

KING IV IS HERE: CORPORATE GOVERNANCE IN SOUTH AFRICA REVISITED

By Vishnu Padayachee

The author is distinguished Professor, and Derek Schrier and Cecily Cameron Chair in Development Economics, School of Economic and Business Sciences, University of the Witwatersrand, Johannesburg. Life-time Fellow, Society of Scholars, Johns Hopkins University, Baltimore and Washington DC.



Vishnu Padayachee

Codes of Conduct for corporate governance have been evolving over the past few decades. The article assesses the progress in local corporate governance with the launch of the latest King IV code for South African corporations in 2016 and argues that unless there is transformation in these critical areas, King IV is not likely to have any teeth.

In 2013 I published an article entitled “Corporate governance in South Africa: from ‘Old Boys Club’ to Ubuntu?” in the journal *Transformation* (81/2, July 2013) on which I draw from here. With the launch in November 2016 of local corporate governance code King IV (with its focus on ethical leadership, organisational values and responsible corporate citizenship, as well as further refinements to governance structures) (Directorship, April-June 2016) it may be useful to return to assess progress in some areas of South African corporate

governance. While I believe that all the King codes have been valuable to improve corporate governance in South Africa since 1994, many issues of concern remain, which are not in themselves matters for any code but rather about corporate culture in the context of South African capitalism.

In this regard we are pleased to support the King IV focus on the themes of (1) the need for further board diversity (race, gender), and (2) the process, transparency and ethics surrounding remuneration, including of board members and executives. (Business day 16 November 2016). My argument first made in 2013 that South African corporate boards especially in the private sector, remain largely untransformed and are governed in the old ways, is vindicated by this latest King IV Report (2016). The focus on remuneration draws attention to, even if it does not and itself cannot resolve, the matter of the growing inequality evident in our society and in many other capitalist countries between a corporate elite and the rest. If these recommendations regarding diversity and remuneration become incorporated into revised JSE listings >>



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requirements, we will have arguably for the first time given real teeth to King recommendations.

In the 2013 article I examined developments in the culture and practice of corporate governance largely within the private sector in South Africa. My analysis showed the dominance of powerful individuals, family trusts and groups sharing common social, cultural, and linguistic norms, bound together outside the boardrooms thorough old school, club, societal, political, church, sports and other such networks. A sound corporate governance culture based on transparency and disclosure hardly existed before and during the apartheid era. Since 1994 and as South Africa opened up to global economic circuits and institutional rules and practices, there has been a much stronger commitment, at least nominally, to compliance with developments in global corporate governance. The King codes of corporate governance (then version 3) are the strongest indication of this. South African companies have over the last 18 years shifted from an initial state (a management controlled, 'social club' approach to corporate governance) towards an Anglo-American corporate governance model, practising what is widely referred to as 'shareholder wealth maximization'. But I also argue that the practice of this approach remains uneven, as large family networks (both old and new) still exercise significant influence in boardrooms.

CORPORATE GOVERNANCE IN THE TRANSITION: A SUMMARY

Corporate governance in South Africa has changed since the advent of democracy in 1994. It has moved along the governance spectrum towards an Anglo-American approach, sharing features of the light-touch, regulatory kind found in the UK. This is evident

from the requirements of three codes of corporate governance, King 1 (1994), King 2 (2001) and King 3 (2009) which apply to all JSE listed companies, public entities which have to comply with the Public Finance Management Act, as well as all banks and financial institutions. The King codes stress outsider control, independence and transparency aimed at maximising shareholder wealth. Technical (tick-box) compliance appears on the increase, but whether South African corporates are, in fact, getting right the balance between improved governance and better performance remains unclear. The new Companies Act became law in May 2011 and it requires that directors will be held legally responsible if it can be shown that they did not apply their minds to their fiduciary duties, among other legal sanctions, a move that would nudge the corporate governance framework towards the post-Sarbanes-Oxley US model. I do not underestimate the significance of this "shift" to Anglo-American model of corporate governance in South Africa over the last 15 or so years.

