# Interview Summary Report

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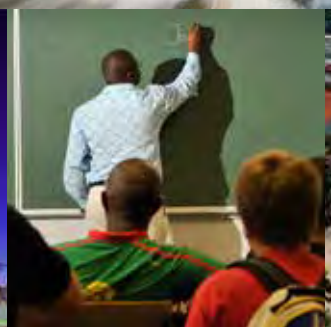
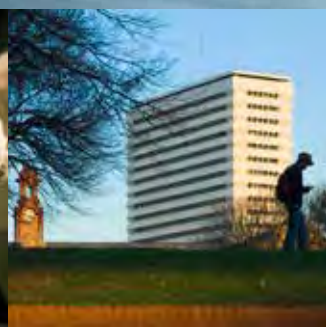
Corporate Governance Research Programme
Albert Luthuli Centre for Resposible Leadership





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# Executive summary

Human beings are essentially social animals defined by their shared humanity – their mutual dependence. Cooperation and altruism are part of our nature, an evolving set of behaviours that are equally relevant across society and business organisations. As an inherently social species, we tend to display cooperative behaviour – but not always persistently, or indeed competently.

Prior to 1990, the South African economy was almost entirely isolated due to sanctions enforced during the Apartheid era. Most large corporations were family owned conglomerates, operating within a culture of cronyism and a general lack of accountability. South Africa's turbulent history, culminating in a largely successful transition to democracy, has left a profound and lasting impact on its people, giving rise to an increasing sensitivity towards reconciliation, dialogue and – most importantly – *inclusivity*. Such factors, most commonly witnessed in South African politics, have also pervaded the economic sphere, specifically in the context of corporate governance. Today, corporate governance in South Africa is among the most advanced in the world, largely supported by the three King Codes of Governance Principles which were issued in 1994, 2002 and 2009.

The first King Report was an attempt to mitigate uncertainty, reintroduce and update business practices in preparation for exposure to international markets. More importantly, the King Committee sought to help (re)build a society, based on a reassessment of *values*. Unlike rules based approaches, such as the Sarbanes Oxley Act in the US, the King Reports focus on providing corporate governance *principles*: both a practical and ethical framework that attempts to show corporations how to create value, both for themselves and their stakeholders.

The initial King Report and its long-standing Committee may be seen as a positive outcome of a society in turmoil. Published in 1994, King I coincided with South Africa's transition to a unified and democratic state. Both the Report and the first free elections marked a fundamental transition: the former in business and the latter in politics. A common element shared by both events is the concept of inclusivity, specifically the central role of the stakeholder. In effect, the King Report argued that South African corporations could no longer operate within a social and economic vacuum. King I was also notable for integrating a number of principles into the Johannesburg Stock Exchange as a listing requirement. The JSE's role in promoting the King principles strongly contributed to the success of corporate regulation across South African listed companies.

The aim of the second King Report was to consolidate and provide practical guidance on emerging governance trends. King II was also a response to the large-scale corporate failures that rocked the financial markets *circa* 2002. The causes behind this initial period of global economic tumult were perceived by many to be a result of short-termism, greed, uncontrolled risk taking and an associated lack of accountability. The Report duly emphasised a stakeholder-inclusive model of governance, while also tackling sustainability issues for the first time. Both these themes were strongly associated with the African values philosophy commonly referred to as *Ubuntu* – loosely translated as 'shared humanity'.

King III, driven largely by the introduction of the New Companies Act of 2008, marked a shift toward integrated reporting, particularly in the context of embedding sustainability practices into governance strategy. Integrated reporting aims to unify both

Photos (Left to right): Sizwe Nxsaana, Roy Anderson, Ann Crotty, John Oliphant and Joanne Yawitch

financial and non-financial performance into strategy, processes and reporting. King III further saw a strong emphasis on the importance of ethical values and leadership, in an attempt to establish a theme of corporate *citizenship* within its principles. The tenets of ethical behaviour and sound leadership were chiefly aimed at helping internalise and actively apply principles of governance to corporate strategy formulation. In short, King III argued for a shift from the 'comply or explain' to an '*apply* or explain' approach within corporate governance.

Lately, however, the King principles' intrinsic usefulness within real world scenarios has come under increasing scrutiny, obliging all involved parties (the King Committee, corporations and South African society as a whole) to take a long, hard look at themselves – and at each other. Despite a progressive commitment to corporate governance based on responsibility, accountability and transparency, the principles' interpretation and their actual application appears to have faltered to a degree, with many South African firms failing to transcend a 'tick box' mentality to corporate governance.

A part of the problem may lie in the ever-increasing complexity and granularity of the King Codes. For some corporations, the King Reports and the principles they promote are a bridge too far. An associated dilemma concerns the fact that the King principles are *not* laws or embedded rules, which may be interpreted as both their greatest strength and weakness. That said, the King principles are intentionally ambitious, wide ranging and inclusive.

A growing realisation is that principles of corporate governance – however well meaning or elegantly argued – will see relatively limited success without the support of an informed and proactive investor base. On a broader scale, the King principles' successful application can only be truly effective if they take root in *all* facets of an organisation and its stakeholders. In order for the principles to work they must first be integrated into the cultural mindset, which effectively includes every member of South African society.

The problem of achieving such levels of inclusivity raises deeper questions concerning responsible leadership, self regulation and human behaviour – and the sacrifices an individual is willing to make in the interests of the *other*. The King Codes effectively force us to confront our bad habits and all-too-human idiosyncrasies. For example, is it possible for a business organisation to take into account the interests of *all* its stakeholders, including investors, employees, local communities and the environment? Conversely, will stakeholders ever accept their responsibilities, or will the promise of short-term profits continue to enjoy precedence? Can a set of progressive principles gain greater traction than reactionary laws? Can an entire society be *persuaded* to be good, as opposed to being *coerced*?

And yet, the fact that questions such as these are raised and seriously discussed suggests that South African society is making a measure of progress. What remains to be seen is whether these dialogues ultimately lead to sustained action and a fundamental shift in human behaviour, based on the tenets of inclusivity, responsibility and sustainability. In that respect, the King principles may best be utilised as a guide on a continuing journey, rather than the goal itself.

# Foreword: corporate governance research project

## Interview summary report

There is no doubt that South African society is still coming to terms with the social and labour-related unrest that defined the Apartheid Era – an era we all desperately want to put behind us.

A current concern seems to be the lack of leadership, as seen in the events that culminated in the tragedy commonly referred to as the "Marikana Massacre". Such lapses in leadership, specifically responsible leadership, need to be placed in the context of a growing awareness of the role of business in society, particularly where good corporate governance is concerned. Taking a historic perspective of the role of business in society, it is evident that the debates we witness today have nearly come full circle. These debates are not isolated within a single theme or agency, where shareholders enjoy centre stage. Rather, today's debates are characterised by a much deeper appreciation and interrogation of the inter-dependency between business and all its stakeholders, including the natural environment. However, this "enlightened" view requires responsible leadership from all sectors in society, a harnessing of collective intent and a shared vision to make South Africa a better place for all.

The Albert Luthuli Centre for Responsible Leadership (ALCRL) aims to develop the next generation of responsible leaders in support of a just society and environment. The ALCRL further acknowledges that debating and creating a future world where leaders from all sectors in society act as "transient caretakers"[1] has never been as relevant and urgent as it is today. The current local and global landscape is in great need of leaders from all sectors in society who are deeply aware of their role in shaping a sustainable future world.

A key ingredient in achieving these goals involves identifying the context and frameworks in which leaders operate and to enable them to succeed in reaching the desired outcome. In the case of leaders in the corporate sector, corporate governance as a philosophy and practice plays a key role in providing a platform for exploring ways in which the role of business (and hence leaders) in society can be justified and strengthened. South Africa has undoubtedly made significant contributions to the corporate governance discourse over the past two decades.

The ALCRL's decision to pursue research in determining the drivers and consequences of corporate governance in South Africa falls clearly within its mandate to advance responsible leadership. There is no doubt that the progression of corporate governance from King I to King III has led to a situation where ethics, culture and responsible leadership form the pillars of good corporate governance. It can therefore be argued that the unique trajectory of corporate governance in South Africa over the last two decades mirrors the country's progression towards a democratic state that ultimately aims to build a solid moral foundation within society, characterised by a culture of ethics and responsible leadership. Whether we have succeeded in reaching the desired outcome (either as a country or within the business sector) remains a point of contention.

In my mind, the study conducted by the ALCRL makes an important contribution in the continuing investigation of evolving corporate governance, particularly with regard to responsible leadership lessons learned in the process. We should be mindful of these lessons as we head into an increasingly complex and uncertain future. This Interview Summary Report captures the crucial voices of thought leaders in the field of corporate governance over a period of two decades, offering a candid view of the history of corporate governance and the unique transitions from King I to King III. Further, the Report also examines future issues, providing a vision based on the lessons from the past in an attempt to shape behaviour and practices in support of a sustainable future world.

The research, interviews and the Report would not have been possible without the participation of the interviewees. Our sincere appreciation goes to each and every one of the 16 thought leaders who offered their time and invaluable expertise. I was struck by their passion, commitment and belief in the importance of corporate governance.

We are also deeply grateful for the role the Gordon Institute of Business Science (GIBS) played in offering their time and expertise in creating the documentary, including the recording and editing of the video interviews. We also wish to express our appreciation for Bruce Whitfield, whose professionalism and ability to harvest crucial information added a critical level of value to the Report.

Further, Ernst & Young and the South African Institute of Chartered Accountants (SAICA) have made this project possible through their generous sponsorship and support. The ALCRL greatly appreciates their continued support.

Finally, a special word of appreciation to Senior Researcher Jess Schulschenk for her enthusiasm and professionalism in compiling and delivering the Report.

We hope our readers enjoy the journey, and that it will inspire you to join us in our pursuit to advance responsible leadership for a sustainable future.

**Professor Derick de Jongh**
Director: The Albert Luthuli Centre for Responsible Leadership
University of Pretoria

[1]King M and Lessidrenska T. *Transient Caretakers: Making Life on Earth Sustainable*. 2009

## 1. Introduction

Corporate governance in South Africa is considered by many to be among the best in the world, as seen with the three King Codes of Governance Principles issued in 1994, 2002 and 2009, which have set international standards of best practice. A turbulent political history and active corporate citizenry have played a large part in shaping these dynamics. Despite the progressive commitment to corporate governance based on principles of responsibility, accountability, fairness and transparency, the interpretation and application of these principles appears to differ widely, and many South African firms are grappling to transcend a tick box mentality.

We ask the question: *can good behaviour be mandated*?

