduct, and prevent expenditure not complying with the operational policies of the company.[29] The PFMA further requires that

[19] s 50(1)(c) of Act 1 of 1999.
[20] s 50(1)(d) of Act 1 of 1999.
[21] s 66(1) of Act 71 of 2008.
[22] s 88(2) of Act 1 of 1999 states, 'the Minister, after consulting the Auditor-General, appoints the members of the Board.'
[23] Auditor-General South Africa *PFMA Report* (2018 – 2019) Section 7: Governance, Oversight and Financial Stability of SOEs (2019) 114 (hereafter *PFMA Report*).
[24] AGSA *PFMA Report* (2019) 114.
[25] AGSA *PFMA Report* (2019) 114.
[26] AGSA *PFMA Report* (2019) 114.
[27] s 51 of Act 1 of 1999.
[28] s 51 of Act 1 of 1999.
[29] s 38(1)(c) (*i and ii)* of Act 1 of 1999.

the company manages the available working capital efficiently and economically.[30] The board is required to comply with any tax, levy, duty, pension and audit commitments as required by legislation.[31] The board is further required to take the appropriate disciplinary steps against any employee of the SOC who contravenes a provision of the PFMA, or who commits an act which undermines the financial management and internal control system of the company, or who permits an irregular expenditure or a fruitless or wasteful expenditure.[32] Most importantly, the board is required to comply and ensure compliance by the SOC with the provisions of the PFMA and any other legislation applicable to the SOC.[33]

3.2.3 The Role of Oversight and Board Effectiveness

Despite the substantive framework for the fiduciary duties of directors, SOC boards still face corporate governance challenges.[34] In 2013, a report by the Presidential Review Committee (PRC) revealed a number of challenges faced by SOCs.[35] The PRC identified inadequate governance and oversight systems as one of the challenges faced by SOCs.[36] In addition, questionable financial management at SOCs has resulted in an increasing need for financial injections from government.[37] In the 2019/20 Public Enterprise Public Budget Vote speech, Minister of Public Enterprises, Pravin Gordhan, expressed concern over 'a decade of mismanagement, negligent board and executive fiduciary accountability for poor performance, and malfeasance that enable State capture, [and] rampant corruption at our SOCs.'[38]

The recruitment of board and executive members is a pertinent challenge faced by SOCs, as the appointment of board members without the required competence and qualifications has often led to unintended consequences and has compromised the quality of the board and executive recruitment process.[39] SOCs are further faced with the challenge of an insufficient division of power between the board and the Executive Authority, regarding governance and operational management.[40]

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[30] s 38(1)(c)(*iii*) of Act 1 of 1999.
[31] s 38(1)(e) of Act 1 of 1999.
[32] s 38(1)(h) of Act 1 of 1999.
[33] s 8(1)(n) of Act 1 of 1999.
[34] *DPE – SOC Board Evaluation Framework* (2021).
[35] The Presidency *PRC Report* (2013).
[36] The Presidency *PRC Report* (2013).
[37] The Presidency *PRC Report* (2013).
[38] Minister Pravin Gordhan – Speech on Public Enterprise Budget Vote 2019/20 (11 July 2019).
[39] The Presidency *PRC Report* (2013).
[40] The Presidency *PRC Report* (2013).

A long-standing question in corporate governance is the effect that the board of directors has on organisational performance.[41] In 2018, a global survey by McKinsey & Co found that boards with better dynamics and processes, that manage to execute core activities more effectively, report stronger financial performance at the companies they serve.[42] The Department of Public Enterprises (DPE) has thus emphasised the critical importance of board effectiveness, as it ensures that boards are aware of the level of their effectiveness, and have an opportunity to grow, develop and improve in order to have a more positive impact on their organisations.[43] The DPE has identified that in SOCs specifically, one key challenge is that there is no standardised framework to define what board effectiveness is, or to inform the SOC board evaluation practice, so that boards can derive increased value from the evaluation process.[44] This informed the DPE's decision in 2019 to embark on a process to develop an effective and strengthened Board Evaluation Framework (BE Framework).[45] The aim of the BE Framework, according to the DPE, was to support the strengthening of governance and oversight at SOCs.[46] The SOC BE Framework was designed to ultimately improve the effectiveness of boards in the SOCs accountable to the Executive Authority, the Minister of Public Enterprises.[47] The BE Framework was tabled to be implemented in January 2021.[48]

The BE Framework by the DPE was a well-informed framework, with the potential to solve the governance issue regarding oversight and overall board performance. However, the DPE Strategic Plan for 2020/21 – 2024/2025 does not specifically mention the implementation of the BE Framework.[49] In terms of oversight at SOCs, the DPE's strategic plan simply summarises the key outcomes for 2020/21 – 2024/2025 as '[t]he alignment across SOCs and uniformity of oversight models and their execution; and improved governance and accountability.'[50]

As the custodian of corporate governance in a company, the responsibility of oversight is vested in the board of directors. A clear framework that would enable an efficient assessment for evaluation of the board's performance, as well as the company's performance, would increase

[41] *DPE – SOC Board Evaluation Framework* (2021) 30.
[42] *DPE – SOC Board Evaluation Framework* (2021) 30. The survey referred to is McKinsey & Co. *A Time for Boards to Act* (2018).
[43] *DPE – SOC Board Evaluation Framework* (2021) 30.
[44] *DPE – SOC Board Evaluation Framework* (2021) 30.
[45] *DPE – SOC Board Evaluation Framework* (2021) 31.
[46] *DPE – SOC Board Evaluation Framework* (2021) 34.
[47] *DPE – SOC Board Evaluation Framework* (2021) 34.
[48] *DPE – SOC Board Evaluation Framework* (2021) 93.
[49] Department of Public Enterprises *Strategic Plan 2020/2021 – 2024/2025* (2020) 59 (hereafter *Strategic Plan).*
[50] DPE *Strategic plan* (2020) 59.

board effectiveness. Effective oversight mechanisms would additionally assist the shareholding minister, to which the board is accountable, in ensuring that specific strategic objectives are met. A framework that would assist in board evaluation, and positively impact board effectiveness, is particularly important, in the South African context, given the large impact these companies have on GDP, and society. Reverting to Havenga's earlier sentiments, that a board requires freedom and discretion in order to be really effective, it is important that the effectiveness of a board is monitored and measured, so that challenges may be identified and addressed in a timely manner.

It is evident that the board of directors is accountable for collective duties and responsibilities imposed on the board, in terms of the Companies Act and the PFMA. While directors are individually accountable for the duties imposed on them, the board as a collective carries a responsibility towards the company. A board effectiveness framework would assess and measure the effectiveness of the board's performance in terms of financial management, oversight mechanisms etc. Unfortunately, oversight mechanisms in South Africa, particularly at SOCs, are underdeveloped, making it hard to assess and measure the collective performance of the board.

3.3 DIRECTORS' DECISION-MAKING FUNCTION

In *Fisheries Development Corporation of SA Ltd v Jorgensen*,[51] Margo J held that a director is not a servant or agent of the shareholder, and rather referred to the company as the director's 'principal.'[52] According to Margo J, a directors' duty is to 'observe the utmost good faith' to the company.[53] Therefore, directors are required to exercise independent judgement and make decisions based on the best interests of the company.[54] In this case, it was held that while a director may be representing the interests of the shareholder when carrying out his functions as a director, he is obliged to serve the best interests of the company, 'to the exclusion of' any other interests of the shareholder, employer or principal.[55] It was further held that, to a considerable degree, a director's duty of care and skill depends on the nature of the business, and on any obligations assumed by him or assigned to him.[56] In the context of SOCs, it can be

[51] *Fisheries Development Corporation of SA Ltd v Jorgensen* [1980] 4 All SA 525.
[52] *Fisheries Development Corporation of SA Ltd v Jorgensen* [1980] 4 All SA 525 p166.
[53] *Fisheries Development Corporation of SA Ltd v Jorgensen* [1980] 4 All SA 525 p166.
[54] *Fisheries Development Corporation of SA Ltd v Jorgensen* [1980] 4 All SA 525 p166.
[55] *Fisheries Development Corporation of SA Ltd v Jorgensen* [1980] 4 All SA 525 p166.
[56] *Fisheries Development Corporation of SA Ltd v Jorgensen* [1980] 4 All SA 525 p166.

deduced that directors must apply a higher degree of care and skill, given the nature of these businesses and the obligations assigned to them.

In most cases, corporate misconduct and malpractice are a result of the decisions made by those occupying high-level, structural positions in the organisation. The decision-making function of directors is therefore vital for ensuring the company's growth, and to avoid misconduct within the organisation. According to Van Tonder, the director-centric model of corporate governance seeks to discourage the notion of a passive director.[57] This is important, as the company's business and affairs must be managed under the control and direction of the board, subject to the MoI.[58] Therefore, the board as a collective is tasked with managing the company's affairs, monitoring its officers and employees, and making business decisions.[59] When making business decisions, the fiduciary duties imposed on directors require that they exercise their powers in good faith, for proper purpose and in the best interests of the company.[60]

The decision-making function of directors entails that the board determines matters of policy and makes significant decisions that plan the company's future.[61] This function applies to all decisions made by directors, where their powers are used to benefit the company.[62] The standard required of a director when making a business decision, is that he has taken reasonably diligent steps to become informed on a matter, prior to making the decision.[63]

3.4 DIRECTORS' OVERSIGHT FUNCTION

As discussed in chapter two, the oversight function of directors is an underdeveloped function in South Africa. This function deals with the directors' responsibility to actively monitor company officers, employees, and corporate affairs.[64]

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[57] Van Tonder JL 'An Analysis of the Directors' Decision-Making Function Through the Lens of the Business-Judgement Rule' (2016) 37(3) *Obiter* 577 (hereafter *An Analysis of the Directors' Decision-Making Function).* Lipton 'Some Thoughts for Board of Directors in 2013 – The Harvard Law School Forum on Corporate Governance and Financial Regulation' (undated) available at *http://www.blogs.law*.

[58] s 66(1) Act 71 of 2008. Van Tonder JL 'A Primer on the Directors' Oversight Function as a Standard of Directors' Conduct Under the Companies Act 71 of 2008' (2018) 39(2) *Obiter* 305. (Hereafter *A Primer on the Directors' Oversight Function*).

[59] Van Tonder JL (2018) 305.

[60] s 76(3)(a) of Act 71 of 2008. Van Tonder JL *A Primer on the Directors' Oversight Function* (2018) 305.

[61] Van Tonder JL (2018) 305.

[62] Van Tonder JL (2018) 305.

[63] s 76(4)(a)(*i*) of Act 71 of 2008. Van Tonder JL (2018) 306.

[64] Van Tonder JL (2018) 303; Fairfax 'Managing Expectations: Does the Directors' Duty to Monitor Promise More Than It Can Deliver?' (2014) 10(2) *University of St. Thomas LJ* 416.

In *Fisheries Development Corporation of South Africa Ltd. v Jorgensen*,[65] Margo J provided a summary of the duty of care and skill.[66] However, South African courts are yet to provide direct authoritative guidance on the content and meaning of the oversight function, and the standard of conduct expected of directors when discharging this function.[67]

In *Pretorius v PB Meat (Pty) Ltd.*,[68] Cloete J held that the power to manage the affairs of the business, as provided for in terms of s66 of the Act, are two-fold.[69] The power and obligation is original in terms of the new Act, and not delegated through the MoI as it was in terms of the 1973 Act.[70] Therefore, the 'ultimate power' is with the board of directors, and not with the shareholders.[71] Cloete J held that the directors' powers and duties are now partially codified in the Act.[72] Directors are therefore required to exercise their powers as directors bona fide and in the best interests of the company.[73] From this case, it is clear that directors, under the obligation to manage the affairs of the business, must do so in the best interests of the company. Therefore, although the oversight function of directors is underdeveloped in South Africa, directors must still abide by the duty to manage the affairs of the business and do so in the best interests of the company. Directors are bound to act with care, skill, and diligence, which implies that directors must perform their oversight function, even though the oversight function is not explicitly provided for in the Act.

In *Ragavan v Optimum Coal Terminal (Pty) Ltd*,[74] Victor J delivered judgement on a matter concerning the powers of the directors of a company. Victor J made reference to the decision in *Kaimowitz v Delahunt,*[75] where Davis J held that the overall management and supervision powers reside in the board of directors.[76] Writing on the decision in *Kaimowitz,* Cassim argues that although s66 of the Act provides for the powers of the board in terms of the business and affairs of the company, there are still limitations to their role.[77] Victor J also emphasised that

[65] *Fisheries Development Corporation of SA Ltd v Jorgensen* [1980] 4 All SA 525.
[66] *Fisheries Development Corporation of SA Ltd v Jorgensen* [1980] 4 All SA 525.
[67] *Fisheries Development Corporation of SA Ltd v Jorgensen* [1980] 4 All SA 525.
[68] *Pretorius and another v PB Meat (Pty) Limited and Another* [2016] JOL 35367 (WCC).
[69] *Pretorius v PB Meat (Pty) Ltd.* [2016] JOL 35367 (WCC).
[70] *Pretorius v PB Meat (Pty) Ltd.* [2016] JOL 35367 (WCC). Reference to Companies Act 61 of 1973.
[71] *Pretorius v PB Meat (Pty) Ltd.* [2016] JOL 35367 (WCC). s 71 of Act 71 of 2008.
[72] *Pretorius v PB Meat (Pty) Ltd.* [2016] JOL 35367 (WCC).
[73] *Pretorius v PB Meat (Pty) Ltd.* [2016] JOL 35367 (WCC). s 71 of Act 71 of 2008.
[74] *Ragavan and Others v Optimum Coal Terminal (Pty) Ltd and Others* [2022] JOL 52124 (GJ).
[75] *Kaimowitz v Delahunt* 2017 (3) SA 201 (WCC).
[76] *Kaimowitz v Delahunt* 2017 (3) SA 201 (WCC).
[77] Cassim R 'The right of a director to participate in the management of the Company: *Kaimowitz v Delahunt* 2017 (3) (WCC)' (2018) 30 *SA Merc* 14.

the powers of directors are now statutorily provided for in the Act.[78] He therefore emphasised that the business and affairs of the company must be managed by, or under the direction of, its board of directors.[79] The *Ragavan* matter emphasises the directors' obligations to oversee the business and affairs of the company, and therefore further justifies the oversight role of the board.