THE 'END' OF PYRAMID STRUCTURES

Some commentators I spoke to as part of that earlier research regarded the "ending" of the pyramid holding structure for governing South African companies prevalent for over a century mainly in the mining-industry and finance, as the most dramatic indication of the changed corporate governance structure in South Africa after the end of apartheid. I questioned whether or not this was in fact totally true.

The advent of democracy, the opening out to global competition and the sheer scale, vision and ambition of key figures in the South African corporate world have all contributed to change within South Africa's

corporate structure and in the strategic restructuring of these corporations. Those who recognise major changes in this area include Malherbe and Segal (2001: 1) who point out that:

A decade ago, the six mining finance houses – corporate structures peculiar to South Africa, though reminiscent of the Japanese pre-war Zaibatsu, and formed under similar circumstances – dominated the economy. Today, the mining finance house no longer exists. Along with the demise of the mining finance house, two of its widely imitated characteristics – diversified holdings and the entrenchment of control through pyramid structures – have fallen from favour.

The main forces of change, they argue, for this has been market discipline imposed through falling equity prices, as well as the 'role played by foreign institutional investors, who robustly criticized corporate structure, governance and performance upon their return to South African markets in 1994. (2001: 4).

Andrea Goldstein (nd: 31) makes this point in the following way: "The great Transvaal houses, that dominated the economy for a century or so, are fast disappearing, to be replaced by focused operating companies with only a few dozen head office employees.

Jim Sutcliffe (ex-Old Mutual plc CEO) when asked what he would regard as the most significant change in South African capitalism post-1994 pointed to the demise of the group-holding, pyramid structures and extensive cross-holding directorships which characterized capitalism under apartheid (Interview, 30 July 2007). Not only have companies unbundled and restructured as pointed out above, but the phenomenon of the 'big man', the Executive Chairman and CEO rolled into one, who no director

would dare challenge (people in the mould, I would suggest, of Ernest Oppenheimer, Harry Oppenheimer, even more recently, Brian Gilbertson, Mike Levett, Warren Clewlow), is no longer a dominant feature of South African corporate boardrooms. Many of the new non-executive directors also have a very different sense of their fiduciary responsibilities (their duties and personal liability for example will increase hugely in the proposed new Companies Act to the point that analysts have expressed concern about who would want to serve as non-executive directors). In general a far greater sense of democracy and consultation over strategic decisions exist. (Barry Wood, Neville Kerdachi, directors VCB SA Holdings Pty Ltd, joint interview, May 2007).

These developments in corporate structures and governance may have dealt a blow to the appeal of the MEC as a way of making sense of capital accumulation in South Africa, but is it a fatal blow? Alan Hirsch has pointed out that while the holdings of the ‘big five groups – Anglo, Sanlam, Mutual, Liberty and Rembrandt – slipped from control of companies accounting for 85.7% of the market capitalization of the JSE in 1992 to 54.7% by 1998’ (2005: 196) it rose again to nearly 60% by 2002. This is still a highly significant figure. Hirsch has argued that while ownership concentration has declined somewhat, market concentration has not. Chabane et al have referred to a process whereby South African conglomerates, partly under BEE imperatives, partly to stave off the perceived threat of rising foreign competition, unbundled, then rebundled within more focused areas of economic activity, and in the process have become powerhouses and dominate their sectors locally and globally. Anglo (mining), BHP Billiton (mining), SAB Miller (beer) and Standard Bank Liberty (finance) are prime examples in their respective sectors. (in, Hirsch, 2005: 197-8).



corporate governance in South Africa’s public sector, has been characterised by one major scandal or other over the last ten years

Despite the erosion of group holding structures’, Zav Rustomjee former Director General in the Department of Trade and Industry, maintains ‘the locomotive of the Minerals Energy Complex that dominated the structure of the South African economy still continues... group holding power (largely domestic capital) may have morphed into a slightly more diffused form – but the same business characters and groups (with a few additional domestic and global players) seem to have continued to determine the course.’ (Personal communication, 28 January 2007).

B-SHARES

In some cases some novel strategies have been introduced to ensure that while ‘restructuring’ and ‘dismantling’ appears visible and transparent, control, especially by founding dynastic families, continues.