A series of interviews was conducted with key thought leaders on the topic of *Corporate Governance in South Africa*. Interviewees were chosen from a diverse range of backgrounds, experience and opinions. The interview panel included members of the King Committees since 1992, current and previous leadership of key industry bodies, both executive and non-executive directors of companies, as well as journalists and activists. A list of the interview panel is included as Appendix A. The interviews took the format of voice recorded research questions by the author followed by video recorded interviews by Bruce Whitfield for educational material purposes. Copies of the transcripts are available from the author.

This series of interviews forms part of a wider research initiative to investigate the drivers and subsequent development of corporate governance in South Africa. Through these interviews, the development of corporate governance in South Africa is explored while touching on the broader issues of compliance and performance, responsible leadership, and corporate sustainability. Finally, thoughts are shared on the future of corporate governance, along with lessons learned from the South African experience.

Copies of the transcripts are available from the author."

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Photos: Pravin Gordhan (top), Graham Terry (below)

## 2. The purpose of corporate governance

Corporate governance, in its original conception, was understood to be the system and process by which organisations are directed and controlled in order to ensure the protection of the interests of the owners. This defining purpose of corporate governance holds true for many who agreed that corporate governance should promote the stewardship of companies by ensuring accountability of management to shareholders (Nxasana, 2012a). Simple but critical aspects of corporate governance include the need for transparency and effectiveness to ensure that companies are not just profitable, but that this profit is realised in a regular manner (Andersen, 2012a).

Corporate governance should provide a benchmark that ensures a minimum standard of consistency that one can expect in relation to the way in which companies are managed and governed (Yawitch, 2012a). In more practical terms, corporate governance provides practical guidance on important issues relating to the application of the law in the boardroom and throughout the company (Armstrong, 2012a). This 'framework of accountability' explores the crucial questions: "What are boards for? What are they meant to do – or not? This is a good thing and a difficult thing" (Godsell, 2012a).

### The stakeholder's inclusive model of corporate governance

Gordhan (2012a) identified the role of corporate governance as guiding companies to be accountable not only to their internal missions, but also to the broader stakeholder community. South Africa's corporate governance principles, as embodied in the King Codes of Governance Principles, have successfully developed and refined an arguably stronger definition of the purpose of corporate governance compared to traditional Anglo-American models. South African corporate governance goes further by taking into consideration the role of business in society and placing strong emphasis on stakeholder inclusivity, long term sustainability and, ultimately, responsible leadership.

> "Today, the notion of sustainability and redefining success in terms of positive lasting benefits for the company, society and environment means that the purpose of corporate governance is to ensure that the way the organisations lead is conducted in a sustainable manner" (Adam, 2012a).

Corporate governance needs to take into consideration the environment in which a company is operating. In order for the company to be successful in the long term, it needs to consider both society and the environment as part of its long-term license to operate. This broader understanding of corporate governance places strong emphasis on a stakeholder-inclusive model of corporate governance for the company's own success. Further, such assumptions go hand in hand with the growing appreciation for the role of companies in society.

> "Companies are an important social structure. Most people spend most of their time at work– and most people work at companies. It's a very important part of social reality, so [companies] should be accountable, well governed, and function effectively. That's what corporate governance is meant to achieve" (Godsell, 2012b).

A broader understanding of corporate governance as a system for both internal and external accountability moves beyond the limitations of classical forms of capitalism, by providing guidance on issues of stakeholder capitalism and the responsibility of the business as a whole. Nxasana (2012a) sees this as the ultimate purpose of corporate governance: "to make sure that companies are accountable for their conduct, they are accountable for how they operate. They can make a positive contribution to the shareholders, but also to society as a whole".

### 2.1 Corporate governance and citizenship

Terry (2012a) interprets corporate governance in organisations attuned to a broader range of stakeholders as effective *corporate citizenship*. He acknowledges that while there are companies where the boards and directors are working primarily to enrich themselves, there is a growing understanding of the corporate citizenship context within corporate governance. Khoza (2012a) reflects on the concept in a broader sense, whereby he sees corporate governance as a manifestation of a company's sense of destiny – what it aspires to be, how it plans to achieve it and, ultimately, what principles guide both its actions and the destination. Such notions reach beyond the academic definitions of 'doing more of the right things and less of the wrong things'. Corporate governance addresses the big picture by keeping companies on track towards their long-term sustainability (Payne, 2012a).

> "This is not something that is completely new that has been dreamed up by academics or bureaucrats who are trying to impose it on you. In many cases, if you are busy with something reasonable, good and valuable and you've got like-minded people around you, it is no big adjustment. Corporate governance to me is usually common sense, […] basically doing the right thing all the time to all the stakeholders. I specifically use the word *stakeholders* because that encompasses everything and everybody. It's your staff, your shareholders, the community and spreads to non-human stakeholders – like climate, for instance" (Loubser, 2012a).

In simple terms, corporate governance is essentially about the moral integrity of a company.

## 3. The development of corporate governance in South Africa

South Africa's unique history has given rise to its arguably strong affinity to the values of inclusivity, dialogue and consultation. The interviewees agree that such factors play an important role in the development of corporate governance in South Africa – as has the drive to be internationally competitive. This report explores the development of corporate governance through a narrative on key historical events, an examination of some of the drivers that led to each of the King Reports, and the subsequent content and principles that emerged as a result.

### 3.1 King I

Prior to 1990, the South African economy was largely isolated due to the sanctions enforced during Apartheid. Most large corporates were family owned conglomerates. Corporate governance was essentially absent and many companies were characterised as having become complacent and ineffectively managed.

Nxasana (2012b) shared his experiences of being an articled clerk in the early 1980s:

> "Auditing and accounting operated on the basis of the Companies Act of 1973. When I started articles in the early 80s, companies were allowed to withhold information even to their auditors, on the basis of national interest. The level of accountability has changed quite dramatically over the last couple of years".

The King Committee was commissioned in 1992 by the Institute of Directors (IoD), amidst a period of tremendous political and economic turmoil. The mandate of the King Committee was to promote the highest standards of corporate governance in South Africa whilst taking into consideration global trends, the need to enable successful business environments for emerging business men and women entering into the South African economy, and the importance of ensuring South Africa's competitiveness as it re-entered global markets.

> "The report was issued 29 November 1994. The decisions had not been made about which way the new South Africa was going to go – whether it was going to follow the communist, socialist or capitalist route. So we stuck our neck out an awful long way in publishing this report before such decisions were made" (Wilkinson, 2012a).

Whilst largely influenced by the Cadbury Report issued in the UK at the time, the first King Report released in 1994 went beyond financial and regulatory aspects, placing a strong emphasis on inclusivity and the centrality of the stakeholder. This was the same year that South Africa celebrated its first democratic elections. Armstrong (2012a) notes that "Inclusivity was an important feature because, at the time, King I coincided with a transition into a fully fledged democracy and the need for business to integrate itself into the community of democratic South Africa – or at least to lend its credentials to being part of that process."

Professor King (2012a) shared his early experiences of founding the King Committee, and the realisation that the report would need to go beyond aspects of financial regulation as investigated by the Cadbury Committee.

> "In 1992 I was approached by the IoD to form a committee (because of my practical corporate background) to write down guidelines on how people should direct and manage companies. Our Companies Act was based entirely on the English Companies Act and it had never said anything about how you govern. The first time there was ever anything written about it was Adrian Cadbury's report in the late 80s, which discussed the 'financial aspects of governance', focusing on the primacy of the shareholder and on the financial aspects. That was his mandate. I wouldn't say it was his thinking, but it was his mandate. I started to realise that this was absolutely wrong because you simply can't look at this thing in isolation.

The King I Committee was very representative of South Africa and we came up with this concept to fit in with this new nation, of what became known around the world as the inclusive approach to governance – as opposed to the exclusive approach, which was the single bottom line in the primacy of the shareholder. The inclusive approach essentially means that the board should take into account the needs, interests and expectations of the stakeholders. The board's duty is therefore to promote the best interests of the company through maximising the *total economic value* of the company, *not* just book value."

**The Institute of Directors (IoD) establishes the King Committee – An overview by Richard Wilkinson**

Richard Wilkinson, CEO of the IoD in 1992, was instrumental in establishing the King Committee. Whilst the British Government had commissioned the Cadbury Committee as a result of corporate failures and a move towards increased financial regulation, the Institute of Directors in Southern Africa (a voluntary industry body) pursued the challenge of developing a set of corporate governance principles for what they felt was in the best interests of the country's development.

"Back in December 1992 our then Chairman, Glynn Herbert, received a copy of the Cadbury Committee Report. He came into the office to show it to me, as the Chief Executive Director of the IoD. I read it over a weekend and found it to be an interesting document. Bear in mind this was when everything was in a state of flux in South Africa. The talks had effectively begun when I said 'Well, if the Institute of Directors wants a meaningful place in the new South Africa, we should take the lead in developing a code of corporate governance'. We then took it to the IoD Council in the first week of February 1993. 'Right, run with it,' they told us, 'provided it doesn't cost us anything'. This was a challenge; Glynn and I went around looking for sponsors, and literally got a couple of thousand rand. We interacted with Cadbury a couple of times and then we started trying to identify people who we thought could make a meaningful contribution. That is how the King Committee came about.

"We decided that Mervyn King would be the right person to chair the Committee and that it should be named after him, in order to stay at arm's length from the IoD. The reason for our decision was that we were also looking for the support of organisations like the Institute of Chartered Accountants, the Institute of Chartered Secretaries, Business South Africa and a few of the other internationally recognised organisations. We ended up with a committee of 16 members. The IoD, through me, provided the entire secretariat for the committee – which was exactly the same way as had happened subsequently: everyone offered their services voluntarily. Not a soul was offered one cent in terms of remuneration. We all carried our own expenses as well. It was all done on a real shoe string.

"After 18 months of work King I was produced, with a lot of input from the likes of the Cadbury's, the Boschs and others. Mervyn King, Chairman of the Committee, travelled a lot and interacted with these other people involved in governance. So, we were getting ideas and inputs from other published reports for the workings of committees, and when the King I report was released in 1994 it was hailed not only in South Africa but internationally as the most comprehensive report on corporate governance that had been prepared up to that time."

Photo: Richard Wilkinson

## A stakeholder inclusive model

Adam (2012a) further contextualises the establishment of the King Committee by asserting that "King I came around when there was recognition that stakeholders have a role to play in organisations and [it] must be one of the first sets of corporate governance principles around the world that started talking about stakeholders". Stakeholder recognition, he asserts, was a critical driver for King I.

## The drive to be globally competitive

A key driver in the writing of the first King Report was also the drive to be globally competitive as South Africa re-emerged from its previously isolated economy. Good governance standards and practices are considered to be a cornerstone of a healthy and productive economy, and an important indicator for international investors. The King Committee sought not only to address the poor state of corporate governance in South Africa, but aspired to set international standards of best practice (Payne, 2012a).