In terms of the codification of director duties in statute, in *Westerhuis v Whittaker*,[80] it was held that the duties of directors in terms of s76 of the Act extends beyond the common law duty of directors as it relates to the standard of conduct expected from directors.[81]

Section 76 of the Act provides no standard of directors' conduct for the oversight function.[82] Cassim, however, argues that the insertion of the word 'diligence' in section s76(3)(c) is different from the words 'care and skill.'[83] Cassim argues that the word 'diligence' means 'attentiveness;' and should be interpreted as directors practicing 'diligence' or 'attentiveness' at board and other meetings, in relation to paperwork, company affairs and the proper supervision and general monitoring of corporate affairs and policies.[84] Other than discussions concerning the interpretation of the insertion of 'diligence' in s76(3)(c), nothing else in the Companies Act or its regulations indicates what is required of directors in terms of their oversight function.[85] Although the King IV provides guidelines in respect of directors' oversight function, it is still not law.[86]

As a result of the undeveloped nature of this function, Van Tonder's research relies on s5(2) of the Act, which provides that, to the extent appropriate, a court interpreting or applying the provisions of the Act may consider foreign company law.[87] Van Tonder thus relied on the Model Business Corporation Act (MBCA) from the United States of America (USA).[88] This

[78] *Kaimowitz vs Delahunt 2017* (3) SA 201 (WCC).
[79] *Ragavan and Others v Optimum Coal Terminal (Pty) Ltd and Others* [2022] JOL 52124 (GJ).
[80] *Westerhuis v Whittaker and Others* (4145/2017) [2018] ZAWCHC 76 (26 April 2018).
[81] *Westerhuis v Whittaker and Others* (4145/2017) [2018] ZAWCHC 76 (26 April 2018) para 22.
[82] Van Tonder JL (2018) 306.
[83] s 76(3)(c) reads: 'Subject to subsection (4) and (5), a director of a company, when acting in that capacity, must exercise the powers and perform the functions of director –
(c) With the degree of care, skill and diligence that may reasonably be expected of a person.'
[84] Cassim et al *Contemporary Company Law* (2022) 559 – 560.
[85] Van Tonder JL (2018) 306.
[86] Van Tonder JL (2018) 307. See King IV Report 42.
[87] Van Tonder JL (2018) 304.
[88] The Model Business Corporation Act (Revised 2016) (December 9, 2016) (hereafter MBCA). Van Tonder JL (2018) 305

Act addresses the level of performance expected of directors undertaking the role and responsibilities of the office of director.[89]

Mongalo has emphasised the influence of Delaware corporate law, and states that it was used as a benchmark in a number of aspects in South Africa's corporate law reform project which culminated in the enactment of the Companies Act of 2008.[90] A report in 2001 by the Committee on Corporate Laws of the Business Law Section of the American Bar Association, recommended that South Africa should consider 'regulating director conduct and liability by statute and empowering shareholders to hold directors accountable for violations.'[91] In this regard, South Africa has managed to implement the advice from American lawyers, through incorporating director duties in the Companies Act of 2008, and partially encoding common law rules pertaining to director duties.

Corporate failures in the United States had collectively cost shareholders $460 billion, by the end of the first decade of the 21st century.[92] These failures brought attention to the corporate governance of directors' duties,[93] as a prominent Delaware jurist, attributed the failure to the 'lassitude and indifference' of some directors who were not proactive in their oversight roles.[94] Federal intervention into corporate governance put pressure on the Delaware judiciary to evolve expectations for directors and institute firmer legal duties.[95] In terms of the MBCA, directors' oversight duties are encoded, although the standards do not carry direct liability consequences.[96] The MBCA categorises the standard of liability for the oversight function as 'the failure to devote attention.'[97] The inclusion of the word 'attention,' confirms Cassim's contention, that the word 'diligence' should be interpreted as 'attention.'

South African corporate law offers little on the oversight function as a standard of directors' conduct, and although the King IV provides guidelines on oversight, it is not law and does not

[89] MBCA official comment 180.
[90] Mongalo T 'Directors' Standards of Conduct Under the South African Companies Act and the Possible Influence of Delaware Law' (2016) 2 *Journal of Corporate and Commercial Law & Practice* 2. Mongalo states that the influence corporation law of Delaware, has earned it the status of being the unofficial national corporate law of that country.
[91] Mongalo T (2016) 4. American Bar Association Section of Business Law, Committee on Corporate Laws, Report on South African Companies Act No. 61 of 1973 and Related Legislation (2001) at 20.
[92] Van Tonder JL (2018) 309. See also Bainbridge, Lopez & Oklan 'The Convergence of Good Faith and Oversight' (2008) 55 *UCLA LR* 571.
[93] Van Tonder JL (2018) 307.
[94] Van Tonder JL (2018) 309-310. See also Veasey 'Policy and Legal Overview of Best Corporate Governance Principles' (2003) 56 *SMU LR* 2136.
[95] Van Tonder JL (2018) 310.
[96] Van Tonder JL (2018) 310.
[97] Van Tonder JL (2018) 313. See MBCA official comment 191.

provide guidance on the standard of conduct expected of directors in this regard. The Act contains no express mention of directors' oversight function. [98] In light of this, Mongalo wonders whether South African policy makers had missed an opportunity, during the corporate law reform process, to adopt the Delaware position in terms of directors' standards of conduct.[99] The lack of provision for the oversight function of directors, is reflected in the poor performance at SOCs in South Africa, in the way that these companies have experienced little growth over the past two decades. In this way, the framework governing directors' duties could do more to contribute to good corporate governance at SOCs.

3.5 CONCLUSION

This paper so far has highlighted the influence of SOCs on the country's GDP, and the vital nature of the goods and services provided by many of these companies. As with any other company, the effective control and management of the company is essential to the interests of the company and the stakeholders. However, in the context of SOCs, the effective control and management of the SOC is vitally important, given the causes and effects on society and the economy, when SOCs do not perform to a certain standard.

This chapter discussed the composition and functions of the board of directors. The two broad functions of the board, namely the decision-making function and the oversight function, were analysed. Furthermore, the issue of board effectiveness, as it relates to the oversight function of directors, was discussed.

This chapter seeks to identify the causal connection between the regulatory framework governing directors' standards of conduct, and the effects thereof on the performance of SOCs. This requires an honest reflection on the performance of SOCs. As mentioned at 3.2.3,[100] one long-standing question in corporate governance is the effect that the board of directors has on organisational performance. The survey by McKinsey & Co found that boards with better dynamics and processes reported stronger financial performance at the companies at which they serve. This survey serves as evidence of the causal connection between the board's efficacy, and the performance outcomes of the company. The oversight function of the board of directors is therefore essential, particularly in ensuring board effectiveness. Compliance by an SOC with the provisions of the PFMA, the Act, and the SOCs founding legislation, is essential in establishing an environment of accountability and responsibility. The board must

[98] Van Tonder JL (2018) 315.
[99] Mongalo T (2016) 12.
[100] See sub-chapter 3.2.3 The Role of Oversight and Board Effectiveness.

evaluate the performance of those tasked with the implementation of certain performance objectives and must take corrective action on a timely basis, to ensure board effectiveness. The Presidential Review Committee (PRC) identified inadequate governance and oversight systems as one of the pressing challenges faced by SOCs, hence the concern over mismanagement, negligent board accountability for poor performance, and corruption, as expressed by the Minister of Public Enterprises. Corporate governance failures as those referred to in Chapter two,[101] are evidence of inadequate governance and oversight systems at SOCs. The extent of the effects of poor performance at SOCs, are seen in the effects of loadshedding on the country's economy.[102]

The DPE identifying that the lack of a standardised framework defining board effectiveness, further proves the causal connection between board efficiency, and the effects it has on the company. This makes sense, as the board of directors are the custodian of corporate governance in a company, and therefore have the responsibility of oversight vested in them. The board effectiveness framework, as proposed by the DPE, would certainly be a great benefit to SOCs in exercising their oversight role, as it would hold the board accountable, and would assist these companies in ensuring specific strategic objectives are met. A board effectiveness framework would ensure that the effectiveness of the board is monitored and measured and will ensure that challenges will be identified and addressed in a timely manner.

'Board effectiveness' unequivocally relates to oversight, which, as emphasised within this chapter, is an underdeveloped function in South Africa. This chapter has identified that although standards of directors' conduct are codified in terms of the Act, the Act still provides no guidelines to directors for their oversight function. The Act does, however, require that directors act with care, skill, and diligence, thus implying that directors are bound to perform an oversight role within the company. King IV provides guidelines regarding this function, although it is still not law. Poor performance at South African SOCs is a reflection of the lack of provision for the oversight function of directors, codified in statute.

Oversight mechanisms should be developed to aid in board effectiveness and profitability. The issues at SOCs have their roots in the process for the appointment and dismissals of board members. The triplicate role of government in SOCs once again comes to the fore. Questionable board appointments have led to questionable financial decisions and

[101] Chapter Two, at 2.6 'Challenges Faced by SOCs in South Africa.'
[102] Chapter Two, at 2.6 'Challenges Faced by SOCs in South Africa.'

management, and little accountability on both sides. It appears that power lines between the shareholder and the board are blurred, whereas a clear division of power between the two would leave room for better accountability. A framework providing for the implementation and safeguarding of that division of power, could potentially see SOCs boards becoming a better custodian of corporate governance. SOCs would potentially benefit from ethical leadership, by appointing board members who meet the required standards of experience and qualifications for the position. The PFMA refers to the executive authority's, 'ownership and control' powers, in terms of which the relevant shareholders may appoint or remove board members and executives, or control majority in board or general meetings of SOCs under their control. The division of power between the shareholder and the board may well be blurred, however board members remain accountable to their fiduciary duties in terms of common law principles and statute. This leads us back to the overarching question: are the fiduciary duties imposed on directors efficient in aiding corporate governance at SOCs in South Africa? Considering the state of governance at most SOCs, the blame has easily been shifted to political meddling and shareholder involvement. However, as the board of directors of a company, their duties, inter alia, are to safeguard the financial management of the company, and to be the custodian of corporate governance. The framework sufficiently provides for guidelines for directors' conduct, however the efficiency of the framework in terms of aiding better corporate governance at SOCs is doubtful.

In terms of active oversight mechanisms, I believe an effective system in this regard, would influence better dynamics and processes, ultimately resulting in stronger financial processes. Studies have suggested that there is a positive correlation between corporate governance and performance (various measures of performance). As the custodian of corporate governance in a company, the responsibility of oversight is vested in the board of directors. A clear framework that would enable an efficient assessment for evaluation of the board's performance, as well as the company's performance, would increase board effectiveness. Effective oversight mechanisms would additionally assist the shareholding minister, to which the board is accountable, in ensuring that specific strategic objectives are met. A framework that would assist in board evaluation, and positively impact board effectiveness, is particularly important I believe, in the South African context, given the large impact these companies have on GDP, and society. It is important that the effectiveness of a board is measured, so that challenges may be identified and addressed in a timely manner.

The second function of directors, namely the director's decision-making function, is more developed in terms of South African law. Regarding this particular function, Van Tonder discourages the notion of a passive director, in light of the director-centric model of corporate governance. This chapter has emphasised that the company's business and affairs must be managed under the control and direction of the board, subject to the MoI. The *Fisheries Development Corporation of SA Ltd v Jorgensen*[103] case highlights that a director's duty of care and skill depends on the nature of the business, and any obligations assumed by him or assigned to him. In this context, this chapter has argued that directors of SOCs must apply a higher degree of care and skill, given the nature of these companies and the obligations assigned to them.

This chapter has successfully highlighted the two main functions of directors and has identified certain challenges and shortcomings of the regulatory framework, as it related to directors' duties and functions. Essentially, this chapter has identified that although the regulatory framework provides established guidelines for directors' duties and standards of conduct, it falls short in providing a guideline for directors' standard of conduct in exercising their oversight function. The Companies Act does a good job in codifying directors' standards of conduct and is in line with international standards of corporate governance. However, in the context of the board of directors as the custodian of corporate governance, the current state of many SOCs in South Africa displays poor corporate governance practices. In light of this, it appears that the regulatory framework governing directors' duties and standards of conduct, particularly at SOCs, requires more development.

[103] *Fisheries Development Corporation of SA Ltd v Jorgensen* [1980] 4 All SA 525.

CHAPTER FOUR

LEGAL FRAMEWORK GOVERNING DIRECTORS' DUTIES AT STATE-OWNED COMPANIES

4.1 INTRODUCTION

This chapter provides an in-depth synopsis of the legal duties applicable to directors at State-Owned Companies (SOCs). As emphasised throughout this paper, the board of directors is the custodian of corporate governance in a company. A company must act through its individuals, as it is a separate entity from its management and shareholders.[1] In light of the framework governing directors' duties in South Africa, the question of 'freedom and discretion' in relation to directors and their decision-making is a worthy discussion, considering the political meddling that often occurs at the hands of the shareholding ministers.

The duties and responsibilities of directors are found in the Constitution,[2] the Public Finance Management Act (PFMA)[3] and National Treasury regulations, the Companies Act (the 'Act')[4] and regulations, the respective founding legislation for an SOC, common law, as well as the Memorandum of Incorporation of the company.[5]

This chapter identifies and explains the duties of directors in terms of common law and the relevant legislation, as well as recommendations in terms of the King IV Report on Corporate Governance.[6] The South African regulatory framework governing directors' duties creates various liabilities, remedies and penalties to discourage non-compliance.[7] SOCs are subject to clear provisions in terms of the PFMA, and yet some SOC directors have been implicated in meddling in the awarding of lucrative tenders, falsifying qualifications and other fraudulent

[1] In *Dadoo Ltd and Others Appellants v Kurgersdorp Municipal Council Respondents* 1920 AD 530, Innes J held that 'A registered company is a legal *persona* distinct from the members who compose it.' This sentiment is codified in s19(1)(a) of the Companies Act 71 of 2008, where it states the legal status of companies.
[2] Constitution of the Republic of South Africa, 1996.
[3] Public Finance Management Act 1 of 1999.
[4] Companies Act 71 of 2008.
[5] State-Owned Company Board Evaluation Framework Version 2, 2021 Department of Public Enterprises (2021) 21 (hereafter *DPE – SOC Board Evaluation Framework*).
[6] The King IV Report on Corporate Governance for South Africa 2016, The Institute of Directors in Southern Africa (hereafter *King IV Report*).
[7] Olivier EA 'Regulating Against False Corporate Accounting: Does the Companies Act 71 of 2008 Have Sufficient Teeth?' (2021) 33 *SAMJL* Olivier refers to the framework governing director duties, and how it attempts to discourage and penalise non-compliance in terms of a company's financial reporting obligations specifically.

practices.[8] Compliance in terms of the Act, the PFMA and King codes at some SOCs thus remain questionable.

This chapter assesses and discusses recommendations from King IV regarding the board of directors, particularly at SOCs. Essentially, this chapter investigates the extent to which the framework governing the duties and responsibilities of the board of directors, enforces good corporate governance at SOCs in South Africa. It identifies certain challenges in the current framework, and certain areas that require further development.

The following sub-chapter analyses the legal duties and responsibilities imposed on directors, as individuals, at state-owned companies.

4.2 LEGAL DUTIES AND RESPONSIBILITIES OF DIRECTORS AT SOC's

King IV requires that the board behaves as a good corporate citizen, while upholding the principles of the King IV Report on Corporate Governance (2016). SOC board members are responsible to a greater number of stakeholders, given the contribution of SOCs to the country's GDP. SOCs serve as the corporate vehicle for the government to supply the population with water, electricity, sanitation, and transportation, and are among the main sources of urban employment,[9] thus perhaps carry a greater duty to be good corporate citizens. This subchapter discusses the sources of director duties, certain relevant principles, and identifies areas that are potential challenges to sustainable corporate governance standards.

4.2.1 Common Law

Although South African common law originates from Roman-Dutch law, South African company law is largely influenced by English company law.[10] In fact, the first Companies Act (46 of 1926), was based on English statutory law, and the new Companies Act (71 of 2008) has modified some English law concepts.[11] When interpreting unclear portions of statutory company law, South African courts have often looked to other jurisdictions, especially to

[8] Thabane T & Snyman-Van Deventer E 'Pathological Corporate Governance Deficiencies in South Africa's State-Owned Companies: A Critical Reflection' (2018) 21 *PER / PELJ* 11. See also Brümmer & Sole 2008 *Mail & Guardian*.