In June 2016 the retail giant Pick and Pay, founded by Raymond Ackerman in 1987, announced that it would end its ‘much derided’ and ‘archaic’ pyramid control structure only in August 2016. “The founding Ackerman family introduced the pyramid structure in 1981 to prevent a hostile takeover”. The new proposal will allocate to the Ackerman family a new class of unlisted voting shares in Pick n Pay Stores — “B-shares” This will ensure

that the family continues to have a controlling interest in the company. (<http://www.financialmail.co.za/moneyinvesting/2016/06/14/pick-n-pay-unbundles-its-pyramid>).

In other words, as the Business Day pointed out “the status would remain. “The Ackerman family – via Ackerman Investments – will retain voting control of Pick and Pay after being issued a new class of unlisted B-shares (Business Day, June 15, 2016).

Similarly the Rupert family also controls investment giant Remgro through unlisted B-shares.

The other great dynastic South African family the ‘Oppenheimers’ sold the family interest in de Beers only in 2011, some 84 years after they first assumed it in 1926. In a “stunning and historic announcement that ends an 85-year-old dynasty, the Oppenheimer family ...sold its 40 percent stake in De Beers to the diamond giant’s one-time sister company, Anglo American, for \$5.1 billion. (<http://www.jckonline.com/2016/01/20/oppenheimer-family-gives-control-de-beers>.) It is worth looking into the role of the Oppenheimer family in South African boardrooms today, but that is not what I am able to do here.

B-Shares carry important and potentially controlling voting rights but do not participate in dividends or other income distributions. “Usually, the purpose of the super voting shares is to give key company insiders greater control over the company’s voting rights, and thus its board and corporate actions. The existence of super voting shares can also be an effective defence against hostile takeovers, since key insiders can maintain majority voting control of their company without actually owning more than half of the outstanding shares”.

<http://www.investopedia.com/ask/answers/05/070405.asp#ixzz4BkG89Lh3>

Through such B-shares a shareholder with minority interest could hold sway over key votes and >>

it would appear common-sense to be somewhat way above any company which has more than one class of ordinary shares. It is an 'anti-market' and 'artificial' practice that is nominally frowned upon by the JSE. So since the 1980s and early 1990s when many pyramid structures existed, many have been dismantled more recently: Mobile (through Trencor); Bidcorp (which held Bidvest); and Liberty Holdings are notable examples. A few will still remain if Pick and Pay is dismantled. These include Capevin, which has a significant minority stake in liquor giant Distell; and African and Overseas Enterprises, which owns Rex Trueform. (Business Day, 15 June 2016).

In South Africa's particular circumstances during the transition to democracy where there is pressure from above for true black economic empowerment, there exists the danger that B- class shares (and similar devices such as N-Class shares) could offer the potential to appear to increase black shareholding while old dynastic white male "old boys clubs" and founding families, could continue to exercise effective power through such mechanisms. I say could advisedly because we need to look deeper at some cases before reaching any conclusions.

THE PUBLIC SECTOR

One may surmise that corporate governance within South Africa's powerful state-owned enterprises (SOEs) would be conducted within the framework of a more developmentalist agenda than being based on a narrow pursuit of profit. That is, that it would be more stakeholder driven rather being based on narrow shareholder wealth maximization. However, corporate governance in South Africa's public sector is set by the Protocol on Corporate Governance in the Public Sector (Department of Public Enterprises, 2002), which, as



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Benjamin Marx confirms (2008:178) aims to 'maximize shareholder value and provide guidance on corporate governance issues in the public and SOE sector'. The first objective is rather strange, and despite the clarity of the guidance set out, corporate governance in South Africa's public sector, has been characterised by one major scandal or other over the last ten years. SOEs in South Africa comprise some 270 entities with a turnover in excess of R15 billion per year. The six major ones, including Eskom, Transnet, Denel, fall under the political control of the Department of Public Enterprises. Others are controlled by the National Treasury (World Bank 2006). However, the state's interests in some have been privatised (e.g. Telkom, Acsa) and some SOEs have been corporatised (run along commercial lines, e.g. Eskom, Transnet). The international buyers in the case of Telkom and Acsa, were given management control, so diluting board oversight to some extent. In other cases, the requirement to become less dependent on state funding (eg. the national and provincial development finance corporations) has driven their management and governance logic into highly confusing territory. Powerful

SOEs such as Eskom, SAA, Transnet and the SABC, have been in the news regularly over the last few years for one or other corporate scandal (involving either allegations or proven instances of bribery and corruption at board and top management level, ineffectual or incompetent leadership, state interference, secret deals, and the like).