## Cultivating a culture of corporate governance

At the time the Institute of Directors took further steps to build a culture of corporate governance in South Africa beyond issuing the first King Code of

Governance Principles. Wilkinson discusses the bold steps they took in developing the initial education programmes in-house, through the Centre of Directorship and Corporate Governance: "We must have run 150 programmes in the first three years, one-, two- and three-day programmes for bringing in newly appointed and aspirant directors. One of the major objectives of King I was to recognise what the previously disadvantaged could contribute to the new South Africa through business." (Wilkinson, 2012a)

### A principles-based approach

A defining characteristic of King I that has been maintained throughout subsequent King Reports is that it was principles-based. Wilkinson (2012a) shared the thinking behind this approach: "The codes are a set of principles. It's not law or regulation; we have enough of them which are not complied with in the country anyway so we didn't want the code to be in any way legalised". Subsequent legislation has resulted in a hybrid system of corporate governance in South Africa, The hybrid system, in conjunction with the debate behind a principles-based approach, will be explored further in following sections.

### Guidance for boards

> "With the benefit of hindsight, it was motherhood. Nobody had previously documented how companies should be governed and I think it was also the first attempt to get some sort of clarity to what the duties of the boards and committees of the boards were." (Andersen, 2012a)

The five key areas that the first King Code of Governance Principles investigated can be described broadly by the committees that were established, which included:

- The Director task group, which examined the responsibilities of executive and non-executive directors as well as the frequency, substance and form of information for stakeholders;
- The Audit task group dealt with the principle roles of auditors and internal auditors, as well as the appointment of audit, remuneration and nomination committees;
- The Stakeholders Links task group investigated the links between the various stakeholders;
- The Ethics task group developed a Code of Conduct setting out ethical practices in business enterprises; and
- The Compliance task group, which investigated the adoption and compliance of recommendations by all interested parties.

Roy Andersen chaired the Director Task Group and would play a crucial role in the months ahead as the newly elected President of the JSE.

**A blank canvas**

As a result of the broader processes of transformation over the past two decades, South Africa has had the opportunity to put a number of new operating systems in place – from the constitution through to a complete overhaul of legislation. Whilst their implementation remains a contentious issue, Yawitch (2012a) recognises the tremendous opportunity such a blank canvas provided South Africa. Andersen (2012a) further points out how revisions to the Johannesburg Stock Exchange and the New Companies Act in parallel to the development of the King Codes benefitted the country tremendously.

## 3.2 King becomes a JSE listing requirement

A critical step in the evolution of corporate governance of South Africa was a move by the Johannesburg Stock Exchange in 1995 to make aspects of the King Code a listing requirement. Whilst the principles remained applicable on a 'comply or explain basis', the backing of the JSE brought the centrality of corporate governance to the fore.

Roy Andersen (2012a), President of the JSE at the time, shared his experience of getting the King I recommendations applied as a listing requirement:

> "It was a very intense meeting at the stock exchange because there was a view that it wasn't our job to regulate the companies. Rather, it was our job to regulate the market. […] It was also clear to me that if the JSE didn't link King I to the listings requirement it would flounder because the King committee was a self-appointed committee without any backing. Yes, there was backing from the Institute of Directors, but what teeth would King have – unless it was linked to a listings requirement?"

Payne (2012a) asserts that the JSE's role in selecting critical principles contained within the King Codes were part of the success of regulation across South African listed companies. The JSE continues to include a selection of the King Codes of Governance Principles as listing requirements. Over time, many aspects of the King Codes have subsequently been incorporated into legislation.

**The early days of corporate governance**

Russell Loubser shared his experiences of championing corporate governance in the early days of King I, when he joined the JSE as President in 1997. At the time, merely asking the question "is that good corporate governance?" effectively implied a failure to understand that businesses simply didn't operate that way. Disclosure of remuneration was unheard of. He reflected on how much things have changed since then and how those companies which don't value corporate governance today are the ones standing at the periphery. His experiences were similar at the international meetings of exchanges:

"I put my position on the table a couple of times and said 'being an exchange doesn't grant you any license or right from being a good corporate citizen. Many of us are starting to list now and being an exchange puts you in a different situation. In many cases you are guiding a huge number of listed companies. Now you have an obligation as an exchange to take a position on corporate governance'. This was just before WorldCom and Enron and things like that. They looked at me and thought I was crazy. They thought they just needed to be there as an exchange: to facilitate the raising of capital and playing with shares – why should they take a position on corporate governance? Even worse was trying to impose corporate governance [such as] disclosing directors' remuneration – which is now a listings requirement. Then there were the [major corporate failures]and at the next meeting they said, 'OK, maybe you have a point'." (Loubser, 2012a)

**The King Reports go global**

"The fascinating thing was how [the King Report] literally went around the world. As an example, in 2001 I was asked by Kofi Anan to chair the UN committee on governance and the problems that had started arising out of the food for oil scandal. Similarly, a Japanese professor said to me: 'Judge King, I've got a book for you. It's in Japanese, but this is your work translated into Japanese in 1995. We've been teaching it in Japan since 1995'. I told the professor I'm flattered, at which he said I'm better known in Japan than I am in South Africa. So that was quite an amusing story, showing that [the King Report] really did go around the world. The King reports have sort of become a brand of corporate governance." (King, 2012a)

## 3.3 King II

Following international developments in corporate governance (including large-scale corporate failures in the UK and USA, as well as a few domestically) coupled with growing awareness of the need for sustainable development, the King Committee was convened to review the King Codes. In 2002 the Committee issued the second King Report. King II recognised the African value system of '*Ubuntu*' (essentially 'shared humanity') as the ethical foundation for corporate citizenship in South Africa, and began to elaborate on the principles with a set of guidelines for best practice.

### Getting practical about the principles

Phillip Armstrong (2012a), convener of the second King Committee, reflects on the global and domestic drivers that led to the comprehensive review of King I: "We'd seen a whole manner of crises around the world and there had been a range of initiatives both at the international level as well as national level with regard to corporate governance. It had pretty much become a key feature of an advanced economy. I think in South Africa the situation had matured – it was very much part of a global economy."

The aim of the second King Report was to provide a comprehensive assessment on corporate governance before defining practical principles to guide companies.

> "The real defining feature of King II was that South Africa had a place to work from in King I. This offered a real opportunity to really step up. The extensive consultation process that took place in South Africa and within the working groups made it a very thorough report that really sought to capture and address the many concerns into something that was cohesive, and which companies could use as a guiding principle as much as a regulatory tool" (Armstrong, 2012a).

Photo: Russel Loubser

## Reviewing the stakeholder-inclusive model of governance

Greater attention was paid to the issue of diversity in King II, owing to the recognition that leadership in many South African companies at the time remained predominantly white. Armstrong (2012a) saw the need for diversity not just as what any business should sensibly be thinking about, but he saw that it "offered the opportunity to really widen the director pool and bring in people who were skilled in their field or at least experienced enough to offer the necessary diversity that any company should look for, and not just in South Africa" (Armstrong, 2012a).

## Bringing African values to the fore

King II made an explicit reference to the role that African values played in evolving the ethics and values underpinning the code. Khoza (2012b) shared his reflections on the parallels between the spirit of *Ubuntu* and the principles of governance:

> "We are effectively dealing with the human condition as it relates to *others*. We are an interdependent species. The guiding principle of *Ubuntu* can be stated in one sentence: '*Ubuntungubuntu*'. In English you can put as, 'I am because you are, you are because we are'. We are interrelated beings, we operate best when we care about one another" (Khoza, 2012b).

## Sustainability and the triple bottom line

The shift in focus towards integrated sustainability reporting (and performance) that emerged in King II was one of its key features (Adam, 2012a; Andersen, 2012a; Khoza, 2012b). King (2012a) places strong emphasis on the growing awareness of planetary and leadership crises linked to the role of corporations that came about during the time of the World Summit for Sustainable Development in Johannesburg in 2002.

For Armstrong (2012a), it was a natural progression to introduce the concepts of sustainability, as South Africa was part of the global economy and beginning to understand that a company's credibility is not linked to financial returns alone. The second King Report again set international benchmarks, as the first such report to introduce a recommendation for sustainability reporting following the GRI guidelines.

> "South Africa really provides one of the few codes that provides a very comprehensive integration of the sustainability aspects of the company governance, particularly within the structural and functional role that a board and its directors would play – not just on corporate governance but in terms of the company's wider activities" (Armstrong, 2012a).

In retrospect, King (2012a) acknowledged that assigning sustainability within its own chapter left it considered by many as a silo – a self-contained topic – as opposed to the overarching context for which it was intended. Armstrong (2012a) reflects that it was a difficult concept to grasp for many companies: "The idea of the King report was to show how sustainability and its various aspects play a very critical and important part of any boardroom decision and strategy".

## Bringing in risk management

King II was also the first such report to introduce a chapter on risk management, which again contributed to international debates on corporate governance. Payne (2012a) reflects how "some of it was luck, like the timing – it just happened to coincide with the Enron-related world collapses.

But a lot of it was the continuity of the King Committee membership and the people of the JSE who were backing us. It gave us the confidence to say we can set some trends here".

## Disclosure of remuneration

Andersen (2012a) reflects how the King Committee was "under a lot of media pressure at the time to make sure we did go ahead with disclosure of remuneration" and felt that this was a major step in King II. The importance of executive remuneration will be discussed further in Sections 6.2 and 8.1.

## Introduction of IT governance

King II also saw the introduction of IT governance and security – a reflection of the evolving nature of corporate governance and the extent to which the King Committee was working to be cognisant of material issues for governance.

> "[IT] is now part of the DNA. IT governance is absolutely critical – if you let information out about your employees it's a criminal offence, so IT security is very critical" (King, 2012a).

## Concerns around the progressive nature of King II

King II introduced a number of world firsts in corporate governance codes and principles. Armstrong reflects on concerns that some of the recommendations may have been too advanced for the South African market.

"Given the socio and political environment that South Africa operated in, these were issues that all companies should be naturally thinking about. Over time these were going to be issues that would confront many companies anywhere in the world. We just felt it was relevant to have it in the codified structure of the King reports so there was some sort of ability to consolidate all these different aspects into a common platform of objectives and priorities that any board member should consider" (Armstrong, 2012a).

The very fact that many of these issues were being raised and addressed is an outcome of South Africa's unique situation and sensitivity to such matters. Armstrong also acknowledged that there was already considerable guidance from bodies such as the Global Reporting Initiative, AccountAbility and similar organisations. The aim of the second King Code was to consolidate and provide practical guidance on emerging governance trends.