[9] Organisation for Economic Co-Operation and Development 'South Africa Policy Brief' (2015) available at *http://www.oecd.org/corporate/south-africa-state-owned-enterprise-reform.pdf.*

[10] Girvin SD 'The Antecedents of South African Company Law' (2007) 13 *The Journal of Legal History* 63-77. See also Levenberg PN 'Directors' Liability and Shareholder Remedies in South African Companies – Evaluating Foreign Investor Risk' (2017) 26 *Tulame Journal of International and Comparative Law* 1.

[11] Girvin SD 'The Antecedents of South African Company Law' (2007) 13 *The Journal of Legal History* 63-77. Levenberg P *Directors' Liability and Shareholder Remedies* (2017) 12; Olivier EA 'The Capacity Provisions in the Companies Act' (2020) 31 *Stellenbosch Law Review* 534.

England.[12] This is in line with section 5(2) of the Companies Act which expressly provides that a court can, when interpreting or applying the Act, consider foreign company law.[13]

A director is subject to three fiduciary duties in terms of common law, namely: the duty to act in good faith and loyalty to his company; the duty to exercise his or her powers as a director bona fide in the best interests of the company; and lastly, the duty to avoid a conflict of interest between that of the company and his own or her own interests.[14] A director owes a further duty, to display 'reasonable care and skill;' a duty which is distinct from the three fiduciary duties.[15]

This subchapter however does not address each of these broad fiduciary duties, but closely describes two more narrow instances of breaches of these duties, as recognised at common law.

4.2.1.1 The 'Secret profit' rule

A well-established rule in terms of common law, is that a director must act in the best interests of the company, which includes the best interests of both present and future shareholders.[16] A director may not place themselves in a position where a personal interest conflicts, or potentially conflicts, with the duty to act in the best interests of the company.[17] As decided in *Phillips v Fieldstone Africa*,[18] a director may not place himself in a position of a potential conflict of interest between himself and the company, where he may possibly secure a benefit for himself at the expense of the company.[19] In *Industrial Development Consultants Ltd. v Cooley*,[20] Mr Cooley, managing director of Industrial Development Consultants (IDC), was told that a lucrative project by the Eastern Gas Board sought not to contract with his firm, but directly with him instead.[21] As a result, Mr Cooley resigned from his position as managing director, on early notice, and began work on the gas board on his own account.[22] When the IDC found out, they sued him for his breach of loyalty.[23] The court held that even though the IDC had no chance of getting the contract, if they were aware of the situation with Mr Cooley, they

[12] Levenberg P (2017) 13.
[13] Levenberg P (2017) 13. Referring to s5(2) of Act 71 of 2008
[14] Mupangavanhu B 'Fiduciary Duty and Duty of Care under Companies Act 2008' (2017) 28 *Stellenbosch Law Review* 151
[15] Mupangavanhu B (2017) 151.
[16] Havenga M 'Directors' exploitation of corporate opportunities and the Companies Act 71 of 2008' 2013 *Journal of South African Law* 257.
[17] *Industrial Development Consultants Ltd v Cooley* [1972] 2 All ER 162 172. *Boardman v Phipps* 1966 3 All ER 721 (HL). See also Havenga M (2013) 257.
[18] *Phillips v Fieldstone Africa (Pty) Ltd and Another* [2004] 1 All SA 150 (SCA).
[19] *Phillips v Fieldstone Africa (Pty) Ltd* [2004] 1 All SA 150 (SCA).
[20] *Industrial Development Consultants Ltd v Cooley* [1972] 2 All ER 162 172.
[21] *Industrial Development Consultants Ltd v Cooley* [1972] 2 All ER 162 172.
[22] *Industrial Development Consultants Ltd v Cooley* [1972] 2 All ER 162 172.
[23] *Industrial Development Consultants Ltd v Cooley* [1972] 2 All ER 162 172.

would not have released him.[24] The court decided that as managing director, Mr Cooley had 'one capacity, and one capacity only.'[25] That capacity was as director of the IDC. It was held that all information that came to Mr Cooley should have been passed on.[26]

To determine the possibility of a conflict of interest, Havenga argues that a 'common sense' approach is followed, which entails an assessment of whether or not a reasonable person would consider the relevant facts and circumstances of the case and think that there was a real possibility of conflict.[27] In practice, this rule entails that a director should not make any profit from their position, other than those specified in the company's constitutive documents, or in a separate contract which may exist between the director and the company.[28] Essentially, directors may not make a profit, or retain a profit made in the course of their office as directors, without the informed consent of the company, as these 'secret profits' are to be disregarded.[29] This is known as the 'secret profit' rule.[30] This rule derived from the case of *Robinson v Randfontein Estates Gold Mining Co Ltd*.,[31] where it was held that where one is under the duty to protect the interests of another, he is not allowed to make a secret profit at their expense, or place himself in a position where his personal interests is in conflict with this duty.[32] It is clearly evident that directors must not only avoid conflicts of interest, but they must also avoid placing themselves in a situation wherein their personal interests conflict with their duties to the company.

According to Havenga, the term 'secret profit' is somewhat misleading, as the rule applies even if the advantage was obtained properly and in good faith, and even if it was not at the expense of the company.[33] The court in *Regal (Hastings) v Gulliver*,[34] held that that the rule which required directors to account for profits made while they are in a fiduciary relationship, is not dependant on fraud, the absence of bona fides, or upon the question of whether or not the profit should have gone to the company.[35] It was held that liability arises merely from the fact that profit was made.[36] The deciding factor in terms of this rule, is whether or not the profit was

[24] *Industrial Development Consultants Ltd v Cooley* [1972] 2 All ER 162 172.
[25] *Industrial Development Consultants Ltd v Cooley* [1972] 2 All ER 162 172.
[26] *Industrial Development Consultants Ltd v Cooley* [1972] 2 All ER 162 172.
[27] Havenga M (2013) 257.
[28] Havenga M (2013) 258.
[29] Havenga M (2013) 258.
[30] Havenga M (2013) 258.
[31] *Robinson v Randfontein Estates Gold Mining Company Co.* [1921] AD 168 177.
[32] *Robinson v Randfontein Estates Gold Mining Company Co.* [1921] AD 168 177.
[33] Havenga M (2013) 258.
[34] *Regal (Hastings) Ltd v Gulliver* [1942] 1 All ER 378.
[35] *Regal (Hastings) Ltd v Gulliver* [1942] 1 All ER 378.
[36] *Regal (Hastings) Ltd v Gulliver* [1942] 1 All ER 378.

obtained as a result of the director's occupation of office.[37] The principles from *Regal (Hastings)* were reaffirmed in *Phillips v Fieldstone,* where it was further held that after full disclosure by the director, only the free consent of the principal will suffice as a defence.[38]

4.2.1.2 The 'Corporate opportunity'

In terms of common law, an exploitation of a 'corporate opportunity' occurs in the instance of conflicting interests and profit-making by a director for personal benefit, rather than for the company.[39] In *Da Silva v CH Chemicals (Pty) Ltd*.,[40] it was held that if a director has acquired an opportunity for his own benefit rather than for that of the company, he is said to have expropriated a corporate opportunity.[41] In this instance, the intention of the director is disregarded, the acquisition is treated as having been made on behalf of the company, and the company may claim the acquired property from the director.[42]

The court held that the inquiry into a perceived corporate opportunity involves a close and careful examination of all relevant circumstances, particularly including the opportunity in question, to determine whether the exploitation of the opportunity by the director whether for his or her own benefit or that of another, has resulted in a conflict between the director's personal interests and those of the company – which the director was duty-bound to protect and advance.[43]

In *Robinson v Randfontein Estate Gold Mining Co ltd,* the court dealt with an issue where a director acquired a corporate opportunity.[44] The court held that where one man has the duty to protect the interest of the other, he is not allowed to make a secret profit at the other's expense, or place himself in a position where his interests conflict with his duty.[45] In this matter, it appears that a director is only liable for a breach of duty if he buys or sells a property in which the company may be interested in, or where he is specifically charged with buying or selling that property.[46] A transaction that took place may however be validated, even where the director has a conflict of interest, by the consent of the principal, following full disclosure by the

[37] *Regal (Hastings) Ltd v Gulliver* [1942] 1 All ER 378.
[38] *Phillips v Fieldstone Africa (Pty) Ltd* (2004) (3) SA 465 (SCA).
[39] Havenga M (2013) 258.
[40] *Da Silva and Others v C H Chemicals (Pty) Ltd* 2008 (6) SA 620 (SCA) 110 at 17.
[41] *Da Silva and Others v C H Chemicals (Pty) Ltd* 2008 (6) SA 620 (SCA) 110 at 17.
[42] *Da Silva and Others v C H Chemicals (Pty) Ltd* 2008 (6) SA 620 (SCA) 110 at 17
[43] *Da Silva v CH Chemicals (Pty) Ltd* 2008 (6) SA 620 (SCA) 6271-J.
[44] *Robinson v Randfontein Estates Gold Mining Company Co.* 1921 AD 168 177-78.
[45] *Robinson v Randfontein Estates Gold Mining Company Co.* 1921 AD 168 177-78.
[46] *Robinson v Randfontein Estates Gold Mining Company Co.* 1921 AD 168 177-78.

director or agent.[47] In terms of common law, the general rule is that the disclosure must be made to the members in a general meeting, and only they have the power to approve the contract.[48] The transaction must be approved by all of the shareholders and not simply a majority, to prevent directors from committing a fraud upon the company.[49]

Although rooted in Roman-Dutch law, common law duties remain relevant even in the modern era of business and corporate governance. Common law principles such as the corporate opportunity and secret profit rules, remain applicable. Common law fiduciary duties have been partially codified in the new Companies Act, corroborating the relevance and importance of common law in the modern world.

4.2.2 The Companies Act 71 of 2008

While the regulation of directors' duties were largely left to common law, the Companies Act of 1973[50] ("1973 Act") added specific statutory obligations, which included directors' fiduciary duties and directors' obligations to exercise due care and diligence.[51] The Companies Act of 2008 (the "Act") contains a partial codification of common law duties.[52] The Act is defined by Jennings as 'so novel' and 'so flexible' that is has the ability to appropriately regulate from the smallest of companies to the largest.[53] Mupangavanhu argues that the hope and goal of this law reform was to ensure that the standards of directors' conduct are made more clear, more accessible and more enforceable in a manner that improves corporate governance.[54]

Section 66(1) of the Act imposes a positive duty on a company's board of directors to manage the company, which entails that the business and affairs of the company must be managed by or under the direction of its board, which has the authority to exercise all of the powers and perform any of the functions of the company, except to the extent that the Act or the company's MOI provides otherwise.[55] To guard against the abuse of this power, the Act imposes several duties on directors.

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[47] *Robinson v Randfontein Estates Gold Mining Company Co.* 1921 AD 168 177-78.
[48] *Robinson v Randfontein Estates Gold Mining Company Co.* 1921 AD 168 177-78.
[49] Levenberg P (2017) 19 -20.
[50] Companies Act 61 of 1973
[51] Havenga M (1997) 263. Referring to Companies Act 61 of 1973.
[52] Havenga M (2013) 263
[53] Jennings BPL 'Are Shareholders Exclusive Beneficiaries of Fiduciary Obligations in South Africa? The Role of Fiduciary Obligations in the 21st Century' (2015) 1(2) *Journal of Corporate and Commercial Law & Practice* 55.
[54] Mupangavanhu B (2017) 152.
[55] s 66(1) of Act 71 of 2008.

4.2.2.1 Duty to Disclose Personal Financial Interests:

Section 75 of the Act is concerned with the disclosure of directors' personal financial interests in a contract.[56] In terms of section 75(5), a director who has a personal financial interest in respect of a matter, must disclose the interest and its general nature before consideration of the matter at a company meeting.[57] A director is required to disclose any material information relating to the matter known to him, and if requested to do so, may disclose any observations or pertinent insights relating to the matter.[58] In this instance, the common law position is confirmed, that full disclosure to the company, and approval by the company, is required to avoid directors' liability.[59] In terms of section 75(6), it is required that the nature and extent of any personal financial interest, and the material circumstances relating to the acquisition of that interest, is promptly discussed.[60] Although s75 serves as a partial codification of the common law approach to serving the best interests of the company, the common law approach has a more strict application. In terms of common law, a director may not even place himself in a position of potential conflict.[61] Furthermore, in *Industrial Development Consultants Ltd. v Cooley*, it was held that *all* information that came to the director should have been passed on to the company,[62] whereas in terms of s75, any material information must be passed on. The board's approval of a transaction or agreement is valid, despite a personal financial interest of a director or person related to a director, if it was approved in terms of s75, or if it had been ratified by ordinary resolution of the shareholders.[63] The court may, on application, declare a transaction as valid and approved by the board or shareholders, despite the failure of the director to satisfy the requirements of section 75(8).[64] This particular section, when irregularly applied, may prove to be problematic given that in recent years executives at large SOCs have been criticised for using their position to satisfy personal financial interests. The common law approach on the other hand, followed a more strict approach to this kind of breach, as the 'secret profit' rule applied even if secret profits were attained properly and in good faith.[65] In *Robinson*

[56] s75(4) of Act 71 of 2008 reads: 'At any time, a director may disclose any personal financial interest in advance, by delivering to the board, or shareholders in the case of a company contemplated in subsection (3), a notice in writing setting out the nature and extent of that interest, to be used generally for the purposes of this section until changed or withdrawn by further written notice from that director.'
[57] s75(5) of Act 71 of 2008.
[58] s75(5)(b) and (c)of Act 71 of 2008. In terms of section 75(8) of the Act, an interested party may apply to a court to have an agreement or transaction approved by the board, declared invalid.
[59] Havenga M (2013) 264.
[60] s 75(6) of Act 71 of 2008.
[61] *Phillips v Fieldstone Africa (Pty) Ltd* [2004] 1 All SA 150 (SCA).
[62] *Industrial Development Consultants Ltd v Cooley* [1972] 2 All ER 162 172.
[63] s 75(7)(a) and (b)(*i*) of Act 71 of 2008.
[64] s 75(8) Act 71 of 2008.
[65] Havenga M (2013) 258.

v Randfontein Estates Gold Mining Co Ltd.,[66] it was held that the such a transaction must be approved by *all* shareholders, not just the majority, to prevent directors from committing a fraud on the company.[67]

In the context of South African SOCs, one example of an SOC director using his position, and personal financial interests, to benefit himself at the expense of the company, is the Kusile power station corruption incident at Eskom.[68] In this matter, former CEO Matshela Koko used his politically-connected, businessman friend, Thabo Owen Mokwena, to launder a bribe payment.[69] Investigations found that Mokwena had close connections with the State Security Agency, and is connected to the ANC's Chancellor House Holdings.[70] In 2015, the Kusile Control and Instrumentation (C&I) contract was awarded to Asea Brown Boveri (ABB) South Africa (Pty) Ltd, with a part of the ABB group based in Switzerland.[71] ABB has admitted to paying bribes to secure the contract, and in 2020, ABB repaid Eskom up to R1.56billion.[72] The United States Department of Justice signed a plea agreement with ABB South Africa in December 2022, in terms of which ABB agreed to pay more than R5.544billion to resolve an investigation into the violations, stemming from the bribery of a 'high ranking official' at South Africa's state-owned energy company.[73] Koko and Mokwena were arrested and charged with allegations of fraud, corruption and money laundering, in October 2022.[74]

Another example of directors benefiting themselves at the expense of the SOC, is the incident of a South African Express (SA Express) contract, worth R400 million, which was found to be riddled with procurement irregularities.[75] Four suspects were arrested, including former SA Express Executive for the Commercial division of the airline, Tebogo Van Wyk.[76] In 2014, the North West government sought to reintroduce commercial aircraft to the province, with a

[66] *Robinson v Randfontein Estates Gold Mining Company Co.* [1921] AD 168 177.
[67] *Robinson v Randfontein Estates Gold Mining Company Co.* [1921] AD 168 177.
[68] 'When Integrity Fails: The Networks Linked to Eskom Contracts' *OUTA* 30 March 2023 available at *https://www.outa.co.za/blog/newsroom-1/post/when-integrity-fails-the-networks-linked-to-eskom-contracts* (accessed 12 September 2023).
[69] *OUTA* (2023).
[70] *OUTA* (2023).
[71] *OUTA* (2023).
[72] *OUTA* (2023).
[73] *OUTA* (2023).
[74] *OUTA* (2023).
[75] Vincent Cruywagen 'Four Suspects Charged in North West Court Over Dubious Mulit-Million-Rand SA Express Contract' *Daily Maverick* available at *https://www.dailymaverick.co.za/article/2022-10-05-four-suspects-charged-in-north-west-court-over-dubious-multimillion-rand-sa-express-contract/* (accessed 30 August 2023).
[76] Cruywagen V *Daily Maverick* (2023).

subsidy of R400 million.[77] The NPA found that an amount of R51 million was channelled irregularly through the charged companies, and money was being paid for services not rendered.[78] The suspects are charged with 34 allegations, including allegations of fraud, corruption, money laundering, and contraventions of the PFMA.[79]

These two instances are clear contraventions of section 75(5) of the Act. In terms of the common law position, the implicated directors should not even have placed themselves in the position of potential conflict. Although section 75 provides clear guidelines in terms of disclosing personal financial interests, these two examples, out of many similar instances, prove that section 75 does not necessarily keep directors on their toes, and is not effective in discouraging dishonest corporate behaviour.