Board room intrigues, financial irregularities, and serial breaches of even the most basic corporate governance codes and rules, are now commonplace. My colleague Jannie Rossouw makes the following observations in respect of South African Airways, arguably the most scandal-ridden and poorly governed state entity in South Africa.

That South Africa's national airline is in a parlous state is no longer in dispute. It has delayed releasing its financial statements four times over the past 10 months. No convincing reasons have been provided for the delays. The failure to issue financial statements on time is partly a reflection of the incompetent leadership that has led the airline astray in recent years. To be sure, the airline has been rocked by boardroom shenanigans for some time. It has over the past 10 years or so experienced unprecedented leadership volatility with frequent changes to the board and the CEO post. The tenure of the current board chairperson, Dudu Myeni, has taken things to a new level of scandalous corporate governance. It is clear that Myeni is unqualified for the post of chairing the SAA board and has only survived due to her close relationship with President Jacob Zuma. (Rossouw, 2016).

There is no doubt in my assessment that, despite some criticisms of some of its features (see Padayachee, 2013), that the King codes introduced in South Africa since democracy have been a very valuable tool in the

corporate governance landscape in this country, building upon and even extending upon global developments in this field. However, I argued in my 2013 article that there is little substantive evidence that corporate governance in the new South Africa had moved beyond some level of nominal and technical compliance with King recommendations, and even thus unevenly, embracing a more stakeholder-oriented philosophy. Andreasson's assertion (2011) that principles of Ubuntu and African values are to be found in our corporate governance framework, remains a desirable goal that is still far from current reality. That is a reflection of poor and weak leadership at board levels as practised by both the 'Old Boys' and the so-called "transformed boards". The latter have largely failed to penetrate the corporate culture of the old South Africa, and in fact appear to have accommodated themselves rather nicely into past practices.

The adoption of triple-bottom line reporting by companies (financial, environmental and social sustainability) as expected by the King codes is being observed more in the breach than in reality, as financial issues override goals of social responsibility and environmental sustainability. This view is confirmed by a former Deloitte's chartered accountant, with over 40 years experience of South African corporate practice. (Gavin Brown, 21 August 2013). A number of features in the country's governance framework suggest that a more broad-based, socially based corporate governance framework in which the interests of all stakeholders, including workers and their representative organisations, are taken into account, and suggestive of a more caring, humane capitalism is still far off the mark. These features, in summary, include:

- non-executive directors are still drawn from a narrow circle and

remain overwhelmingly white and male, and despite BEE imperatives, black share ownership remains a very low percentage of market capitalisation on the JSE;

- moves towards establishing two-tiered boards, with worker and other social-partner representation on its 'supervisory' boards, are not on the cards;
- attention to what many consider legitimate business issues outside financial considerations, such as social and environmental concerns, labour standards and safety measures, are exceptions rather than the norm;
- private equity buy-outs of listed companies continue to shrink the possibilities of a more broad-based participation of South Africa's black majority in corporate ownership and activity;
- governance at South Africa's powerful state-owned enterprises, which could have been expected to lead the move to more stakeholder models is, with notable exceptions, characterised by incoherence, lack of focus, and corruption scandals.



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In my review of developments since then, and as the adoption of King IV approaches, suggests that little has changed. At the level of public sector governance, there is little doubt that the news is unambiguously

negative. Any claims that the country's corporate governance approach is more stakeholder-oriented, more transparent and democratic, more caring, more harmonious, more Ubuntu-oriented and more connected to society, would appear somewhat exaggerated.

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