**Ongoing work of the King Committee**

While the King Committee is well known for the King Reports which they produce, a lesser known fact is that Committee meetings have continued since 1992. King (2012a) points out that these meetings were held on the advice of Sir Adrian Cadbury, whose own committee has since disbanded: "He said to me 'Mervyn, don't ever disband your Committee, because this is an evolutionary process. It's changing as society changes – and so will governance change. Keep your Committee going'. This was the best advice I ever received. Since 1992 we have met every quarter and we've kept up-to-date with what is happening around the world".

King also shared the motivation behind the King Committee being entirely voluntary and unremunerated: "You did this in the interest of South Africa. You did not get remunerated. You don't even get reimbursed for your disbursements. I wanted to know that everybody sitting around that table really had South Africa's long-term interests at heart – and it worked. We have the best of everybody on the committees and the sub-committees".

The contribution of the King Committee in writing the King Reports cannot be underestimated, nor the extensive consultation that was undertaken. Armstrong (2012b), convener of the Second King Report, shared his experiences and reflections: "The development of the code has always involved a very complex level of engagement and consultation – it wasn't just something that was prescribed in terms of what a small group of people felt was a good idea. It had a much wider consultative process, which I think is the strength of the report in terms of the public-private sector dialogue that took place".

**JSE launches the JSE SRI Index**

In 2005, the JSE launched the Social Responsibility Index (JSE SRI Index) in a move to bring key sustainability issues to the fore through a structured index. Again, they were the first emerging market and the first exchange in the world to do so: "We were the first emerging market and the first exchange, and there is no reason why an exchange should come up with an SRI Index. There are lots of other NGOs and bodies and COP 17s that should come up with something like that – but didn't" (Loubser, 2012a).

Photos: Nigel Payne (top), Mohamed Adam (bottom)

## 3.4 King III

With the revision of the South African Companies Act, the King Committee reconvened in 2008 to review the currency of the King Codes. The third King Report was released in 2009. The report placed strong emphasis on leadership, sustainability and corporate citizenship (Andersen, 2012a). A key recommendation from King III was that all companies should produce integrated reports. Integrated reports aim to embed integrated thinking on both financial and non-financial performance into strategy, process and reporting. King III also saw a shift from 'comply or explain' to an '*apply* or explain' approach.

### The New Companies Act

The introduction of the New Companies Act (NCA) was a major driving force behind the publication of King III. Considerable delays in the release of the NCA proved to be problematic to King III, which sought to align itself with the Act (Payne, 2012a). The problem is further discussed in later sections.

### Deeper understanding of sustainability through integrated reporting

A major outcome of the third King Report was a shift toward embedding sustainability into governance strategy, achieved in large part through the recommendation for integrated reporting. Integrated reporting will also be explored in more detail in Section 6.3.

### Leadership and corporate citizenship

The introduction of King III places a strong emphasis on the importance of ethical values and leadership, and endeavours to set a tone of corporate citizenship for the principles that follow (Payne, 2012b). This is in part due to the fact that many of the issues, such as stakeholder inclusivity, are being passed on to communications departments and boards who are not internalising nor applying the principles of governance to their decision making and broader strategies.

Photo: Mervyn King

"What King III was trying to do was elevate issues about what leadership was thinking and create that link between the responsibility of an organisation to the society that it fits into. Leadership needs to be involved in these sustainability issues and how we report to stakeholders about these things. It was firstly trying to give a context of what leadership entailed and that it was responsible leadership on an ethical foundation. From that stepping stone, the board should integrate sustainability issues with strategy. That is how you *lead* an organisation" (Adam, 2012a).

**The doyen of corporate governance: Professor Mervyn King**

"Mervyn King has had a tremendous impact on the country in terms of his vision and the way in which King I, II and III have progressed. I think very often – and you see it in all walks of life –when you have somebody that has that vision and leadership it does have an impact. You get criticised as well, but I think for him he has had a clear picture" (Terry, 2012a).

"Mervyn King is a very sought-after brain in thought leadership. He is one of those that are at the cutting edge on thought leadership where corporate governance is concerned" (Khoza, 2012a).

Professor Mervyn King convened the first King Committee and has been leading the corporate governance process in South Africa ever since. South Africa is often considered ahead of the game in terms of introducing new principles or incorporating burning issues into the governance frameworks. Many contribute this to Professor King's extensive involvement in international developments of corporate governance which he fed back into the King Committee during their quarterly meetings over the past two decades. As the chair of the Global Reporting Initiative, for example, he led the latest thinking on sustainability reporting which, combined with his visionary take on governance, led to integrated reporting being a core principle in King III.

Professor King is currently the Chairman of the International Integrated Reporting Committee and has previously held positions in the United Nations Steering Committee of eminent persons, reviewing corporate governance within the United Nations. He has served as Chairperson of the three King Reports on Corporate Governance in South Africa and numerous other national and international positions.

### The shift towards 'apply or explain'

King III also marked the transition from the 'comply or explain' to the '*apply* or explain' approach. This natural progression was in line with international trends at the time and sought to deal with the difficulties of a voluntary system by giving companies the opportunity to motivate their decisions (Armstrong, 2012b).Many companies, investors and even the media are either not aware of, or have not fully come to terms with the implications of this shift, a topic which will be explored in Section 4.1.

### Application to all entities

A new inclusion of King III was a statement that its principles should be considered applicable to *all* entities, including small and medium enterprises, as well as non-profit organisations. Whilst the principles of good governance should certainly be considered by any organisation, many felt that the task of applying all 76 principles of King III was simply too onerous and resource intensive for smaller enterprises (Armstrong, 2012a; Botha, 2012a; Yawitch, 2012a). Further, non-profit organisations don't report to shareholders but rather to society at large. With the stakeholder model perhaps not deeply enough embedded in King III, it becomes difficult to transfer what is essentially a set of *corporate* governance principles to *non*-corporate entities. There is a clear need for improved governance in the public sector, but some feel that existing principles and legislation should be supplemented by the latest thinking in King III, rather than making King III directly applicable to the public sector.

### A diversity of opinion on King III

> "For me, King III is vastly different from the other two as it regards in essence a change of behaviour within companies. But it's very difficult to implement. I think it has created a foundation on which we can go forward. It's unique in that when I engage with people overseas they don't have the same governance frameworks in which to see the integrated reporting – there is a reason why we are doing it. For them it's new, and they don't have that foundation on which to base that particular direction" (Terry, 2012a).

Some applaud King III for its progressive principles and the deep embedding of leadership, sustainability and ethical values. Others feel that it may have gone too far. They found it to be disconnected and felt that the chapters were written in isolation, giving rise to its complexity and density. A number of these discussions will be explored in the section on the *State of Corporate Governance in South Africa Today*.

> *"A lot of the people are saying King II was great but you've over cooked it in King III – and maybe we have?" (Payne, 2012a).*

## 3.5 The Code for Responsible Investment in South Africa (CRISA)

The development of responsible investment in South Africa is a crucial part of the corporate governance debate. Progressive principles can promote best practice in companies but will this ever really gain traction if shareholders fail to value corporate governance and sustainability performance?

John Oliphant, Head of Investments and Actuary for the Government Employees Pension Fund (the largest pension fund in Africa) and Chair of the Code for Responsible Investment in South Africa (CRISA) shared some background on the development of responsible investment in South Africa.

South Africa was the second emerging country to establish a national, investor-led United Nations Principles of Responsible Investment (UN PRI) network in May, 2009. This was in a move to progress from the UN PRI being a marketing tool, to becoming a tool for action.

Following its publication, there was a strong feeling that King III was not going to work as long as companies can voluntarily opt out of the 'apply or explain' approach. King III would not work unless the asset owners of companies become *active* owners. Companies would need active shareholders holding them to account. The UN PRI felt that there was insufficient guidance in South Africa for institutional investors on how to act as active owners of assets. The King Committee held to its 'apply or explain' principle, so a move was made to develop a code for institutional investors.

A committee was formed with the backing of the IOD and other industry bodies, with the aim of holding directors accountable. As elected Chair of CRISA, Oliphant was encouraged by how productive the committee has been to date, but was also faced with the challenge of producing what he was looking for – 'an uncompromised code' that was not driven by the various role player's agendas.

The CRISA code was launched in July 2011 and became effective on 1 February 2012. The code provides a simple but strong message regarding the

principles of responsible investing for South Africa. One important inclusion in CRISA is that investors should identify and publicly acknowledge when they are conflicted.

> "I think after we put that code through there was a greater acceptance. I also realised that it was an important principle because it encourages transparency and you don't try to hide anything under the carpet. We said 'let the system be that transparent that we can all be held accountable'. Also, the principles are all about having a policy around active ownership" (Oliphant, 2012a).

An important but challenging principle is that policy should be disclosed publicly, which stems from the code being voluntary: there are no means of holding an investor accountable if you don't know what their intentions are. Ultimately, the code doesn't describe a responsible investment policy but rather asserts that a policy on active ownership should be implemented. In this way, the "code caters for everybody in the spectrum. You need to have a policy that people are aware of and states your position" (Oliphant, 2012a).

Oliphant had been involved in commenting on the drafting of the Pension Funds Act which places strong emphasis on environmental, social and governance (ESG) issues: "There is a principle in Regulation 28, stating that trustees must apply their mind on the ESG issues. Once you start including such elements in the regulations, it creates a space for people who are smart enough to sue trustees. If that happens I think it will also raise more attention. All the trustees are scratching their heads, asking 'What does this principle mean? What should we be doing?'Now there is the CRISA code that says how you can go about it. That is the unique thing about the South African context not seen anywhere else in the world" (Oliphant, 2012a).

Oliphant further shared how this process is really only a beginning. Considerable education and training movements as well as the development of templates and support systems are underway with other industry bodies. He is looking forward to the point when "you have asset managers more actively involved and trustees more actively involved [as] then you start seeing companies being more encouraged and engaged" (Oliphant, 2012a).

# 4. A principles-based approach

## 4.1 Principles versus rules-based

The King Reports have consistently advocated a principles-based approach. The Committee share a strong commitment to this approach, which may be summarised by King (2012b) with his personal reflection on the matter: "As a lawyer of many years experience I can tell you that you can get around a rule – but it's not so easy to get around a *principle*".

### Avoiding the purely rules-based approach

Considering the route the US took with Sarbanes Oxley legislation, many shared the view that this has not stopped companies from breaking the law. By contrast, adopting a principles-based approach has stood South Africa in good stead (Andersen, 2012a). The exceptionally high cost of compliance with Sarbanes Oxley is well documented, and South African firms such as Telkom where were listed on the New York Stock Exchange gain little benefit from the cost (Nxasana, 2012a).

> "And at the end of the day I believe a rules-based approach to governance always comes short if it's not underpinned by a very sound sense of values, and that was a disconnect that I could see" (Nxasana, 2012a).