4.2.2.2 Fiduciary Duty to Act in the Best Interests of the Company:

Section 76 of the Act addresses the standards of directors' conduct, which includes the obligations of directors to act with the degree of care, skill and diligence reasonably expected of a person carrying out the functions of a director.[80] In terms of this section, 'director' has a wide meaning, extending to a prescribed officer and a member of a board committee or of the audit committee.[81] Section 76(2) of the Act emphasises that a director may not use their position to gain advantage for themselves, or another person other than the company, or knowingly cause harm to the company.[82] This section of the Act thus serves as a partial codification of the 'corporate opportunity' common law principle, in terms of which a director may not exploit his position as director to serve a personal interest, or 'corporate opportunity.' Instances of directors exploiting 'corporate opportunities' are often the cause of corporate governance failures at SOCs, as discussed in Chapter Two.[83]

Section 76 essentially codifies the decision in *Industrial Development Consultants Ltd v Cooley,* where it was held that the director of a company has 'one capacity, and one capacity

[77] Cruywagen V *Daily Maverick* (2023).
[78] Cruywagen V *Daily Maverick* (2023).
[79] Cruywagen V *Daily Maverick* (2023).
[80] s 76 of Act 71 of 2008.
[81] In terms s76(1) of Act 71 of 2008, 'director' includes an alternate director, and –
(a) 'a prescribed officer; or
(b) A person who is a member of a committee of a board of a company, or of the audit committee of a company, irrespective of whether or not the person is also a member of the company's board.'
[82] s 76(2) of Act 71 of 2008.
[83] Chapter Two at 2.5 'Corporate Governance Failures in South Africa.'

only,' which is the capacity as director.[84] Section 76(3) of the Act confirms the fundamental fiduciary relationship between a director and the company whose board they serve.[85]

4.2.2.3 The Duty of Care, Skill and Diligence:

The duty of care, skill, and diligence in terms of s76(3)(c)(*i*), states:

> '(3) [... a director of a company, when acting in that capacity, must exercise the powers and perform the functions of director –
>
> (c) with the degree of care, skill and diligence that may reasonably be expected of a person-
>
> (i) when carrying out the same functions in relation to the company as those carried out by that director.'

It thus imposes an objective standard, as the standard provided for is that of a reasonable person.[86]

However, s76(3)(c)(*ii*) introduces a subjective element to the objective standard, as it considers the knowledge, skill and experience of a director.[87] Therefore, if a director does not possess a high quality of skills, experience or knowledge, a lower level of care and skill is expected of him, provided he exercises the minimum reasonable level of care and skill.[88] The subjective standard of skill, knowledge and experience is therefore only taken into account if it improves or increases upon the objective standard.[89] Van Tonder argues that the combined effect of the two subsections appears to put aside the director's personal level of skills, in favour of an objective test of what is reasonably expected of a director, so that an incompetent director who fails to match the minimum threshold can be held liable.[90] However, if a director is appointed to exhibit a higher professional or technical competence, like a lawyer or engineer, his own liability threshold is placed above that of the reasonable director, and he must be judged by the standards of a reasonably competent exponent of his industry.[91] Therefore, if a director's skill and knowledge exceeds that of a reasonably diligent person, it must be considered when deciding whether or not the director in question had exercised reasonable care and skill, and

[84] *Industrial Development Consultants Ltd v Cooley* [1972] 2 All ER 162 172.
[85] s 76(3) of Act 71 of 2008.
[86] Van Tonder JL (2016) 568. See also Stein & Everingham 'The New Companies Act Unlocked' 244, Cassim et al *Contemporary Company Law* 559, Botha (2009) 30 *Obiter* 710, Cassidy (2009) 3 *Stell LR* 385, Du Plessis (2010) *Acta Juridica* 269.
[87] Van Tonder JL (2016) 568.
[88] Van Tonder JL (2016) 568.
[89] Van Tonder JL (2016) 568.
[90] Van Tonder JL (2016) 569.
[91] Van Tonder JL (2016) 569.

has complied with the requirements of s76(3)(c).[92] Van Tonder thus argues that the objective standard is reasonable and flexible.[93]

The board of directors at SOCs must exhibit a higher level of skills, knowledge, and experience, given the mandate of an SOC to provide the country with certain goods and services. An objective, reasonable and flexible standard to assess a director's skill, knowledge, and experience, is beneficial to South African SOCs, in light of the discriminatory history of the South African economy and affirmative action policies imposed as a result thereof. However, scandals regarding the falsifying of qualifications of directors, such as the scandal at SAA, still take place.[94] In this regard, I agree with Olivier's sentiments, that the legislature can only do so much from a legislative perspective to discourage irregularities,[95] as criminals will still find a way to escape the law.

McLennan argues that the word 'reasonably' used throughout the section appears to conflate the duties into one objective standard.[96] Therefore, the subjective elements under s76(3)(*c*) do not overshadow or undermine the objective elements but are rather in addition to the objective standard.[97]

Nonetheless, according to Van Tonder, the duty of care, skill and diligence indirectly reflects the importance that the legislature has placed on corporate governance best practices.[98] He argues that if the provision was structured in reasonable terms, a high standard of corporate governance would not be achievable. According to Van Tonder, the provision must be interpreted in relation to commercial realities, rather than outdated precedents.[99] This is important because commercial realities have rapidly changed over the last decade, and the framework governing corporate governance must reflect that. The duty of care, skill and diligence must therefore be interpreted to reflect current commercial realities faced by SOCs and must reflect corporate governance best practices.

[92] See s76(3)(c) of Act 71 of 2008.
[93] Van Tonder JL (2016) 569.
[94] Thabane T & Snyman-Van Deventer E 'Pathological Corporate Governance Deficiencies in South Africa's State-Owned Companies: A Critical Reflection' (2018) *PER / PELJ* Vol 21 11. See also Brümmer & Sole (2008) *Mail & Guardian*.
[95] Olivier EA (2021) 22.
[96] Van Tonder JL (2016) 569. See also McLennan (2009) 1 *TSAR* 186.
[97] Van Tonder JL (2016) 569.
[98] Van Tonder JL (2016) 569.
[99] Cassim et al *Contemporary Company Law* 558.

Ultimately, directors have a duty to make informed business decisions. They are required to inform themselves of all material information reasonably available to them, prior to making a decision.[100] In terms of s76(4)(*b*) and (5) of the Act, a board is allowed to retain consultants or other advisors, to assist directors in becoming more informed.[101]

4.2.2.4 Liability of Directors

Section 77 of the Act addresses the liability of directors and prescribed officers.[102] This liability is towards the company, as s77(3) of the Act holds a director liable for and losses, damages or costs sustained by the company, as a direct consequence of a director's actions, as prescribed under s77(3). In terms of section 77(2)(*a*), and in accordance with the principles of the common law relating to breaches of a fiduciary duty, a liability may arise for any loss, damage or costs sustained by the company as a consequence of any breach, by a director, of a duty contemplated in section 75, 76(2), 76(3)(*a*) or (*b*).[103]

In terms of liability to third parties, according to section 218(2) of the Act, any person who contravenes any provision of the Act, is liable to any other person for loss or damage suffered by that person as a result of the contravention[104] This liability is in addition to any other liability incurred in terms of the common law or the Act.[105] In *Forum Exporters International v Park Village Auctioneers (Pty) Ltd.,*[106] the plaintiffs brought two claims against the Park Village Auctioneers (PVA), one against the company, and one against one of the directors at PVA, in his capacity as director.[107] The plaintiffs based their claim on common law, and on s76(3) read with s218(2) of the Act.[108] The plaintiffs alleged that the director of PVA had expropriated his position as director to benefit himself, and failed to act in good faith and proper purpose, thus breaching his statutory duties.[109] The court decided that the evidence was insufficient to warrant the application of s76(3) and therefore s218(2) does not apply either.[110] The court thus dismissed the second claim.[111] In *Lomastep (Pty) Ltd v Galego,*[112] it was held that s218(2) of

[100] Van Tonder JL (2016) 576.
[101] Section 76(4)(b) and (5) of Act 71 of 2008.
[102] s 77 of Act 71 of 2008.
[103] s 77(2)(a) of Act 71 of 2008.
[104] s 218(2) of Act 71 of 2008 deals with civil actions and reads: 'Any person who contravenes any provision of this Act is liable to any other person for any loss or damage suffered by that person as a result of that contravention.'
[105] Havenga M (2013) 267.
[106] *Forum Exporters International v Park Village Auctioneers (Pty) Ltd.* [2021] JOL 15131 (GJ)
[107] *Forum Exporters International v Park Village Auctioneers (Pty) Ltd. [2021] JOL 15131 (GJ)* at par 3
[108] *Forum Exporters International v Park Village Auctioneers (Pty) Ltd. [2021] JOL 15131 (GJ) at par 9*
[109] *Forum Exporters International v Park Village Auctioneers (Pty) Ltd. [2021] JOL 15131 (GJ) at par 137*
[110] *Forum Exporters International v Park Village Auctioneers (Pty) Ltd. [2021] JOL 15131 (GJ) at par 157*
[111] *Forum Exporters International v Park Village Auctioneers (Pty) Ltd.* [2021] JOL 15131 (GJ) at par 158.
[112] *Lomastep (Pty) Ltd v Galego and others* [2023] JOL 59955 (GP) at par 21.

the Act should not be interpreted as a standalone provision, and should rather be interpreted purposively. The court in *Lomastep* referred to Uithaler J, where he argued that s218(2) should not be interpreted in a literal way.[113] In *De Bruyn NP v Steinhoff,*[114] it was held that s218(2) of the Act should not be interpreted on the basis that it discards the common law requirements of fault, foreseeability, causation and a proper plaintiff.[115] Unterhalter J argued that in terms of common law, directors are not held liable to shareholders for loss of value of their shares.[116] He argued that in terms of s218(2) of the Act, directors cannot be read to hold directors liable for breach of their duties in terms of s76(3), when common law does not recognise such a liability.[117] This case reaffirmed that s218(2) of the Act should not be interpreted in a literal way.[118] Unterhalter J held that the provision recognises liability for loss or damage arising from a contravention of the Companies Act.[119] Unterhalter J argues that s218(2) of the Act imports common law concepts of liability, and that legislation should be interpreted in conformity with the common law.[120]

4.2.2.5 The Business Judgement Rule

The business judgement rule, now enacted in the Act, protects directors who face liability claims for breaching their duty to act in the best interests of the company, and their duty to act with care, skill and diligence.[121] The availability of the defence mechanism, the business judgement rule, protects directors from personal liability for harm or losses incurred due to specific decisions and/or actions by the board.[122] In terms of section 76(4)(*a*) of the Act, a director would have satisfied the obligations of section 76(3)(*b*) and (*c*), if certain requirements are met.[123] The requirements to be met in order for the business judgement to apply, include:

i. ‘That the director must have taken reasonably diligent steps to become informed about the subject matter of a business decision to be made;[124]

[113] *Lomastep (Pty) Ltd v Galego and others* [2023] JOL 59955 (GP) at par 20.
[114] *De Bruyn NP v Steinhoff International Holdings N.V. and Others* 2022 (1) SA 442 (GJ).
[115] *De Bruyn NP v Steinhoff International Holdings N.V.* par 185.
[116] *De Bruyn NP v Steinhoff International Holdings N.V.* par 189.
[117] *De Bruyn NP v Steinhoff International Holdings N.V.* par 189.
[118] *De Bruyn NP v Steinhoff International Holdings N.V.* par 191.
[119] *De Bruyn NP v Steinhoff International Holdings N.V.* par 191.
[120] *De Bruyn NP v Steinhoff International Holdings N.V.* par. 193.
[121] Mupangavanhu B (2017) 157.
[122] Van Tonder JL ‘A Primer on the Directors’ Oversight Function as a Standard of Directors’ Conduct Under the Companies Act 71 of 2008’ (2018) 39(2) *Obiter* 303.
[123] s 76(4) (a) (*I – iii*) of Act 71 of 2008.
[124] s 76(4)(a)(i) Act 71 of 2008.

ii. The director, or any related person, must not have conflict of interests, whether personal or financial, in a matter relating to the business decision to be made by the company board;[125] and

iii. The director must have complied with the requirements of s75, in respect of any personal financial interest;[126] and

iv. That the director must have made a decision; and that there must be a rational basis to believe that the decision made is in the best interest of the company.'[127]

v. The director is entitled to rely on any of the persons referred to in subsection (5);[128] or any person to whom the board may reasonably have delegated the authority to perform one or more of the board's functions;[129] and

vi. The director may rely on any information presented by any of the persons specified in subsection (5).[130]

The board's management function is divided into two broad areas: decision-making and oversight.[131] The business judgement rule relates to the decision making and oversight function of directors, as it relates to the duty of care, skill and diligence.[132] The rule presumes that directors, when making a decision, 'have taken reasonably diligent steps to become informed about the matter, and that the decision was made in the best interests of the company'.[133] Van Tonder thus argues that, through the lens of section 76(4)(a)(*i*) of the Act, the business judgement rule sets out the decision making function of the duty of care, skill and diligence as a standard of directors' conduct.[134]

The business judgement rule will not be applicable in the instance where directors have failed to adequately carry out their monitoring and oversight function.[135] The rule only applies where directors have followed a due process in order to exercise a business judgement.[136] In the instance where a director is alerted of possible wrongdoing, and consciously decides not to act or fails to act, their decision amounts to a business decision.[137]

[125] s 76(4)(a)(*ii*) (aa) Act 71 of 2008.
[126] s 6(4)(a)(*ii*) (bb) of Act 71 of 2008.
[127] s 76(4)(a)(*iii*) of Act 71 of 2008.
[128] s 76(4) (b) (*i*) (aa) of Act 71 of 2008.
[129] s 76(4) (b) (*i*) (bb) of Act 71 of 2008.
[130] s 76(4)(b)(*ii*) of Act 71 of 2008.
[131] Van Tonder JL (2018) 303.
[132] s 76(3)(c) of Act 71 of 2008.
[133] s 76(4)(a)(i), (ii), and (iii) of Act 71 of 2008.
[134] s 6(4)(a)(i) of Act 71 of 2008.
[135] *Aronson v Lewis* 473 A.2d 805 813 (Del. 1984).
[136] *Aronson v Lewis* 813.
[137] *Aronson v Lewis* 813.

Van Tonder argues that the oversight function creates an incentive for directors to act or respond to reasonable suspicion of wrongdoing in order to gain the benefit of the business judgement rule.[138] In terms of common law, a director is only required to exercise the standards of care and skill which could reasonably be expected of a person with his knowledge and experience.[139] However, in terms of section 76(3) of the Act, a director is required to meet objective standards and act with the degree of care, skill and diligence that can reasonably be expected of a person carrying out the same functions in relation to the company, as those carried out by that director.[140] In terms of s76 of the Act, it is a clear that it is inappropriate to take on an appointment as a director, if one does not have sufficient education and knowledge to discharge one's obligations with a reasonable degree of skill and care.[141]

In terms of the decision-making function, the board is required to determine matters of policy and make significant decisions to plan the company's future, by taking reasonably diligent steps to become more informed about a matter.[142] The oversight function deals with the directors responsibility to actively monitor corporate affairs.[143] Liability arises where it is proven that a director had failed to take action under circumstances where the director should have acted in order to prevent loss or harm to the company.[144] Van Tonder emphasises the importance of the oversight function, although it is not a well-developed function in South Africa, having received very little to no attention.[145] As a result of the undeveloped nature of the oversight function, courts may rely on section 5(2) of the Act, which provides that a court may consider foreign company law, when interpreting or applying provisions of the Companies Act.[146]

The business judgement rule (hereafter BJR) only applies to a business judgement or decision that has been made by a director or board of directors. It does not apply in the case where directors have failed to adequately carry out their monitoring and oversight function.[147] Van

[138] Van Tonder JL (2018) 308.
[139] *Fisheries Development Corporation of SA Ltd v. Jorgensen & Another* [1980] (4) SA 156 (W) at 165 F.
[140] s 76(3) of Act 71 of 2008.
[141] Levenberg P (2017) 24.
[142] Van Tonder JL (2018) 305.
[143] Van Tonder JL (2018) 303.
[144] Van Tonder JL (2018) 303.
[145] Van Tonder JL (2018) 303. The following article supports Van Tonder's findings: Olivier EA 'Regulating against False Corporate Accounting: Does the Companies Act 71 of 2008 Have Sufficient Teeth? *South African Mercantile Law Journal* 1 (2021) 33.
[146] s 5(2) of Act 71 of 2008.
[147] Van Tonder JL (2016) 563.

Tonder argues that the rule provides directors with a shield from liability, provided the decision-making process is not tainted by a personal financial interest.[148]

Van Tonder argues that the statutory managerial authority imposed on directors in terms of the Act, means that directors now have a positive duty to manage the company.[149] This statutory authority enables the board to make business decisions, and direct the management of the company.[150] The BJR provides protection to directors in exercising their discretion to make business decisions for the benefit of the company. It is an important component of a director's duty, and it provides directors with the freedom and discretion to make decisions and influence the growth of the company. The definition of gross negligence, which includes 'a deliberate disregard to the whole body of shareholders,' in the context of South African SOCs, appears out of touch with the realities of many SOCs, where grossly negligent decisions are often made, *for the benefit of* the majority shareholder, being the government. The issue of political meddling once again comes to the fore in this regard.

In addition to the duties and responsibilities imposed on the board of directors at a company, in terms of common law and the Companies Act, directors of SOCs are additionally subject to duties imposed on them in terms of the PFMA.[151]

4.2.3 The Public Finance Management Act

The Public Finance Management Act (PFMA) seeks to establish accountability of the board.[152] In terms of the Act, directors are required to exercise the duty of utmost care to ensure the reasonable protection of the SOC's assets and records.[153] The Act is responsible for imposing stringent reporting and financial accountability provisions on the SOC.[154] While the PFMA is primarily aimed at regulating the financial reporting structures of national public entities, national SOCs are by definition, under the 'ownership control' of the national executive, or Cabinet Minister.[155] Thus, SOCs fall within the ambit of the PFMA.[156]

[148] See s76(4)(a)(*ii*) of Act 71 of 2008. See also Van Tonder JL (2016) 563.
[149] Van Tonder JL (2016) 566.
[150] Van Tonder JL (2016) 566.
[151] Public Finance Management Act 1 of 1999.
[152] *DPE – SOC Board Evaluation Framework* (2021) 15.
[153] *DPE – SOC Board Evaluation Framework* (2021) 15.
[154] *DPE – SOC Board Evaluation Framework* (2021) 15.
[155] De Visser J et al (2019) 11.
[156] *DPE – SOC Board Evaluation Framework* (2021) 22.

In the instance of a conflict between the provisions of the Companies Act and the PFMA, the provisions of the PFMA take precedent.[157] The PFMA explicitly provides that the board of an SOC must ensure the reasonable protection of the assets and records of the SOC, and that the board acts with fidelity in the best interests of the company, in managing the financial affairs of the SOC.[158] Individual directors, and the board as a whole, carry full fiduciary responsibility in terms of the PFMA.[159]

Section 50 of the PFMA provides the fiduciary duties of the board of directors, which largely corresponds with the common law fiduciary duties of directors. These duties include:

1. The duty to exercise the utmost care and reasonable protection of assets and records;[160]
2. The duty to act with fidelity, honesty, integrity and in the best interest of the SOC in managing the financial affairs of the company;[161]
3. The duty to disclose all material facts to the shareholder, which may influence the decisions or actions of the executive authority or legislature;[162]
4. The duty not to act in a way that is inconsistent with the responsibilities assigned to the board in terms of the PFMA;[163]
5. The duty not to use the position, or privileges of, or confidential information obtained as board members, for personal gain or to improperly benefit another person;[164]
6. The duty to disclose to the board any direct or indirect personal or private business interest that they, or any spouse, partner or close family member may have in any matter before the board;[165] and
7. The duty not to participate in the proceedings of the board when that matter is considered unless the board decides that the member's direct or indirect interest in the matter is trivial or irrelevant.[166]

Section 63 of the PFMA provides that the executive authority must exercise the ownership control powers to ensure that the SOC complies with the PFMA and the financial policies of

[157] *DPE – SOC Board Evaluation Framework* (2021) 15.
[158] *DPE – SOC Board Evaluation Framework* (2021) 22.
[159] *DPE – SOC Board Evaluation Framework* (2021) 22.
[160] s 50(1)(a) Act 1 of 1999.
[161] s 50(1)(b) Act 1 of 1999.
[162] s 50(1)© Act 1 of 1999.
[163] S 50(2)(a) Act 1 of 1999.
[164] s 50(2)(b) Act 1 of 1999.
[165] s 50(3)(a) Act 1 of 1999.
[166] s 50(3)(b) of Act 1 of 1999.

that executive.[167] This 'ownership control' is evidenced in the powers of the executive authority to appoint or remove board members and executives, or to control majority voting in board or general meetings of SOCs under its control.[168]

In terms of section 49 of the PFMA, an SOC is required to have an accounting authority that is accountable for purposes of the PFMA.[169] This section further provides that if the public entity, in this case the SOC, has a board of directors, that board will be the accounting authority; and in the absence of a board or controlling body, the CEO will be the accounting authority.[170] However, in terms of the appointments or dismissals of board members or executives, the PFMA does not contain any provisions in this regard, nor does it discuss the qualifications of board members or executives.[171]

The general duties of the board, as they relate to the management of the business of the entity, are addressed in s51 of the PFMA.[172] Section 51 provides more details in terms of duties, although it is an equivalent requirement to section 66 of the Companies Act.[173] The section 51 duties in terms of the PFMA include duties such as ensuring effective risk management systems, submissions of returns and reports, and compliance with tax and other laws.[174] Sections 52 and 55 of the PFMA deal with the submission of annual budgets, financial statements, reports, corporate plans and audited financial statements.[175] The wilful or negligent failure to comply with the requirements of sections 50 to 55, is referred to as an act of 'financial misconduct,' in terms of section 83.[176] This extends to board members permitting irregular expenditure or fruitless and wasteful expenditure.[177] Directors may face individual liability for any financial misconduct by the accounting authority.[178] In terms of the PFMA, financial misconduct is grounds for dismissal, suspension or another sanction against a member of the

[167] De Visser J et al (2019) 11.
[168] De Visser J et al (2019) 11.
[169] s 49 of Act 1 of 1999.
[170] s 49(2)(a) – (b) of Act 1 of 1999.
[171] De Visser J et al (2019) 12.
[172] s 51 of Act 1 of 1999
[173] s 66 of the Companies Act 71 of 2008 addresses the 'Board, directors, and prescribed officers' whereas s51 of the PFMA (Act 1 of 1999) addresses the 'General responsibilities of Accounting Authorities.'
[174] s 51 Act 1 of 1999.
[175] s 52 to s55 of Act 1 of 1999.
[176] s 83 of Act 1 of 1999 addresses 'Financial misconduct by accounting authorities and officials of public entities.' s83(1) of Act 1 of 1999 entails: 'The accounting authority for a public entity commits an act of financial misconduct if that accounting authority wilfully or negligently –
(a) fails to comply with a requirement of section 50, 51, 52, 53, 54 or 55.'
[177] De Visser J et al (2019) 12.
[178] s 83(2) of Act 1 of 1999 reads 'If the accounting authority is a board or other body consisting of members, every member is individually and severally liable for any financial misconduct of the accounting authority.'

board.[179] The board may face criminal sanctions, if it is found that a board wilfully or in a grossly negligent way, failed to comply with the provisions of section 50 to 55 of the PFMA.[180] De Visser et al contend that the PFMA does not provide guidance on the interpretation of the test for wilful actions by the board, and is not clear on whether individual board members could be held criminally liable for breaches of their duties.[181] For example, it is unclear how a 'board' could be sentenced to imprisonment; does it imply that all members of the board would face imprisonment?[182]

De Visser et al argue that although the fiduciary duties of directors in terms of section 50 of the PFMA largely correspond to the common law duties of company directors, they do not, in all circumstances, correspond to the partially codified duties of directors as set out in section 76 of the new Companies Act.[183] For example, the PFMA does not contain a provision similar to the business judgement rule found in section 76(4) of the Companies Act.[184] This discrepancy between the Act and the PFMA is worth emphasising, in light of the supremacy of the PFMA in the case of SOCs.[185] De Visser et al argue that, in an instance where the provisions of the Act and the PFMA cannot be applied concurrently, the PFMA will apply and directors will not be afforded the protection of the business judgement rule.[186] However, in an instance of possible concurrent application, board members of SOCs who are in breach of their duties of care, skill and diligence, may escape personal liability for damages caused due to this breach, provided the requirements of section 76(4) of the Companies Act are met.[187] However, the directors may still be held liable for financial misconduct in terms of the PFMA, for breach of their duties in terms of section 50 of the PFMA, and the fiduciary duty of good faith.[188] SOCs that are not registered companies, such as PRASA (Passenger Rail Agency of South Africa), will however not have the option of protection for their board members, through the business judgement rule, and will only face the consequences of section 83 of the PFMA for breach of their duties.[189]

[179] s 83(4) reads 'Financial misconduct is a ground for dismissal or suspension of, or the sanction against, a member or person referred to in subsection (2) or (3) despite any other legislation.'
[180] s 86(1) of Act 1 of 1999 reads 'An accounting authority is guilty of an offence and liable on conviction to a fine, or to imprisonment for a period not exceeding five years, if that accounting officer wilfully or in a grossly negligent way fails to comply with a provision of section 38, 39 or 40.'
[181] De Visser J et al (2019) 13.
[182] De Visser J et al (2019) 13.
[183] De Visser J et al (2019) 13
[184] De Visser J et al (2019) 13.
[185] De Visser J et al (2019) 13.
[186] De Visser J et al (2019) 13.
[187] De Visser J et al (2019) 13.
[188] De Visser J et al (2019) 13.
[189] De Visser J et al (2019) 13.

In addition to the duties imposed on directors in terms of the Companies Act and the PFMA, the guidelines from the King IV Codes are crucial in aiding sound corporate governance systems, particularly at SOCs.

4.2.4 King IV Recommendations

In *SABC v Mpofu,*[190] the High Court considered the principles expounded in the King codes to be binding on state owned entities.[191] In *Minister of Water Affairs and Forestry v Stilfontein Gold Mining Company*,[192] the court held that the principles of the King codes are a yardstick against which the conduct of directors should be measured, as it relates to their fiduciary duties.[193] Van Tonder refers to the King IV's principles of corporate governance as 'aspirational.'[194] These 'aspirational' principles provide extensive guidelines on performance, leadership and governance, although most companies will most likely not be able to uphold every single one of the recommendations to the best standards. Van Tonder further contends that the principles of the King IV are highly desirable, but ultimately does not provide for the standards of directors' conduct nor does it provide for instances in which direct liability will be imposed for a breach of legal duty.[195] It provides an excellent guideline for directors' conduct, and the duties of the board, and should be read in conjunction with the legal duties and liabilities to which directors are accountable. The King IV provides relevant recommendations and contains a sector supplement specifically for SOCs.[196] Although compliance with the King Code is voluntary, it is a mandatory requirement for all JSE listed companies.[197]

King IV promotes ethical and effective leadership in principle one.[198] The first principle entails that the accounting authority (or board of directors) both individually and collectively, cultivate characteristics such as integrity, competence, responsibility, accountability, fairness and transparency in their conduct.[199] Although ethical business practices, particularly in relation to

[190] *South African Broadcasting Corporation Ltd and Another v Mpofu* [2009] 4 SA 169 (GSJ) par 66.
[191] *SABC v Mpofu* [2009] 4 SA 169 (GSJ) par 66.
[192] *Minister of Water Affairs and Forestry v Stilfontein Gold Mining Company Limited and Others* 2006 (5) SA 333 (W) par 16.7 – 16.9.
[193] *Minister of Water Affairs and Forestry v Stilfontein Gold Mining Company Ltd.* 2006 (5) SA 333 (W) par 16.7 – 16.9.
[194] Van Tonder JL (2018) 307.
[195] Van Tonder JL (2018) *A Primer on the Directors' Oversight Function* 307
[196] At part 6 of The King IV Report on Corporate Governance for South Africa 2016, The Institute of Directors in Southern Africa (hereafter *King IV Report*). See also Cliffe Dekker Hofmeyr *King IV: An Overview* (2017).
[197] Janse van Vuuren H 'The Disclosure of Corporate Governance: A Tick-Box Exercise or Not?' (2020) 12 *International Journal of Business and Management Studies* 52.
[198] IodSA *The King IV Report* (2016) 43.
[199] IodSA *The King IV Report* (2016) 43.

directors' standard of conduct, is not legislated, it is a recommended practice in terms of the King IV. In line with principle 1, principle 2 in the sector supplement for SOCs recommends that the accounting authority govern the ethics of the entity in a way that supports the establishment of an ethical culture.[200] As earlier stressed, an ethical approach to business practices is foundational to good corporate governance.[201]

In terms of principle 3, the accounting authority must ensure that the SOC is seen to be a responsible corporate citizen.[202] I have previously stressed the importance of SOCs in particular being led as responsible corporate citizens, considering the large impact these companies have on the economy and South African society at large. Most SOCs in South Africa see to the basic human needs of ordinary citizens. In this regard, it is imperative that SOCs are run as responsible corporate citizens.