Khoza (2012b) refers to a rules-based approach as cultivating an environment which "subscribes to the survival of the sleekest". For him, a principles-based approach is dependent on moral persuasion: "You inculcate a way of looking at the world that is wholesome, where people actually govern themselves as a local control. That is a lot more effective than an imposition that is instigated by law" (Khoza, 2012b).

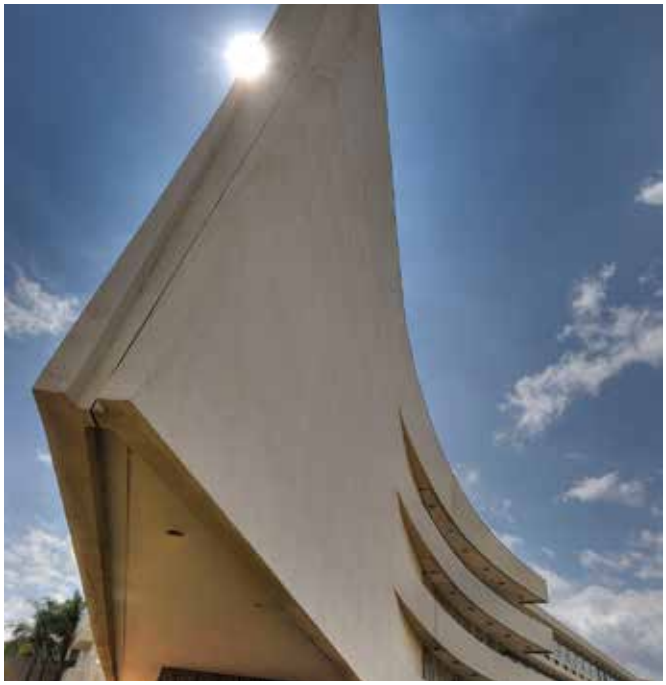
> "I've been in discussion in board meetings where directors were not able to differentiate between the Companies Act and King III, thinking that both are law. I have read examples of that in the press, such as "But, King says…" It's often referred to as the King Commission – but we are a *committee*, a broad group of intelligent people with practical experience who offer *guidance*. It's not a book, or a law. The guidance generally works. When in doubt, follow what the King Report says." (Payne, 2012a).

## The 'apply or explain' principle

A critical and often undervalued aspect of the King Reports is the 'apply or explain' approach which provides leadership with the opportunity to adapt the codes to their contexts. One key issue is that companies may consider the applicability of the codes to their own situation, with the opportunity to explain to their stakeholders why they have chosen a different approach (Adam, 2012b). This allows for a tremendously wider scope of interpretation and application compared to inflexible legislation. Such an approach is both empowering – and potentially dangerous. Botha (2012a) holds that the 'apply or explain approach' creates a loophole for companies to avoid accountability. Adams (2012a) further maintains that transparency should keep companies accountable to both their shareholders and the stakeholders. The missing ingredient is participation by both shareholders and stakeholders alike, who can hold companies to account on their decisions.

## A combination of principles and legislation

Ultimately, it was felt that a principles-based approach is best. Good behaviour will always exist without the codification of principles, but they serve as an important safety net against bad behaviour. The right combination of principles and legislation is important though to be able to enforce, where necessary, minimum standards of acceptable behaviour. Discussions of ethical leadership are included in subsequent sections, as are potential recommendations for improving the future balance of principles and enforcement.



## JSE listing requirement

The weighting behind the King Codes of Governance Principles (which remain voluntary) stems from the move by the JSE to make certain of the principles a listing requirement, as well as the incorporation of aspects of the principles into legislation over a longer period. Loubser (2012b) shared his experiences with colleagues at other exchanges, who initially found the subscription to principles amusing and then started coding principles of corporate governance in a similar fashion – to ensure that certain principles can't be side-stepped: **"**We took a decision as there were some principles so fundamental that we didn't want to give any company an opportunity to avoid them".

**Conflicts of interest for the JSE?**

Botha (2012a) raises the issue of a fundamental conflict of interests for the JSE in their position as both a securities exchange and a regulator: "On the one hand they want lots of companies to come through and list on the JSE. They therefore have a marketing exercise, putting the checks and balances in to get these companies listed. On the other hand they are a regulator. How do you actually combine the two? You need to have a split in terms of a regulation so we can have serious rules and regulations that can hold people to account, that we can reprimand them to make it public. What's the use of reprimanding somebody without stakeholders knowing that a company had deviated on certain rules and regulations?" (Botha, 2012a).

## The New Companies Act

The new Companies Act of 2008, which came into effect in April 2011, incorporated aspects of King I and King II, whilst King III was written to reflect the changes in company law. Wilkinson (2012b) states that the NCA doesn't undermine the King Reports but rather strengthens good governance by reinforcing some of the key principles through legislation. Whilst there is the concern that it may lead to a compliance mindset (that is already being expressed by some companies), Wilkinson maintains that the principles of the King Reports are far broader than the terms in the NCA.

The interplay between King III and the NCA is not without its tensions. New practice notes have recently been issued for King III in light of the publishing of the NCA and many feel a process of further refinement is required to bring the two into alignment. A more fundamental issue is the extent to which King and the NCA truly embrace a stakeholder model of governance. These problems are discussed further in Section 5.1.

### A call for smarter regulation

> "A values- and principles-based approach is still the most effective way of dealing with corporate governance as opposed to more rules. In my view the world doesn't need more regulations. I think we need more *effective* regulations – and the fewer there are, the more they are going to be remembered by those people that are supposed to comply with them" (Nxasana, 2012b).

### Looking forward

Wilkinson (2012b) maintains that a principles-based approach will always lead the way. Whilst we do see an interplay between principles and legislation, the developments in governance move at a faster pace than the revisions in legislation. Such developments drive legislation, and should continue to do so.

## 4.2 Fostering a good governance mindset

The leaders that have been interviewed agreed that a mindset of good governance was not a compliance issue. There is a need for minimum standards of ethical behaviour, which ultimately rests upon integrated thinking on strategy, risk and opportunity in an accountable and transparent manner. How then can (or should) companies move beyond a compliance mentality and return to the original intention of the King Reports: that businesses govern themselves in a wholesome manner (Khoza, 2012a).

"What you've got to do is really get the mindset right to say we're in this business for risk management, sustainability. It shouldn't be something that is imposed on us, but rather a mindset on how we are really going to manage this business" (Andersen, 2012a).

Such a change would mean shifting away from compliance departments and report writers being responsible for governance, and a move towards *ownership* of governance from a board level, through to the day-to-day running of the company. Nxasana reflects how "unless you implement [good governance] in the day-to-day means of how you do business, you are not going to really affect anyone except those people who compile those reports at the end of the year" (Nxasana, 2012a).

"The key is to make sure it's meaningful and integrated, so that the risk management process is not just imposed on the company but becomes the *essence* of the company. Only then do you gain value from it" (Andersen, 2012b).

Andersen's sentiments form part of what Gordhan (2012b) might call a change in culture, attitudes and mindsets away from compliance, in favour of redesigning what drives human behaviour and finding new ways of managing human conduct – a tall task, certainly, but an important one.

## 4.3 Leadership and ethics

> "You can provide parameters in which good behaviour is allowed to be exercised, but at the end of the day it's about whether all the checks and balances – with the added conscience factor – actually work or don't work" (Gordhan, 2012b).

Ultimately, debates on governance, stakeholder inclusivity and sustainability performance come down to a question of responsible leadership.

### Should this not just be common sense?

> "If you go through the principles it's like deconstructing a day in the life of a director. There is nothing there that they shouldn't be doing anyway. It's like teaching people how to drive: most of it I think is stuff that directors should be doing without being told. It's useful to be reminded" (Crotty, 2012a).

For those who 'just get governance', the King Codes may offer relatively little value. For some, good corporate governance remains 'good common sense' (Loubser, 2012a). There certainly are a number of outstanding corporate citizens in South Africa – leaders and companies of which we can be proud. However, the other side of the spectrum requires more attention, where the King Reports could provide a safety net for society concerning the ethical behaviour in companies.

### It's about effective and responsible leadership

> "If you don't have a good chairman, your board is going nowhere. The effectiveness of the board is about the chairman or, if you don't have an effective chairman, then about the other director who plays the chairman. That is still good enough to manage if you have someone like that. Wrong agendas, focus, not enough strategy, leadership – you end up playing corporate governance games. If you have an absent chairman, then the board has very little chance" (Payne, 2012a).

The intangibles of effective and responsible leadership appear to be the most critical element of good corporate governance. This requires leaders applying themselves and thinking more broadly than just the financial bottom line. Good governance is reflected in *how* decisions are made as much as *what* decisions are taken (Adam, 2012a). The King Reports provide guidance, but it rests with leadership to see to the application of the principles, and then allowing management to see through the implementation: "It's about qualitatively asking: *how do I make sure that what I do adds value to the company, to society and the environment in which I operate*, and then let management sort out the detail" (Adam, 2012b).

"What is important is that we as a country find a way of incorporating King III into the values and the principles of how business is normally conducted. But even then you can have a nice framed statement of values and principles on your wall. There is always the challenge of making sure that those values and principles are interpreted and implemented in any organisation" (Nxasana, 2012a).

### Perhaps even courageous leadership?

Changing the way boards think requires an enormous amount of courage. Management remains incentivised in the short term but until incentive structures are changed, can we really change the way we think about governance? Adam (2012b) speaks of the need for good leadership to be pioneering, to deal with the disincentives and the short-termism inherent in companies: "one of the critical roles of leadership is also to manage those contradictions and paradoxes – to show the path forward and stay true to that path". Yawitch (2012a) agrees that "fundamentally, what we are talking about is leadership; it is those people who are going to step forward and take the risk. A lot of this is about risk" (Yawitch, 2012a).

### An aspirational code

The King Codes of Governance Principles are, at their core, aspirational. The codes have been criticised for being too progressive and difficult to realise. Adam (2012a), however, asserts that just because something is difficult to realise does not mean that we should lower our aspirations. Khoza (2012b) shared his reflections on the aspirational nature of the King Reports:

> "Human development takes place by way of striving for something wholesome. You actually achieve a great deal, even as a corporation, by setting stretch goals. If you just got descriptive [rather than progressive] you would remain mired in mediocrity and that would not address the prerequisite developments that commercial concerns have to strive for, even in terms of setting profit goals. If we were just descriptive about what is happening now and did not set stretch profit goals, our performance would suffer. In a sense, King III had to be idealistic – most religions, belief systems and philosophies are in fact normative. You set the norm and then strive to actually realise that norm" (Khoza, 2012b).

## 5. In the context of sustainable development

A defining feature of the King Reports was the extent to which they went beyond narrow definitions of corporate governance as financial regulation in the interests of the shareholders. Rather, the Reports emphasise the value of a stakeholder-inclusive model of governance. This approach stemmed largely from South Africa's turbulent socio-political history and a growing sensitivity to the importance of social inclusivity as part of businesses' mandate and, ultimately, as the key to mutual success.