Principle 4 recommends that the board, should appreciate that the SOC's core purpose, its risks and opportunities, strategy, business model, performance and sustainable development are all inseparable elements of the value creation process.[203] While SOCs hold the responsibility of providing basic needs, and function as a part of the state, these companies must remain profitable, and continually strive to grow profits and enhance performance.

Principle 5 provides that the board must ensure that reports issued by the SOC enable stakeholders to make informed assessments of the SOC's performance and its short, medium, and long-term prospects.[204]

In terms of principle 6, the board should serve as the focal point and custodian of corporate governance in the SOC.[205] This principle reiterates earlier sentiments alluded to in terms of the board of directors being the custodian of good corporate governance. As the governing body of an SOC, the board bears fiduciary duties in terms of the PFMA as well as the Companies Act.[206] The governing body being the custodian of corporate governance is a natural consequence, in light of the fiduciary duties imposed on them, in addition to being entrusted

[200] IodSA *The King IV Report* (2016) 112.
[201] Mofokeng T (2020) 66. This is the most well-known definition of corporate governance, deriving from the Cadbury Committee, which was set up in the United Kingdom in 1991: Cadbury, A. *Report of the Committee on the Financial Aspects of Corporate Governance* (1992).
[202] IodSA *The King IV Report* (2016) 112.
[203] IodSA *The King IV Report* (2016) 112.
[204] IodSA *The King IV Report* (2016) 112.
[205] IodSA *The King IV Report* (2016) 114.
[206] IodSA *The King IV Report* (2016) 114.

with assets and interests other than their own.[207] Principle 6 serves as a useful guideline for the accounting authority in gaining an overarching understanding of its role.[208] It is thus recommended that the guidelines provided in principle 6 in regards to the primary leadership role of any governing body, be used as a reference point by the board when discharging its responsibilities in any area of governance.[209]

In terms of principle 7, the board must exercise the appropriate balance of knowledge, skills, experience, diversity and independence, in order to objectively and effectively discharge its governance role and responsibilities.[210] According to the King IV, the composition of the accounting authority is a key factor influencing the performance of an SOC.[211] Practices regarding the appointment of members of the governing body and the role of the nominations committee in this process are relevant in terms of principle 7. It is recommended that the accounting authority actively seeks to collaborate with the shareholder, when they do not have the power to nominate or elect members.[212] In terms of this principle, the SOC and the executive authority should practice transparency in regards to the processes followed for the nomination, election and appointment of governing body members.[213] This principle further recommends the 'staggered rotation' of members of the accounting authority, to introduce members with new expertise, while retaining valuable knowledge, skills and experience.[214]

Principle 9 proposes the evaluation of the performance of the governing body, its members and committees at SOCs, in order to achieve continued improvement in performance and effectiveness.[215] It is thus evident that the King Report places value on the role of oversight and evaluating board effectiveness, in order to achieve better performance.

Principle 10 addresses the appointment of and delegation to management and seeks to ensure that these appointments contribute to role clarity and the effective exercise of authority and responsibilities.[216] In an SOC, the executive authority, rather than the accounting authority, has the power to appoint the CEO.[217] The appointment of the CEO should be a robust and

[207] IodSA *The King IV Report* (2016) 114.
[208] IodSA *The King IV Report* (2016) 114.
[209] IodSA *The King IV Report* (2016) 114.
[210] IodSA *The King IV Report* (2016) 115.
[211] IodSA *The King IV Report* (2016) 115.
[212] IodSA *The King IV Report* (2016) 114.
[213] IodSA *The King IV Report* (2016) 114.
[214] IodSA *The King IV Report* (2016) 115.
[215] IodSA *The King IV Report* (2016) 115.
[216] IodSA *The King IV Report* (2016) 116.
[217] IodSA *The King IV Report* (2016) 116.

transparent process, as a matter of good practice. The shareholder reserves the right to make the final appointment, however, it is recommended that the accounting authority is involved in the process to the greatest extent possible.[218] Further recommendations in terms of principle 10 include that the CEOs letter of appointment clearly states that he/she is accountable to the accounting authority, that the CEO's performance is assessed accordingly, and that the accounting authority has primary responsibility for the removal of the CEO.[219] Principle 10 further recommends the appointment of a company secretary, or suitably experienced professional, to provide professional and independent guidance on corporate governance and its legal duties.[220] Principle 13 also addresses compliance, and recommends that the accounting authority should govern compliance in a way that supports the SOC being an ethical and good corporate citizen.[221]

Lastly, in terms of principle 16, it is recommended that the accounting authority adopt a stakeholder inclusive approach that balances the needs, interests and expectations of material stakeholders in the best interests of the SOC over time. This principle recommends that the accounting authority proactively engage with government, in all stakeholder capacities, to foster an understanding of how various expectations and accountabilities are to be reconciled.[222] Furthermore, in terms of principle 16, it is recommended that the accounting authority of the SOC ensures that the shareholder compact accurately defines the role of the accounting authority and he executive authority respectively.[223] The shareholder compact must also contain an alternative dispute resolution procedure, should a dispute about the interpretation of the compact or agreement arise.[224]

Furthermore, principle 16 addresses the triplicate role of government as a stakeholder in SOCs, namely the role of shareholder, policy maker and regulator.[225] King IV highlights that these roles may overlap and may even conflict with each other.[226] According to De Visser et al, the sector supplement for SOCs in the King IV was welcomed in the hopes of addressing some of the concerns plaguing the governance of SOCs. Principle 16 served this purpose, by identifying

[218] IodSA *The King IV Report* (2016) 116.
[219] IodSA *The King IV Report* (2016) 116.
[220] IodSA *The King IV Report* (2016) 116.
[221] IodSA *The King IV Report* (2016) 116.
[222] IodSA *The King IV Report* (2016) 116.
[223] The 'shareholder compact' defines the role of the accounting authority and the executive authority, respectively. IodSA *The King IV Report* (2016) 116.
[224] IodSA *The King IV Report* (2016) 116.
[225] IodSA *The King IV Report* (2016) 116.
[226] IodSA *The King IV Report* (2016) 116.

the problematic triplicate role of government, and made reasonable suggestions to address it, through the shareholder compact agreement.[227] However, it has been argued that, in practice, the shareholder compacts do not fulfil their desired roles, as it is often signed late and is not 'forward thinking enough.'[228]

In terms of principle 7 and 10, De Visser et al argue that the ideal position regarding the nomination and appointment of board members and the CEO, is difficult to attain.[229] They argue that in practice, board members are appointed by the relevant shareholder minister, 'in consultation with cabinet.'[230] De Visser et al however argue that it is not clear what process such consultation entails. This process is infamously problematic, given some controversial board appointments made to prominent SOCs in the last few years.[231] King IV recommends a 'robust and transparent' process for the appointment of the CEO, however this is often far from reality.[232] Over the last decade, board and executive appointments were often found to be for personal gain, as was evident in the state of capture report.[233] Little evidence of a 'robust and transparent process,' as advocated by the King IV, is seen in most SOCs. It must thus be determined whether the aspirational principles of the King IV aid in the effective governance of SOCs in South Africa. Although embracing King IV would lead to compliance with the common law and legislative standards, as it is recommended that the King IV be read in conjunction with legislation.

4.3 CONCLUSION

The purpose of this study is to determine whether the legal framework governing the fiduciary duties of directors is sufficient in aiding good governance at state-owned companies. This chapter seeks to break down the various duties imposed on directors by the regulatory framework. This chapter provided a discussion and analysis on the effectiveness of this framework and found that certain elements of the duties imposed on directors, be it from common law, the Companies Act, the PFMA or King IV recommendations, are in need of development, or better implementation.

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[227] De Visser J et al (2019) 31.
[228] De Visser J et al (2019) 31.
[229] De Visser J et al (2019) 31.
[230] De Visser J et al (2019) 31.
[231] De Visser J et al (2019) 32.
[232] De Visser J et al (2019) 32.
[233] Justice RMM Zondo *Judicial Commission of Inquiry into allegations of State Capture, Corruption and Fraud in the Public Sector including Organs of State* Report: Part 1 Vol. 1: Chapter 1 (2016).

While a substantive framework regarding financial and risk management is provided for in the PFMA, failures by the board to uphold those responsibilities imposed on them has often resulted in government having to assist them in order for them to remain sustainable. Ranging from high salary payouts to corruption and state capture allegations, SOCs who have failed to uphold the responsibilities imposed on them in terms of the PFMA, have had to rely on government to assist SOCs in order for them to remain sustainable. According to the PFMA, SOCs are required to take appropriate steps to collect all revenue due to the company, prevent irregular and wasteful expenditure, prevent losses from criminal conduct, and prevent expenditure for not complying with the operational policies of SOCs. It is thus the board's responsibility, in terms of the PFMA, to ensure the compliance of an SOC with the provisions of the PFMA and other applicable legislation. However, as previously evidenced, irregular, fruitless and wasteful expenditure of funds is a prevalent challenge faced by SOCs.

Challenges that have been identified by the Presidential Review Committee (PRC) in 2013, include the challenge of governance and oversight, board and executive recruitments and questionable financial management by these companies, amongst others. These challenges remain prevalent in SOCs today, a decade after that report has been released. The South African Airways (SAA) serves as an example of an SOC that has been plagued with financial management challenges for over a decade.[234] This illustrates failure by government, the respective shareholding ministers, as well as the boards of these companies, to implement systems and practices that see to the provisions of the PFMA and Companies Act being upheld. Slow action in this regard, on the part of the government, shareholders, and boards, when considering the large impact of SOCs on ordinary South African citizens, in terms of basic needs being met, is perturbing. The global study by McKinsey & Co in 2018,[235] found that governing boards with better dynamics and processes, that manage execution more effectively, report stronger financial performance.[236] This finding alone proves the sentiments, emphasised in King IV, that the board of directors are the custodian of corporate governance.[237] An effective board, with a well-established framework governing board relations and processes, will result

[234] DPE *Strategic plan* (2020) 38.
[235] McKinsey & Co. – A Time for Boards to Act (2018)
[236] *DPE – SOC Board Evaluation Framework* (2021) 30. See also the survey by: McKinsey & Co. – A Time for Boards to Act (2018)
[237] IodSA *The King IV Report* (2016). Principle Six of the Code, on the sector supplement for SOEs, reads: '*The accounting authority should serve as the focal point and custodian of corporate governance in the SOE*.'

in profitable companies, with a more cohesive corporate structure, displaying better corporate governance.

It is clear that the three fiduciary duties of directors in terms of common law form the foundation of a directors responsibility: the duty to act in good faith and loyalty to his company, the duty to exercise his or her powers as a director bona fide in the best interests of the company, and to avoid a conflict of interest between that of the company and his or her own interests, and lastly, the duty to display ' reasonable care and skill' .[238]

The 'new' Companies Act (2008) has been praised for its flexibility, in being able to appropriately regulate small to large companies.[239] The Act serves as a partial codification of common law duties and sought to ensure that the standards of directors' conduct are made clear, more enforceable, and to improve corporate governance.[240] Section 75 of the Act addresses the disclosure of directors' personal financial interests. In terms of s75, the court may declare a transaction as valid and approved by the board or shareholders, despite the failure of the director to satisfy the requirements of section 75.[241] In other words, directors may escape liability for not disclosing personal financial interests, in terms of s75. Directors may also escape liability for breaching their duty to act in the best interests of the company, in terms of the business judgement rule (BJR), provided that in can be proved that director have acted in the best interests of the company.[242] The BJR ensures that the decisions of the board will not be questioned. This rule will thus allow for the freedom and discretion of directors in their work, allowing for more effective performance, as Havenga earlier proposed,[243] provided that the BJR follows strict application. Although decisions of the board have the risk of causing adverse financial conditions in the company, Naidoo has argued that the success of a business cannot be guaranteed, as businesses are risk-dependent.[244] Risky decisions are a requirement for business growth, argues Naidoo.[245] While it is risky that directors may escape liability for certain business decisions, perhaps leaving room for 'risky' business decisions at the hands of directors, for the sake of business growth, is a more progressive approach to business. At a

[238] Mupangavanhu B (2017) 151.
[239] Jennings BPL (2015) 55.
[240] Mupangavanhu B (2017) 152.
[241] s 75(8) of Act 71 of 2008.
[242] s 76(3) and (4) of Act 71 of 2008.
[243] Havenga M (1997) 134.
[244] Naidoo R *Corporate governance: An Essential Guide for South African Companies* (2016) South Africa: LexisNexis.
[245] Naidoo R *Corporate governance: An Essential Guide for South African Companies* (2016) South Africa: LexisNexis.

state-owned company, the stakes may be higher, however the rewards of a 'risky' business decision may be greater and could lead to growth and progression at these companies.

In addition to the legislative framework imposed on SOCs, the boards are accountable to the provisions of the King IV. Although the King IV recommendations have been referred to as 'aspirational' and 'highly desirable,' it serves as a yardstick against which the standards of conduct of directors should be measured.[246] Particularly relevant to the South African governance sphere in terms of SOCs, the King IV highlighted the problematic triplicate role of government in SOCs, and provided reasonable suggestions to address it, through the shareholder compact agreement for example. However, the shareholder compact agreement has not been able to fulfil its desired roles, as it is either signed later, or is criticised for not being 'forward thinking enough.'

From the regulatory framework providing for director duties, responsibilities, and director liability, it appears that the framework is relatively extensive, although certain areas require more attention and development. In particular, the oversight function of directors requires development and attention, the issue of the appointment and dismissal of directors, as well as the pressing issue of the financial management of SOCs. One pertinent issue that I have identified, appears to be one of implementation of the required processes required in terms of legislation, a lack of ethical leadership, and slow movement in terms of identifying the core challenges facing SOCs and developing frameworks to address same. It appears that when challenges appear at SOCs, the 'quick fix' is a cash injection from government, every year, resulting in decades of struggling state-owned entities, experiencing the same core challenges from decades ago.

[246] *Minister of Water Affairs and Forestry v Stilfontein Gold Mining Company* 2006 (5) SA 333 (W).

CHAPTER 5

CONCLUSIONS, FINDINGS AND RECOMMENDATIONS

5.1 SUMMARY OF RELEVANT FEATURES IN KEY CHAPTERS

5.1.1 Chapter One

This thesis sought to identify the extent to which the South African legislative framework governing director duties, particularly at State-Owned Companies (SOCs), facilitates corporate governance. The significance of this paper is to contribute to the available resources on the topic of corporate governance in South Africa, as it pertains to SOCs and director duties.

Chapter one defined the purpose of SOCs and discovered that these companies are the principal drivers of the formal sector of the South African economy, as they are the biggest employers in the economy. SOCs play a vital role in providing certain essential social services to the country, including infrastructure, utilities, transport, energy, telecommunications, and finance.[1] However, the sector has been plagued with allegations of fraud, mismanagement, state capture and severe financial difficulties. The sharp decline in the performance and governance of SOCs, is what informs the basis of this enquiry. [2] The understanding of the purpose of SOCs, and the impact of their contribution to the economy, formed the foundations for further discussions in this paper.

The legal framework governing SOCs in South Africa has been labelled as complex, fragmented, and contradictory.[3] Chapter one formed the foundations for further discussion in this regard as well. Although extensive research on the topic of corporate governance, and director duties in South Africa has been published, this paper sought to add to the available resources, and provide a reflection particularly on the extent to which the legal framework for director duties facilitates good corporate governance at SOCs. In light of current events in South Africa, and the discourse on the state of SOCs, this thesis sought to address the topic, and provide a legal perspective on the sector.

[1] Thabane T *The Ownership and Control Architecture of South Africa's State-Owned Companies and its impact on Corporate Governance* (published LLM thesis, the University of Cape of Town, 2020) 1.
[2] 'State of Capture' A Report of the Public Protector Report No: 6 of 2016/17 (2016) available at *http://www.saflii.org/images/329756472-State-of-Capture.pdf* (accessed October 2022).
[3] Thabane T (2020) 87.

5.1.2 Chapter Two

Chapter two of this paper emphasised that the board of directors is the custodian of corporate governance in a company. [4] This chapter sought to first develop a thorough understanding of the concept of corporate governance, before addressing the question of the extent to which the legal framework governing directors, facilitates good corporate governance at SOCs. This chapter found that the governing body of a company is the 'heartbeat of corporate governance.'

This chapter thus provided discussions on the rise of corporate governance in South Africa and of the instruments facilitating corporate governance. This chapter drew on certain corporate governance failures in South Africa, and also discussed the challenges faced by SOCs currently, particularly at Denel, Eskom, and the SAA.

Chapter two found that good corporate governance provides the foundations for well-managed, effective, and productive companies. The themes of ethical behaviour and social responsibility were recurring in this chapter. I concluded that the notion of running companies like good corporate citizens, best encapsulates the concept of good corporate governance. In the context of the large contribution by SOCs to the economy, it is imperative that these companies uphold high standards of ethics and behave as good corporate citizens. In the context of the South African socio-political history, corporate governance mechanisms such as the King codes and the Protocol sought to address racial exclusionary practices. Considering the purpose of using SOCs to effect economic transformation in South Africa, it is important that companies, and policy makers alike, grasp the understanding that companies are grater agents for change than the government. [5]

It is clear that corporate governance principles have been developed over time, in response to issues and challenges in the market at that time. In this chapter, I have argued that these principles should be flexible, and continuously amended to reflect current issues. In my opinion, recurring issues in the sector of SOCs as it pertains to corporate governance, includes the issue of extensive political meddling, 'blurred' lines of oversight, and a lax approach to director duties. These issues have manifested into poor service delivery, and overall poor governance.

[4] Mofokeng T 'Good Corporate Governance Affirms the Board (Led by the Chairperson) as the Focal Point of Governance and the Courts Have no Mandate to Undermine this Principle' (2020) *Journal of Corporate and Commercial Law & Practice* Vol 6(1) 75.
[5] King ME 'The Synergies and Interaction Between King III and the Companies Act 71 of 2008' (2010) *Acta Juridica* 446.

In the face of continuous and fast-paced changes in technology, commerce and labour markets, corporate governance codes must be constantly evolving and be flexible enough to regulate new challenges in the market. In this regard, I recommended a pro-active approach to contemporary corporate misconduct.

The legal framework governing the sector is extensive and thorough, although the implementation of recommended practices is poor. The issue thus, appears to be the lack of cohesion between the practices implemented at SOCs, and the system of governance available. With the consistent political meddling at the hands of the shareholding ministers, it is arguable whether certain crucial provisions in terms of the Companies Act,[6] PFMA,[7] or King IV,[8] are observed at SOCs.

In the private sector, the Steinhoff-saga brought to light the issue of tick-box compliance systems. Therefore, certain crucial corporate governance practices must not only be upheld and implemented but must also be underpinned by ethical corporate behaviour. Chapter two thus highlighted the discourse on whether ethical practices can be codified.

This chapter additionally discussed the role of the Memorandum of Incorporation (MoI), as an instrument that facilitates corporate governance. However, the incident of the cabinet minister seeking to amend the MoI to afford herself the power to appoint or dismiss board members, accentuates the issue of political meddling. In this regard, one important conclusion one can deduce, is that the legislature does not adequately protect SOCs from political meddling.

5.1.3 Chapter Three

Chapter three dealt with the functions and effectiveness of the board of an SOC's board of directors. Expanding on earlier discussions on board effectiveness, chapter three starts off by explaining that a company is a separate legal entity from its management and shareholder, and therefore, the company must act through its individuals, particularly through its directors.[9] This chapter further expands on Havenga's argument that there should be a balance between directors' freedom to manage, directors' accountability, and the interests of various stakeholders.[10] This argument is a reflection of the *Fisheries Development Corporation of SA*

[6] Companies Act 71 of 2008.
[7] Public Finance Management Act 1 of 1999.
[8] The King IV Report on Corporate Governance for South Africa 2016, The Institute of Directors in Southern Africa.
[9] Havenga M 'The Company, the Constitution, and the Stakeholders' (1997) 5 *Juta's Business Law* 134.
[10] Havenga M (1997) 134.

Ltd v Jorgensen[11] decision, where it was held that a director must act in the best interests of the company, 'to the exclusion of' any other interests of the shareholders, employer or principal.[12] The argument is that directors must remain cognisant of their powers and duties, as well as the limitations to their powers, while also being afforded the freedom to exercise their own discretion in terms of decision making. In light of this argument, a framework which restricts the powers of the board of directors would be detrimental to the company, in terms of exercising their discretion to make business decisions that could foster corporate growth. Affording the board of directors this freedom of discretion, provided the board is consisted of suitably qualified and skilled professionals, and the decisions are based in the best interests of the company, would possibly result in the much-needed turnaround and growth in these companies.

This chapter thoroughly discussed the two main functions of the board of directors, being the decision-making function and the oversight function. In terms of the oversight function, this chapter highlighted the underdeveloped nature thereof in South African law. It has highlighted how the effective control and management of an SOC is important, given the effects on society and the economy, when SOCs do not perform to a certain standard. Essentially, this chapter identified the causal connection between the regulatory framework governing directors' standard of conduct, and the effects on the performance of SOCs. Both the Presidential Review Committee (PRC) and the Minister of Public Enterprises, have expressed concern over the inadequate governance and oversight systems at SOCs, causing poor performance, corruption, and poor board accountability.

The adoption of the DPE's proposed Board Effectiveness Framework (BE Framework) will probably create an administrative burden for SOCs, considering the number of duties already imposed on boards in terms of the Companies Act, PFMA and other regulations. Nonetheless, a form of a board effectiveness programme, that measures the performance and efficiency of the board, would undisputedly benefit SOC boards in executing their oversight function.

Essentially, this chapter found that although the regulatory framework provides established guidelines for the board of directors, it falls short in providing a guideline for the board in conducting their oversight function, one critical function for the board. Although the

[11] *Fisheries Development Corporation of SA Ltd v Jorgensen* [1980] 4 All SA 525.
[12] *Fisheries Development Corporation of SA Ltd v Jorgensen* [1980] 4 All SA 525.

Companies Act does an excellent job at codifying directors' duties and matches international standards of corporate governance, it is clear that the framework needs to be developed in response to the current challenges at SOCs. The current state of SOCs in South Africa displays poor corporate governance practices. It can thus be deduced that the legal framework governing directors at SOCs, as the custodian of corporate governance at a company, does not facilitate corporate governance best practices to the extent at which it is well reflected in SOCs in South Africa.

5.1.4 Chapter Four

Chapter four provided an in-depth synopsis of the legal duties applicable to directors at State-Owned Companies (SOCs). This chapter reflected on the duties and responsibilities of directors found in the Constitution,[13] the PFMA[14] and National Treasury regulations, the Companies Act[15] and its regulations, the respective founding legislation for an SOC, common law, as well as the MoI of the company.[16] This chapter discussed recommendations in terms of the King IV as it pertains to the board of directors, particularly at SOCs. It further identified certain challenges in the current framework and certain areas that require development. This chapter sought to break down the various duties imposed on directors, by discussing specific duties in terms of the Companies Act, PFMA, common law and King IV.

This chapter found that while a sufficient framework regarding financial and risk management is provided for in the PFMA, SOC boards have failed to uphold the responsibilities imposed on them, which resulted in government having to assist them in order for these companies to remain sustainable. The legislative framework governing director duties and liabilities is relatively extensive, although certain areas require more attention and development. These areas include the directors' oversight function, the appointments, and dismissals of directors, as well as the issue of the financial management of SOCs.

One pressing issue identified in chapter four, is the issue of implementation of the required processes required in terms of legislation. Further issues include the lack of ethical leadership, slow identification of core challenges facing SOCs, and slow development of frameworks to address these issues.

[13] Constitution of the Republic of South Africa, 1996.
[14] Public Finance Management Act 1 of 1999.
[15] Companies Act 71 of 2008.
[16] State-Owned Company Board Evaluation Framework Version 2, 2021 Department of Public Enterprises (2021) 21 (hereafter *DPE – SOC Board Evaluation Framework*).

As a result, chapter four identified the need for a framework for the implementation and safeguarding of the division of power between SOCs and their shareholding ministers. Furthermore, this chapter suggests that these companies could benefit from ethical leadership, should a framework be adopted that sees to fair ethical board appointments and dismissals.

5.2 EFFECTIVENESS OF FRAMEWORK

It is trite that South African corporate law matches certain international requirements, particularly in providing for the duties and liabilities of directors. In addition to the statutory requirements governing director duties, boards are encouraged to consider and implement the guidelines provided for in King IV. However, it remains questionable whether this framework is effective in aiding corporate governance best practices at SOCs. In addition to the operational, financial, and socio-economic challenges these companies face, certain governance challenges compound the situation. From the discussions throughout this paper, it is clear that a reliable board of directors, with the freedom and discretion to exercise decision-making, and established guidelines for their oversight function, particularly at SOCs, can benefit society.

Referring to the Steinhoff saga, Olivier argues that not much more could have been done from a legislative perspective, to discourage the financial irregularities and practices that took place.[17] In this regard, Olivier wonders what the Act could do to discourage dishonesty.[18] He argues that regulations can only take a society so far in the quest for honest and accountable financial reporting, and that criminals will always find a way to evade or breach the law.[19] Olivier's sentiments are relevant not only as it pertains to financial reporting, but also in relation to the duties imposed on directors at SOCs. While this thesis seeks to determine the extent to which the regulatory framework governing director duties facilitates good corporate governance, in the underperforming SOC sector, Olivier's contention reflects the reality of any sector: the legal framework can only take a society so far.

Olivier argues that regulatory agencies must at least effectively and consistently enforce penalties for non-compliance.[20] He argues that regulations only have deterrent value if they are consistently enforced.[21] This supports earlier arguments made in this paper, that the issue with

[17] Olivier EA 'Regulating Against False Corporate Accounting: Does the Companies Act 71 of 2008 Have Sufficient Teeth?' (2021) 33 *SAMJL* (hereafter *Regulating Against False Corporate Accounting*).
[18] Olivier EA (2021) 22.
[19] Olivier EA (2021) 22.
[20] Olivier EA (2021) 22.
[21] Olivier EA (2021) 22.

the regulatory framework is not necessarily that it is not efficient in enforcing certain standards, but rather that the standards and requirements are not implemented correctly, or consistently, as Olivier suggests.

Olivier further suggests that it may be impossible to legislatively remove reckless greed from the boardroom though a threat of a harsh sanction.[22] This reality appears true, as reckless financial conduct still occurs at various SOCs, despite the threat of harsh sanctions. Although the Act provides clear guidelines in terms of what is expected from the company and the board of directors in terms of financial reporting, it has not been effective in preventing poor financial management and reporting from occurring.

According to Thabane and Snyman-Van Deventer, one of the challenges at SOCs is ascribed to the lack of appreciation by SOC boards of corporate governance rules, particularly the distinction between management and governance.[23] The disregard for corporate ethics and integrity compounds this issue, they contend.[24] According to these authors, corporate governance is bound to fail when board members are implicated in scandals relating to tenders and fake qualifications, [25] as often reported in South African SOCs over the last decade.[26] The board of directors at SOCs have a duty of being the driver of strategy for the company. [27] However, Thabane and Snyman-Van Deventer argue that where a board has failed to provide strategic direction to management over a period of 20 years, resulting in the company having to be frequently bailed out, and failing to deliver the public goods on which society relies, the board has neglected this duty. [28] 'The disregard for corporate ethics' captures the essence of corporate governance failures at SOCs because, where the legislature appears to cover all bases in terms of what is required and what the sanctions are, companies still appear to disregard corporate ethics. Furthermore, as evident in the challenges identified in the SOCs discussed in this thesis, it appears that SOC boards have become reliant on government bailouts. These companies have shown little effort in providing strategic direction to the company. SOCs

[22] Olivier EA (2021) 23.
[23] Thabane T & Snyman-Van Deventer E 'Pathological Corporate Governance Deficiencies in South Africa's State-Owned Companies: A Critical Reflection' (2018) *PER / PELJ* Vol 21 23.
[24] Thabane T & Snyman-Van Deventer E (2018) 23.
[25] Thabane T & Snyman-Van Deventer E (2018) 23.
[26] For example, at South African Airways (SAA) there have been scandals including tender irregularities, as well as executive managers' bogus and/or lack of qualifications.
[27] Thabane T & Snyman-Van Deventer E (2018) 23.
[28] Thabane T & Snyman-Van Deventer E (2018) 23.

demonstrate stagnancy and slow growth, resulting in reoccurring financial bailouts from government.

Thabane and Snyman-Van Deventer further argue that at the heart of the many challenges faced by SOCs, is the political interference by the dominant shareholder, the government.[29] Political interference in the running of SOCs, executive managers' appointments, suspensions and dismissals, disregards the established rule of the division of power between the board and the shareholder.[30] For example, the move by government as a dominant shareholder to amend an SOC's MoI to arrogate the power to appoint, suspend and dismiss executives. These authors believe this move was ill-conceived and weakens the board of directors. [31] In this regard, political meddling in the affairs of an SOC to this extent, not only disregards the rule of the division of power but achieves the opposite of what Havenga recommends: a board that has the freedom and discretion to make business decisions. The 'political meddling' by the majority shareholder in the affairs of the company disregards the stakeholder inclusive approach that modern corporate law is geared towards. The dire effects of the shareholder primacy approach, where directors' decisions are based on satisfying the short-term interests of shareholders, had already been seen in business failures leading up to the corporate legal enforcement reform in the late 2000s.[32] It appears that while the legislature upholds the stakeholder approach, it is not always enforced in business practices. While the legislature calls for the division of power between directors and shareholders, this position is not reflected in business practices at SOCs. The South African regulatory approach places great emphasis on stakeholder protection and board accountability,[33] but this position is not always enforced in practice, particularly at SOCs.