Gordhan (2012a) recognised such social aspects in saying:

> "The danger with corporate governance is that it's a set of formalities that you follow without necessarily providing a social context within which those formalities are to be exercised. They don't necessarily provide a framework of obligations which would ensure that corporations operate within an emerging market context to play an active social role" (Gordhan, 2012a).

Adam (2012a) recognises that "what King III was trying to do was elevate issues about what leadership was thinking and create that link between the responsibility of an organisation and the society that it fits in". The next major inclusion was the recognition of the limited carrying capacity of the supporting natural environment, and the extent to which both social and environmental sustainability was central to any company's long-term success. Whilst King III has attempted to express these issues through the principles, the challenge remains as to how companies are able to understand and translate sustainability into strategy and performance. Both the stakeholder-inclusive model of governance and governance which drives sustainable performance is investigated further in this section.

Godsell is aware that various aspects of King III with regards to governance remain unresolved:

> "The word *governance* is interesting actually. It's a word that comes out of politics, particularly democratic societies. Whose interests are we trying to look after? Do we understand them and do we report to them? How much veracity can we hold in the social part of a company's annual reports? Qualitatively, how well are we doing? How good are we in industrial relations? Have we been good corporate citizens in the political sense? Interesting questions all" (Godsell, 2012b).

## 5.1 Understanding the stakeholder model

> "In many respects South African executives hold an advantage compared to many executives in other parts of the world, not only because of King I, II and III but because of South Africa's unique situation. For instance, we are sensitive to gender and racial discrimination because of South Africa's past. All of that feeds into corporate governance. I've been sitting on international organisations now for 15 years where I come into a room and don't see a single woman sitting around the table, or a person of colour. The question doesn't even feature in the minds of people not from South Africa – that's the first thing that strikes me. Our hypersensitivity overlaid with a very structured approach to dealing with such matters is largely driven by the King Reports. I think that has made South African corporate governance one of the better models in the world" (Loubser, 2012a).

Several individuals shared their international experiences of boards and noted how fundamentally different the South African experience of diversity is. For example, boards appear far more attuned to stakeholder input and engagement (Terry, 2012a). Armstrong (2012a) affirmed that the importance placed on stakeholder inclusivity in the successive King Reports emerged from the recognition that both diversity across all levels of an organisation and broad consideration of all the company's relevant stakeholders is not only the businesses' responsibility to society, but an opportunity to become more attuned, informed and, ultimately, successful.

Andersen (2012a) noted that stakeholder inclusivity is not without its challenges: "The first challenge involves identifying exactly who the stakeholders are, developing policy on how they should be engaged – and how you report back. The reality is that the shareholders still own the company and they want a return on their capital, but not at *any* price". Wilkinson (2012a) echoed these sentiments and expressed the challenges in changing boards' mindsets in order to take stakeholder issues into account.

Adam (2012a) makes an important distinction between the shareholder-enlightened and stakeholder models:

> "The shareholder-enlightened model says that you engage and build relationships with stakeholders. As long as it adds value, then that's the good thing to do. But in the same vein, does it mean that you don't do it anymore when stakeholder inclusivity stops adding value? The stakeholder model says you engage with stakeholders because it is in the best interests of the company to do so. Establishing strong stakeholder relations will hold you in good stead as a company. The stakeholder model doesn't give the shareholder *de facto* precedence in that debate. On a case by case analysis you say: 'how do I take into account what all the stakeholders' legitimate expectations are and, based on this decision today, I think we do it this way'. We have statements like that in King, but if you look through [the Report] it's not obvious that this is the model being followed. In terms of an aspirational code and pushing for agreement, we've said something I don't even think the King Committee themselves have internalised" (Adam, 2012a).

An interesting point was raised on the extent to which we truly understand the implications of such a stakeholder-inclusive model. Godsell (2012a) shared an interesting view on governance in the broader context of the role of companies:

> "We are still in the rather early stages of understanding companies in democratic society and in knowledge-based economies. I don't think we've gone very far down that road. Most company law in market-based societies like the US, Europe and indeed Asia operate mainly with a shareholder model. I think we've lightly used words to describe companies having multiple stakeholders in the business of creating wealth for its owners and investors. The stakeholder model is entirely different. It's a complicated model that requires different boards with different capacities and different behaviours. I think we haven't taken on board how complicated stakeholder capitalism can be."

The role of the board is "to conceptualise the stakeholder model in a meaningful way. It would be really useful to ask each board 'Who are your stakeholders? Have you identified them and have you talked to them?' Incidentally, this is exactly what you are required to do under the New Companies Act. It's also the role of the social and ethics committee to do that. Who are the stakeholders, what are their interests and how do we balance them? I think we've [paid lip service to] the stakeholder model but we haven't internalised that model yet" (Godsell, 2012b).

### A reflection on African values

An interesting discussion on the role of African values emerged during the interviews. Some felt that African values are central to what the King Codes embodied – a sense of inclusivity and dialogue – whilst others saw it reflected through commitment in the letter, but not the spirit of the principles. Such debates may arise more from South Africa's contextual sensitivity to diversity, rather than from a deeper sense of true stakeholder engagement.

> "I haven't seen a major impact of African values but have seen an impact of values which seem to be universal. Of course, South African values are different given BEE employment equity. However, I don't think that's driven by African values but rather by the injustices of the past. We've got that dimension to manage, along with BEE, employment equity, the ratings and the CSI indices which you don't have overseas. I haven't seen a great deal of African values" (Andersen, 2012a).

Khoza (2012b) reflects that whilst the spirit of *Ubuntu* provides a point of departure as a philosophical statement and a core value system, it nevertheless requires guidance as to how this can be realised in real and meaningful ways: "Where *Ubuntu* is concerned, the core challenge is in fact inclusivity. All too often the major corporations over the years have tended to be somewhat exclusive. They tend to focus more, if you like, on just the shareholders, while forgetting about the existence of stakeholders".

Nxasana sees elements of these value systems incorporated into the broad movements that have taken root in South Africa over the past two decades: "We've been doing those things, whether they are about transformation or about economic empowerment or financial inclusion. We've been doing that in this country for many years. There are different forms of capitalism in the world. [South Africa's] own style of capitalism tries to be more inclusive, to make sure we are involved in communities, that we understand that we need to close the gap between the 'haves' and 'have nots'. It becomes very important but doesn't mean we always get it right. In this country we still have large gaps and that is an even bigger reason why companies have to be involved in sustainability" (Nxasana, 2012a). He further reflected that these values of inclusivity emerged in part due to the history of South Africa since 1994, but also to what might be broadly considered the spirit of *Ubuntu* – or the spirit of inclusion.

## 5.2 The need for sustainable development in South Africa

> "In the South African context, much of the discourse is what governments should and must do – rather than about what *corporations can do*. You can have an absolutely perfect corporate governance set of rules and practices which have an insignificant impact on society. Now, how you connect these two approaches is crucial. You want to develop a mindset in government, business and society which is able to understand the complexity of our environment, the diversity of your stakeholders, how each of the obligations plays themselves out depending on the socio-economic environment in which you find yourself. Rather than responding to push factors, we need to generate our own pull factor which would allow us not only to innovate within the spectrum of our core business but also innovate in terms of what types of contribution we can make to a country's economy or society. In the South African case there are a number of things that corporations could be doing without impacting negatively on their bottom line. I'm not saying that they don't do it, but I would like to see a lot *more* of it. Too much of it is trapped within the corporate social responsibility or CSI [Corporate Social Investment] paradigm. Given our legacy, we require more structural interventions to change the character of poverty and educational opportunities, skill opportunities and work experience in our environment" (Gordhan, 2012a).

The Minister of Finance highlighted the clear need for understanding and applying the broader principles of sustainable development and its centrality in the South African context. The King Reports have been recognised for being exceptionally progressive in their acknowledgement and incorporation of the sustainability imperative. Some of the implications (such as integrated reporting) are discussed further in Section 6.

Ultimately, if companies want to survive and thrive in the South African context, they need to address the social and environmental constraints in which they operate, linking not only to their license to operate, but also to their credibility.

## What does sustainability mean?

Whilst the National Environmental Management Act (107/1998) defines sustainable development as the "integration of social, economic and environmental factors into planning, implementation and decision making so as to ensure [that] development serves present and future generations." (South Africa 1998), the terms sustainable development and sustainability are widely interpreted. Understanding the context of sustainability for businesses needs to address both their role and impact in society going forward.

> "The critical challenge for leadership is how to build sustainable businesses, which concerns understanding your role and impact in society. We have the challenge of the environment, such as climate change issues. How do you run your business in a way that mitigates harming the environment? Unless we do that, it's going to be short term. We need that paradigm shift. The only way to do this is to have an ethical relationship with society, to think about the environment. If you want to be around in 20 years time, then the only way to do so is to build a sustainable business" (Adam, 2012b).

> "It's about the medium and long term. Is a company and society going to be around in the long term? It's about looking at resources and resource constraints – these all have an impact on a company and communities – and conserving those resources as much as we can" (Terry, 2012b)

## Where are we now?

Khoza (2012a) stated optimistically that there is plentiful evidence of good practice in South African firms, while Yawitch confirmed such pockets of excellence exhibiting a sense of increased proactivism in the market place. For the most part all agreed that we still have a long way to go: "There are outstanding corporate leaders who have taken the challenge and risks, given space and integrated sustainability issues into their core business. I think that they are generally reaping the benefits of it, but they are still pretty much at this point in a minority" (Yawitch, 2012b).

Many South African companies have traditionally operated in so-called 'dirty industries'. Today, many of the same companies are leading the way in terms of sustainability commitments and reporting to reduce their impact where ever possible (Terry, 2012a). Whilst it was felt that legislation has strongly driven sustainability compliance to date, there was a strong argument made for the need for incentives that further build the business case for a sustainable approach which is only starting to unfold in South Africa (Yawitch, 2012b). Sustainability legislation is in line with international developments, whereby sustainability is increasingly being recognised as a *core* driver of business, and a business opportunity. A number of drivers are already at play, not least of which is the energy crisis.

> "Are companies performing? It's still early days. What we certainly have is an increased flow of information. What we haven't got is an independent view on that information. Many of the sustainability numbers are not yet audited and that's because companies are still getting it down in their businesses – but that they are disclosing the information is undoubted. Now, is that changing the company's mindset? I think yes." (Andersen, 2012a).