In terms of section 66(1), the Act confers authority on a company's board, subject to the company's MoI and other provisions of the Act, and the obligation to manage the business of the company.[34] It cannot be overemphasised that compliance with the law, inclusive of the duties of directors, is a critical component of 'good' corporate governance.[35]

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[29] Thabane T & Snyman-Van Deventer E (2018) 23.
[30] Thabane T & Snyman-Van Deventer E (2018) 23.
[31] Thabane T & Snyman-Van Deventer E (2018) 23.
[32] Mongalo T 'Directors' Standards of Conduct Under the South African Companies Act and the Possible Influence of Delaware Law' (2016) 2 *Journal of Corporate and Commercial Law & Practice* 2.
[33] Olivier EA (2021) 9.
[34] s 66 (1) of Act 71 of 2008 reads: 'The business and affairs of a company must be managed by or under the direction of its board, which has the authority to exercise all of the powers and perform any of the functions of the company, except to the extent that this Act or the company's Memorandum of Incorporation provides otherwise.'
[35] Olivier EA (2021) 6.

5.2.1 Does the new SOE bill address some of the failures identified in respect of SOC governance?

A new State Enterprises Bill[36] (the Bill) has been published for public comment on 15 September 2023.[37] The draft Bill proposes the dissolution of the Department of Public Enterprises, and plans to replace it with a holding company to supervise all SOCs; this holding company will be named the 'State Asset Management SOC Ltd.'[38]

According to the Bill, the State would be the sole shareholder of the holding company.[39] The president would be the sole representative of the holding company, but may transfer the administration of the Bill or any power or function referred to in the Bill to another member of Cabinet, in accordance with section 97 of the Constitution.[40] The rules of the PFMA and the Companies Act apply to the operations of the holding company.[41] Furthermore, in terms of the bill, the holding company acts through its board.[42]

In terms of the Bill, the holding company may conduct a due diligence of state enterprises and exercise the rights and restrictions as the sole or majority shareholder of any subsidiary of the company, on behalf of the state.[43] Although the Bill explains the steps to be taken when conducting the due diligence, a definition of 'due diligence' is not provided for in the Bill. The Bill proposes that the shareholder exercise all the rights and duties of a shareholder in terms of the Companies Act and PFMA, in relation to the holding company to promote and support the functions of the holding company.[44] Regarding the shareholder's powers and duties, the shareholder is entitled to appoint and remove the directors of the board,[45] and may determine the remuneration of the directors according to best market practice.[46]

The Bill provides a section on the 'material or persistent failure to meet objectives and targets.'[47] In terms of this section, if it appears that the holding company persistently fails to

[36] National State Enterprises Bill in GG 49312 of 1 September 2023.
[37] Davis R 'What's the new National State Enterprises Bill About?' *Daily Maverick* 19 September 2023 available at *https://www.dailymaverick.co.za/article/2023-09-19-whats-the-new-national-state-enterprises-bill-about/* (accessed 23 September 2023).
[38] s 3(2)(a) of National State Enterprises Bill GG 49312 of 2023.
[39] s 3(2)(a) of National State Enterprises Bill GG 49312 of 2023.
[40] s 3(3) of National State Enterprises Bill GG 49312 of 2023 and s 97 of the Constitution of the Republic of South Africa 8 of 1996.
[41] s 3(5) of National State Enterprises Bill GG 49312 of 2023.
[42] s 3(4) of National State Enterprises Bill GG 49312 of 2023.
[43] s 4(1)(d) of National State Enterprises Bill GG 49312 of 2023.
[44] s 5(1) of National State Enterprises Bill GG 49312 of 2023.
[45] s 5(2)(a) of National State Enterprises Bill GG 49312 of 2023. See also s 68 (1) of the Companies Act 71 of 2008.
[46] s 5(2)(c) of National State Enterprises Bill GG 49312 of 2023.
[47] s 6 of National State Enterprises Bill GG 49312 of 2023.

meet its objectives and targets, the shareholder may call a meeting to consider a form of corrective action to be taken.[48] Corrective action in terms of this section includes reviewing board membership and providing additional capacity to the board,[49] issuing instructions to remedy the failure,[50] or appointing an administrator to take control of the management of the holding company.[51]

With regards to the powers, functions and duties of the board, the Bill proposes that the board must advise the shareholder on the phased succession for the transfer of state enterprises to the holding company,[52] and conduct due diligence of state enterprises,[53] among other duties listed under section 7. The board is required to exercise all its powers under the Companies Act and the PFMA.[54] The board is required to devise a corporate plan with annual instructions issued to each subsidiary of the company.[55] The board must establish a governance and reporting framework for its subsidiaries,[56]must establish financial and operational performance monitoring framework for subsidiaries,[57] and is responsible for the appointment of the chief executive officer of the holding company after consultation with the shareholder.[58] According to the Bill, the board should be comprised of a minimum of five, and a maximum of eleven directors.[59]

In terms of standards of directors' conduct, the new Bill insists that directors adhere to section 76 of the Companies Act, as well as common law.[60] It states that the board of directors must act in the best interests of the company, while considering its long-term business sustainability, public interest and developmental objectives.[61] The board is required to submit an integrated annual report to the shareholder, at the end of each financial year,[62] which includes a report of

[48] s 6 of National State Enterprises Bill GG 49312 of 2023.
[49] s 6(2)(d) of National State Enterprises Bill GG 49312 of 2023.
[50] s 6(2)(e) of National State Enterprises Bill GG 49312 of 2023.
[51] s 6(2)(f) of National State Enterprises Bill GG 49312 of 2023.
[52] s 7(1)(a) of National State Enterprises Bill GG 49312 of 2023.
[53] s 7(1)(b) of National State Enterprises Bill GG 49312 of 2023.
[54] s 7(3) of National State Enterprises Bill GG 49312 of 2023.
[55] s 7(2)(a) read with s 7(4) of National State Enterprises Bill GG 49312 of 2023.
[56] s 7(5) of National State Enterprises Bill GG 49312 of 2023.
[57] s 7(6) of National State Enterprises Bill GG 49312 of 2023.
[58] s 7(7) of National State Enterprises Bill GG 49312 of 2023.
[59] s 8(1) of National State Enterprises Bill GG 49312 of 2023.
[60] s 9 of National State Enterprises Bill GG 49312 of 2023.
[61] s 9 of National State Enterprises Bill GG 49312 of 2023.
[62] s 11 of National State Enterprises Bill GG 49312 of 2023.

'detailed performance against targets',[63] a report on corporate governance[64] and a business sustainability report,[65] among a list of other required reports in terms of section 11.[66]

In terms of section 14 of the Bill, the shareholder may instruct the holding company to conduct a due diligence into a state enterprise.[67] The holding company must then make findings and recommendations to the shareholder, in terms of s 14(3).[68]

According to Minister of Public Enterprises, Pravin Gordhan, the initiative of a holding company for SOCs would improve financial performance and reduce political meddling.[69] He argues that the holding company will separate the state's ownership functions, from its policy and regulatory functions, thus minimising the possibility of political interference.[70] While the Bill holds great potential to improve financial performance, it is unclear how this structure would reduce political meddling, especially when considering that the sole shareholder of the holding company is the State.

The focus of the Bill should have been on creating avenues for private investments into the SOC sector, Ghaleb Cachalia, from the Democratic Alliance (DA), argues.[71] Cachalia thus refers to the Bill as a missed opportunity, as he believes SOCs should either be privatised or be open to the public, as public—private investors.[72]

However, Jacky Molisane, Public Enterprises Director General, explains that the aim of the holding company is to run SOCs 'professionally, and insulate them from political interference.'[73] She argues that the holding company would make use of Key Performance Indicators (KPI's) to ensure a certain level of performance is being met.[74]

According to Busisiwe Mavuso, CEO of Business Leadership South Africa (BLSA), a holding company structure could make sense, following the good examples of this structure as

[63] s 11(1)(c) of National State Enterprises Bill GG 49312 of 2023.
[64] s 11(1)(i) of National State Enterprises Bill GG 49312 of 2023.
[65] s 11(1)(j) of National State Enterprises Bill GG 49312 of 2023.
[66] s 11(1) (a – j) of National State Enterprises Bill GG 49312 of 2023.
[67] s 14 of National State Enterprises Bill GG 49312 of 2023.
[68] s 14(3) of National State Enterprises Bill GG 49312 of 2023.
[69] Davis R *Daily Maverick* (2023).
[70] Davis R *Daily Maverick* (2023).
[71] Davis R *Daily Maverick* (2023).
[72] Davis R *Daily Maverick* (2023).
[73] Davis R *Daily Maverick* (2023).
[74] Davis R *Daily Maverick* (2023).

displayed in Kazakhstan and Singapore.[75] According to Mavuso, a state holding company that is fully empowered to do the necessary to turn around and manage SOCs, and bring in private shareholders, is welcomed.[76] Mavuso believes this structure would ensure that proper commercial principles are applied in these entities.[77] She argues however, that in order to achieve that, the holding company needs a level of independence, including budgetary autonomy.[78] Mavuso further emphasises the importance of appointing a board of accomplished, experienced professionals with extensive corporate expertise, and not 'political cronies.'[79] Furthermore, Mavuso suggests that while the holding company must report to a suitable government department, it should have a line of accountability to Parliament.[80]

Mavuso expresses concern over the Bill envisaging sole or majority shareholding for the holding company, leaving out the option of minority ownership. She argues that in good examples of holding companies from across the world, they are able to trade their interests in companies, to realise the most value for the state.[81]

While the proposed holding company would potentially solve the issue of oversight and monitoring board effectiveness, the 'sole ownership' by the State remains an area of concern. The only evidence produced for the reduced political meddling is in the promises from the Minister of Public Enterprises. The Bill does not provide clear guidelines preventing political appointments or political interference in SOCs.

This paper has identified the challenges posed by the process of appointments and dismissals of board members, and the instances of political appointments, particularly at SOCs. The new Bill could have used this as an opportunity to clarify and simplify this process, to effectively remove the possibility of political meddling when it comes to board appointments. Instead, the Bill once again states that the shareholder is entitled to appoint and remove the directors of the board and determine the remuneration of the directors of the holding company.

The section on the 'material or persistent failure to meet objectives and targets,' however, seeks to address the challenge of oversight and board effectiveness. It provides an effective way of

[75] Mavuso B 'BLSA CEO Newsletter – 18 September 2023' *Business Leadership South Africa* 17 September 2023 available at *https://hub.blsa.org.za/blsa-ceos-weekly/blsa-ceo-newsletter-18-september-2023/* (accessed 23 September 2023).
[76] Mavuso B *BLSA* (2023).
[77] Mavuso B *BLSA* (2023).
[78] Mavuso B *BLSA* (2023).
[79] Mavuso B *BLSA* (2023).
[80] Mavuso B *BLSA* (2023).
[81] Mavuso B *BLSA* (2023).

measuring the performance of SOCs, identifying failures, and addressing upcoming challenges. Though this process is potentially tedious and administratively burdensome, it will certainly address the challenge of oversight. The Bill addresses certain deficiencies in the Companies Act, such as the failure of the Companies Act to expressly regulate oversight. The Bill proposes that the board establish a financial and operational performance monitoring framework for subsidiaries, thus addressing the oversight function of directors.

5.3 RECOMMENDATIONS

In summary, this thesis has found that there is a direct causal relationship between the performance and effectiveness of the board of directors, and the productivity and financial performance of the company. The economic contribution of SOCs to the country has been largely emphasised throughout this paper. It is clear that these companies are responsible for certain essential goods and services and are major employers in the country. Thus, the underperformance by an SOC has large societal effects, as seen through the effects of loadshedding due to underperformance at Eskom, for example. This paper thus sought to determine if the mandate of SOCs, to advance economic growth, development, and transformation in the country, are being achieved.

This thesis has emphasised that the board of directors is the driver of corporate governance in a company. By assessing the extent to which the fiduciary duties and liabilities of directors of SOCs facilitate good corporate governance in South Africa, this thesis has found that certain duties of directors are in need of more development and legal guidance. Essentially, this paper has found that the legal framework governing director duties and liabilities should be developed and amended, in response to the recurring challenges faced by SOCs in the country.

As recommended by Mofokeng,[82] the absence of a singular framework governing SOCs has had an adverse effect on the sector. At first glance, the idea of a new singular framework proposes an administrative burden on the entire sector and the companies. However, it could provide clear guidelines, rules, duties, and liabilities, contained in one statute, applicable only to these SOCs. The sector supplement in the King IV for state-owned entities, proves that companies of this nature, could benefit largely from a separate, singular, governing framework. This thesis therefore agrees with Mofokeng and recommends a singular governing framework.

[82] Mofokeng T 'Good Corporate Governance Affirms the Board (Led by the Chairperson) as the Focal Point of Governance and the Courts Have no Mandate to Undermine this Principle' (2020) 6(1) *Journal of Corporate and Commercial Law & Practice* .

Secondly, as extensively focused on in this thesis, the director's oversight function is largely underdeveloped, in comparison to other jurisdictions. South African SOCs will benefit greatly from clear guidelines in terms of performing their oversight function. This function should not be overlooked as a duty of the board of directors, as the performance of the company depends on the leaders of the company executing their oversight role, to ensure compliance with rules, to measure performance, and to ensure certain standards of corporate governance are being implemented.

In line with the recommendation to develop the oversight function, there should be an independent compliance committee developed that would ensure the compliance with legal duties and responsibilities and ensure the implementation of the rules in terms of the Companies Act, PFMA, and other regulations. This independent compliance committee should be established independently from the Department of Public Enterprises, specifically to monitor the division of power between the shareholder representative, and the company in question.

This thesis has largely focused on 'political meddling' at SOCs, at the hands of their shareholder representatives. For many reasons already discussed, this paper proposes the strict enforcement of the division of power between the shareholder and the company. The recommended committee referred to above, should monitor this at SOCs.

In addition, this independent committee should see to the provision of a fair, equal, and ethical process for the appointment and dismissals of board members, in line with the requirements of the King IV, and the Companies Act.

The reasons for recommending a committee to monitor these processes, is to avoid the situation of a tick-box compliance system, wherein companies comply with all legislative requirements, but compliance is not underpinned by ethical corporate behaviour. This independent committee should assess an SOC's compliance with crucial provisions in terms of the Companies Act, PFMA and their relevant founding legislation, by making routine yearly assessments of the company's standing. This committee may provide consulting and advisory services to SOCs, to ensure that ethical business practices are implemented, and that the principles of good corporate governance are maintained.

While an independent committee will assist in ensuring SOCs meet the requirements of the Companies Act and other relevant legislation, it will not, and cannot absolve directors of their legal duties to the companies on which they serve. Not much can be done from a legislative

perspective to avoid instances of directors using their positions to benefit themselves, at the expense of the company. In this regard, it is crucial that systems are in place to detect irregular practices early, and that directors are held sufficiently accountable.

This paper has also clearly identified the crucial nature of the oversight function of directors. In order to fully develop the vital oversight function of directors, legislation must be amended. The well-developed oversight function provided for in terms of the Model Business Corporation Act, discussed in Chapter three,[83] serves as a guideline for South African legislators, in terms of developing this crucial function of director duties.

[83] Chapter Three: The Functions and Effectiveness of an Soc's Board Of Directors. See also The Model Business Corporation Act (Revised 2016) (December 9, 2016)

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