## The challenge remains

> "The challenge for companies is to try to understand the parameters on sustainability. There are so many interest groups and issues around sustainability that companies can't possibly address all the issues. Companies have to make choices. That comes back to judgment, so the real challenge for companies is understanding what the constant themes are and how you operate, how you define your strategic imperatives. Then you have to make those choices – you simply can't accommodate every single requirement. The only worry I have on sustainability is the level to which it's been politicised in some markets such as the US, which distracts from the more fundamental benefits that good sustainability practice brings to its business, it's credibility and the way it operates" (Armstrong, 2012b).

The challenge of integrating sustainability issues into strategy and performance is central to the success of corporate governance, as has been defined by the King Reports. Building an integrated understanding of sustainability, strategy and governance board decision-making remains a struggle so long as leadership continues to outsource these as compliance issues (Adam, 2012a).

# 6. Outcomes of South Africa's corporate governance experience

South Africa's corporate governance experience can be reviewed in terms of (1) direct changes stemming from recommendations contained within the King Codes of Governance Principles and subsequent legislation; and (2) indirect shifts in performance and experiences. This section explores perspectives on both aspects and highlights the diversity of opinion on the outcomes of South Africa's corporate governance experiences.

### South Africa consistently scores well in corporate governance

Over the past twenty years, South Africa has without a doubt progressed from low levels of governance awareness to a point where today it is consistently ranked as a leader in global competiveness surveys for its good corporate governance practices. The perception of corruption is starting to undermine this reputation in recent years, but the country certainly has benefited on the whole from high standards of corporate governance. Many commented on the extent to which good governance standards assisted in attracting foreign investment to the country and helped South African companies to raise cash overseas (Andersen, 2012a).

Payne (2012a) states that an advantage in the South African environment is that whilst companies are large enough to be considered sizeable, the environment in which these companies operate is small enough to be responsive to change: "the ship is nimble enough that it will turn within a timeframe that is capable of being noticed".

South Africa, Armstrong (2012b) puts forward, has managed to achieve an admirable balance between domestic priorities and maintaining good levels of international competitiveness – a valuable lesson for other countries.

### International influence

As discussed earlier, a number of countries have referred to the King Reports as a benchmark of corporate governance principles. This level of positive exposure can further be considered an outcome of South Africa's corporate governance experience. The King Reports, for example, have directly influenced the Commonwealth Governance Principles, with members of the original King Committee playing an influential role (Wilkinson, 2012a).

## 6.1 Company performance

A question often raised is whether or not good corporate governance translates into good company *performance*. Measured in purely financial returns, the results are mixed, although many studies have shown a strong correlation between good corporate governance and financial profit. King (2012a) is a firm believer that good governance creates good business sense. Loubser (2012b) similarly asserts that there is a high correlation between "good, honest common sense corporate governance and good numbers".

### Keeping companies in check

> "King III has been very useful to me as a journalist. If you look through a company's annual report and you can say: 'hang on this isn't quite what it should be, please explain', in which case they will give you an *interesting* explanation. But you can write about [any possible discrepancies], so then the public become informed" (Crotty, 2012b).

### Costs of compliance

Some interviewees argued that the costs of compliance to King III are too great (Botha, 2012a), while others point out that there will always be costs involved with the progression of systems (Armstrong, 2012a). There is no doubt that issues of governance have taken up considerable time for all companies.

> "There is no doubt that King III in particular has cost a lot of money. There is no doubt that the winners have been the accounting, legal and the auditing professions – and there is no doubt that all of us have devoted a tremendous amount of time. This leaves us with the question: is it all worthwhile? I would answer 'Yes'" (Andersen, 2012a).

### The shift to sustainability thinking is key

Andersen (2012a) goes further to comment how good governance practices have not only benefited companies by attracting foreign investment, but have further benefited boards who have taken on issues such as safety and sustainability. He attributes these shifts in board thinking to key sustainability issues raised by the King Reports.

> "To be honest, King I was actually quite an innocuous document if you think about it, but what has it led to today? We said we wanted integrated reports. Now, 400 companies are producing integrated reports. So it has had a major impact on the disclosure of directors'

emoluments. Suddenly, the board is involved in sustainability and risk management, IT, and what the risks are in that area – so it's had a major impact" (Andersen, 2012b).

## 6.2 Board dynamics

Whilst some feel that the dynamics of boards have fundamentally changed over the past two decades towards deeper stakeholder consideration, largely owing to the codes of governance principles, others felt that this was rather a product of decent leadership that would be present (or absent) regardless of governance principles. Reflections on the changing dynamics of boards in South Africa revealed a range of experiences.

### Board attention to governance

Andersen (2012b) highlights how, in his international experience, South African boards can spend up to forty per cent more time on issues of corporate governance than other boards. He felt that this should settle down as changes from King III and the NCA gain a more settled structure. Whilst much of the boards' time may be spent on issues of compliance, there has been a broader shift in the understanding of their role.

### Changing board dynamics

There has been a perceived shift away from the predominantly 'big boss' model to a more consultative board dynamic. The shift is also in part driven by the New Companies Act and increased director liabilities, although concerns remain about the passivity of some non-executive directors (Payne, 2012a).

Andersen (2012b) shares his experiences of the changing nature of board dynamics: "Directors are far more prepared. They seek more information. The non-executive directors are playing a far more active role, probably because they realise they are carrying far more responsibility and risk. It wasn't unusual in the early days for there to be three or four so-called 'heavyweight directors'. I used to call them the 'grumpy old men' and they would call the shots, while the rest would nod wisely. But it doesn't happen like that anymore. Boards are there for everyone to contribute".

### Board independence

The question of board independence appears to be a difficult one to determine, and the guidance given by King III was felt to fall short in this respect. Independence, some felt, is not something that can be determined either by self-evaluation or by setting a time limit on board tenure. "We need external evaluations in terms of the board by totally and utterly independent people. Evaluations should be an ongoing process because whilst the board should actually self-reflect, self *evaluation* is just an internal thing saying we all look good" (Botha, 2012a).

### A growing understanding of board capabilities

Reflections by the interviewees also explored the importance of board capabilities. The first major change was that board members became sourced for their technical skills and experiences, as opposed to being part of the 'same club' (Godsell, 2012b). Increasingly, boards are starting to realise the importance of the human capital around the table: "What's the calibre of your CEO? What's the integrity of the people? What's the culture and value system of this organisation? Is it sound, healthy, and sustainable? Or is there a sickness in this organisation that we are going to have to deal with? Every organisation is about human capital" (Payne, 2012a).

### The issue of director remuneration

King II saw the introduction of a principle on the disclosure of director remuneration. Although controversial at the time and certainly a progressive move considering South Africa's lack of transparency in the past, executive pay remains a contentious issue today.

> "Executive pays is one issue that is really the kind of Achilles heel of it all. It demonstrates what the problems and complexities are" (Crotty, 2012a).

Crotty (2012a) elaborates on how the considerable remuneration packages currently being paid out are not challenged by King III – but many people, including Crotty herself –view them as fundamentally unethical. In this way, she sees King III as allowing unethical behaviour to be treated as acceptable behaviour. The principle behind the King Codes supporting the disclosure of director remuneration was the belief that the relevant stakeholders would apply the requisite pressure for the right changes in behaviour to take place. This has not happened, which further points toward issues of responsible investment. It also suggests a fundamental flaw in the system whereby short-term behaviour essentially remains incentivised.

Andersen (2012b) acknowledges that "the primary problem that went wrong in the US is (if I may be so bold) that executives, particularly bank executives, are being *rewarded for the wrong behaviour*. But the real question is: did the boards understand the risks that those banks were being exposed to, and what sort of remuneration was driving that behaviour? I'd like to think that in South Africa the boards would have been slightly more attuned. Certainly the risks should be reduced in the future as risk management becomes more important and more embedded in the company,"

In reflecting on the path the US followed, Crotty expressed the concern that "there is always incentive for massive failure. I'm not really sure why there hasn't been any – that is interesting. I don't think it necessarily goes to the integrity of the people concerned but presumably there is a systemic explanation for it. But I do think the incentive system in South Africa does lend itself to failure, if not in the short term then definitely the long term" (Crotty, 2012a).

## 6.3 Integrated reporting

***"Corporate reporting as we've been doing it for the last decade is no longer fit for purpose" (King, 2012a).***

Considerable attention was paid to the importance of integrated reporting, leading to multiple interesting discussions on its role and potential.

### Background to integrated reporting in South Africa

At a meeting of key sustainability reporting role players, held at St James Palace by Prince Charles in 2009, Mervyn King shared the realisation that came of age:

> "Corporate reporting as we've been doing it for the last decade is no longer fit for purpose. With the complexity of reporting, nine out of ten people do not understand it. What you need is concise international language so that the trustee of your pension fund can make an informed investment about your money that is invested in that company, that it's going to sustain value creation in the long return. You cannot tell that by looking at a balance sheet or profit and loss statement. In the nature of things that is historical information. You're trying to look into the future when looking at sustained value creation within the completely changed world in which we operate. Climate change, ecological overshoot and overusing the natural assets of the planet – all these things are happening around the world" (King, 2012b).

King (2012a) went on to share how embedding sustainability in long-term strategy is critical, and how it took considerable work to get full 'buy-in' on the concept of integrated reporting: "Eventually everybody agreed with him. Once the JSE buys and the IoD buys then you've got full popularity". King also looked back on how King III was the first ever set of governance principles to recommend integrated reporting, and also on how the JSE 2010/2011 won the World Federation stock exchange prize for the best stock exchange regulator in the world – after making King III a listing requirement. Later that same year King received the award of excellence from the World Federation of Exchanges, for his contribution to corporate reporting for exchanges around the world (King, 2012a).

### The potential for integrated reporting

> "I remember when we published the discussion paper on integrated reporting back in January 2011. I received several phone calls from companies saying how fantastic it is for them to tell their story. They explained how they are being tarred with the same brush of other organisations. Now they have the opportunity to tell their story and put it down in a transparent manner which differentiates them from other companies operating in the same industry" (Terry, 2012b).

Terry (2012b) reflected how "today, probably 80% or more of a company works around non-financial issues. We don't have the kinds of processes to measure that information – it's still very much in its infancy". He is excited about the potential of integrated reporting, given that so much of a company is linked to its intangible assets. For Armstrong (2012b), it's the next logical step and a critical one in breaking down a silo mentality on sustainability issues. Andersen (2012a) sees integrated reporting as an opportunity for boards to look beyond the numbers and ask critical questions, such as: "What impact are we having on society?"

> "A lot of the concepts, even the concept of sustainability, just make sense when looking at the long term rather than short term for the employees. These concepts are a huge problem for the US where you have corporate reporting. Everything is based on that. I think the concept of long term which is included in King is important for the country, but also to be able to look at

> *both* the short term and long term. Accountants are not very good at looking forward. We tend to look backwards. King is asking us to look forward. From a company's perspective, if you are focusing on the long term it changes your strategy going forward and I think that is a major implication" (Terry, 2012a).

What holds tremendous promise is when companies start to identify problem areas through their integrated reports and start to tackle them, when effective reporting drives *strategy* as opposed to just being an outcome (Terry, 2012a). Botha (2012a) sees integrated reporting as a product whereby "when a shareholder reads it he can say 'OK, this company doesn't produce profits at the expense of society and environment, but is putting back into society and environment. This is especially relevant to companies guilty of pollution; you really want to get to grips with them".

> "That does not mean that companies are not going to tell non-truths in the future. Integrated reporting could lead to that because companies are going to want to show themselves up in the best light. I think the good thing about integrated reporting is it's a lot easier for a stakeholder to get a good feel of whether the company in question is lying.

Terry reflected that the process of stating objectives, setting key performance indicators (KPIs) and reporting back on an annual basis makes it difficult for companies to "pull the wool over the eyes of the stakeholders" (Terry, 2012b).

## The state of integrated reporting in South Africa today

Integrated reporting is only entering its second cycle of publication in 2012.The learning curve has been steep as companies come to terms with what an integrated report could mean for them. Andersen (2012a) is involved with eight companies that produced integrated reports, each of which follows a different approach. Companies still need to find their feet in this new space. There is agreement that there certainly is a high level of awareness about integrated reporting, but mixed success in realising effective integrated reporting – and even less so to date on integrated thinking. When speaking to the JSE, Terry (2012a) was told that about 20 or 30 companies are producing true integrated reporting, whilst some are hardly doing anything at all other than changing the names of their existing reports.

Terry (2012b) acknowledges that companies with a track record of producing sustainability reports and the resources to invest in integrated reporting have fared better to date. For others, the journey takes a little longer. Botha (2012a) supports this sentiment and sees the development of integrated reporting as an evolution, closely linked to the development of appropriate KPIs.

Adam (2012a) cautions that companies are too quick to concentrate on form (one vs. multiple reports etc.), when they should be focusing on the core issue of integration: "What we are looking for is integration of strategy, sustainability and governance. When you do that, you create integrated performance, and only from integrated performance and thinking will there be integrated reporting" (Adam, 2012a). Yawitch (2012b) supports these sentiments by advocating substance over form. She relates the levels of resonance in a report with the extent to which companies are engaging with real sustainability issues: "Integrated report is still something that is being struggled with and how to make it work, so there is a fair amount of cobbling. Over time, as companies begin to understand what is required of them and begin to produce better quality reports, that in itself will begin to compel a different kind of thinking".

### Challenges in integrated reporting

> "In terms of integrated reporting, it's far more complex than people explain it to be. It's easy to set principles, but when you start to get into it, it becomes very difficult because there are conflicting principles. What do you put in the report and what do you leave out?"(Terry, 2012a).

Nxasana argued that integrated reporting today faces the danger of becoming ineffective as the crucial information gets lost in the detail: "They have become too large. Accounting performance, as well as all the other requirements and regulatory requirements which are now integrated in these reports, have become, in my view, too unworldly" (Nxasana, 2012b). Crotty (2012a) felt that the 'apply or explain' principle holds merit, but that it becomes pointless when these explanations are scattered around in integrated reports to the extent that too much information almost becomes no information at all. Godsell (2012b) also recognised the challenges of verifying integrated reports, and suggested that we still have a long way to go.

Payne (2012a) cautioned against a checklist approach to writing integrated reports that often results in documents over 400 pages long. Who is going to read these documents and what value do they serve? Companies are facing the difficult challenge of balancing transparency with accessibility. Payne (2012a) argued that in preparing an integrated report: "You need to be aware about the five or six things that are cooking at the moment, the detail and the rest of the stuff is on the website".

Yawitch (2012a) argued that reporting frameworks are highly complex and, in many cases, duplicate themselves. Terry (2012a) cautioned that it is going to take some time to create a framework for implementing integrated reporting. For now, some companies are applying the principles well, others less so. Those showing less success tend to adopt a tick box approach which is reflected in the reports themselves (Yawitch, 2012b). The challenge will be to navigate the integration of principles, actions, outcomes and strategy in a concise and accessible manner.

> "The real step is to be more forward-looking in our reporting and also to provide more real-time reporting, rather than waiting for a major production. We need regular reports that talk about the future, on open databases – that's where we want to go" (Andersen, 2012a).

### Towards integrated thinking

> "A lot of companies aspire to provide integrated reporting, but if you don't have integrated *thinking* it's impossible to have an integrated report. Integrated reporting is trying to show the integrated and holistic performance of a business and its impact on society" (Adam, 2012b).

Yawitch (2012a) urged companies to look beyond the report and requirements in favour of *what* is being reported and *why*. "You start with: 'How do we best run our company? What is the best form of accountability to our investors and to our shareholders? What are the codes and the principles and the ethics according to which we want to run the company and why?' Fundamentally, what one wants to do is drive behaviour within companies and then see evidence that it has been done in a particular way. If it's going to be a meaningful document then it must be owned by the decision-makers in the company. It is not about the actual document, but rather the actual process".

## 6.4 Responsible investment

> "King I came out in 1994 and would have been enough if the shareholders on the other side of the equation had been engaged. King II and III seem like desperate attempts to get more attention from the shareholders. They are paying as little attention to King II and III as they did to King I. Can you imagine what we are going to do with King IV? How big is that going to be? The lack of shareholder engagement seriously undermines the point of it" (Crotty, 2012b).

Responsible investment emerged as a key point of discussion. Many interviewees shared the sentiment that without an active interest from investors, governance would remain fraught with challenges of compliance as opposed to innovation. The questions on environmental, social and governance (ESG) issues are simply not being asked by the investor community. Ultimately, without interest from the investors, there is little to hold companies to account for performing on key ESG issues (Armstrong, 2012a).

### Background to the development of responsible investment in South Africa

Oliphant (2012b) noted how the discourse on responsible investment has evolved considerably from the concept of socially responsible investing to broader sustainability issues and long-term investments. The launch of the UN PRI in 2006 anchored much of the recent thinking on responsible investment. With the

launch of the Code for Responsible Investing in South Africa (CRISA) in 2011, responsible investment has started to become far more practical in South Africa. CRISA aims to provide institutional investors with guidance on what they need to do in order to ensure that they become active owners of capital and owners of companies.

The challenge of King III is that it assumes that South African investors are active. Oliphant sees CRISA as a complement to King III's 'apply or explain' approach: "you obviously need an active shareholder base to ensure they engage with entities they invest in. CRISA provides a framework for some investors to be able to engage with entities. It's got requirements, a policy on active ownership. They need to expose that policy to the public and I think in the coming years we will see active shareholders actually tabling special resolutions at AGMs" (Oliphant, 2012b).

Terry (2012a) placed strong hope in CRISA for bringing investors to the table to start engaging on sustainability issues. They need to start interrogating company boards on the risks involved in not having a sustainable business: "the consequences of not following this route are detrimental".

## Essentially it's about risk and sustainability

Oliphant sees responsible investment as 'big picture thinking', referring to the recent BP oil spill saga of 2010 "that had a big impact on the environment, but also a big impact on the share price of BP, which in turn had a big impact on the savings of people and their pension funds. What we are saying is that all these things that are considered to be soft issues are actually systematic risks for pension funds. As investors we believe that we should engage more to ensure that our long-term investments are sustainable" (Oliphant, 2012b). Payne supported this thinking and sees the trends in boards recognising the massive interplay between sustainability and risk, but is yet to see institutional investors step up to the same level of thinking on sustainability beyond a 'no-harm' policy (Payne, 2012a).

Photos: Theo Botha (left), Reuel Khoza (right)

## State of responsible investing today

Whilst the recently launched CRISA adds momentum to the cause of responsible investment, many felt that there was still considerable work to be done in raising awareness and action from the investment community. Those who were directors of companies had sat through countless meetings with analysts, and were yet to be asked a question on governance or other ESG issues. The focus is still on good numbers, and whilst they felt that this would start to change with time it seems to be moving too slowly (Loubser, 2012b). Minor pressures are being felt on the remuneration side, but to a much lesser degree on issues of sustainability (Andersen, 2012a).

The history of South Africa's corporate and investment sectors has a role to play in the state of responsible investment today. The major investment companies held disproportionately large shares within South African business. Issues were discussed behind closed doors, which resulted in transparency and activism taking a back seat. Essentially, considerable conflicts of interest arose and will continue to arise as investors choose not to engage with companies on sensitive issues, given that many of the companies are also potential clients (Crotty, 2012a).

> "Because institutional shareholders in South Africa have such a powerful position as a shareholder block, I think there are huge conflicts of interest in terms of holding executives to account and in a public forum. We get told constantly that they are engaging with the board behind closed doors. They say they attend meetings either in person or by proxy – but then vote 99% in support of everything". [*It undermines integrated reporting?*] "We are absolutely no further ahead. The CRISA tries desperately to push us further ahead, which was only launched in the last 12 months – but already it's looking like it may not succeed because the signatories to the code are not doing the critical thing, which is to disclose how they voted on their websites" (Crotty, 2012b).

Nxasana (2012a) shared his experiences of investor interest for governance issues in the banking sector: "I think investors certainly put a value to it but even more so in the banks. What does the bank sell? The bank sells *confidence* to you as a depositor. Confidence is strongly linked to what the company does, not just in terms of profit generation but in terms of how it is perceived in society, the role that it plays in society and therefore the reputation that it carries. So investors in banking particularly do put a lot of value in principles and in those things that are not measurable. Certainly it is very important to them" (Nxasana, 2012a).

> "I think we are in a space where we are all still trying to find our feet, where we all have various opinions on various issues. That's when the engagement part of it becomes important. If you feel strongly about it you should be able to engage with management about it. Going forward, I see in the long term there will be ways in which we can report better in a more standardised way – where everyone understands the information" (Oliphant, 2012b).

### The challenges for responsible investment

Many felt that the challenge of realising an active interest in responsible investment was ultimately the challenge for corporate governance.

> "King III is a good code, but it is just not guaranteeing the implementation of what's in there because you don't have shareholder engagement. It's such a bland statement –it's supposed to give comfort and it doesn't" (Crotty, 2012b).

Companies are producing extensive reports, but investors are not paying sufficient attention to them. Asset managers do not consider the reports, as clients have not started to ask for responsible investing (Oliphant, 2012a). Responsible investing should address society at large, which has a greater role to play. Armstrong asks whether it is all just about the money – or are there certain principles at play in how the money is invested? Until the manner in which analysts are rewarded for their investment making decisions changes, there may remain little incentive to fundamentally change the nature of the investment sector. Such changes call for new systems of incentivisation.

### Moving forward

CRISA has potential for changing the current landscape of governance and sustainability in South Africa. Crotty (2012b) sees potential for directing more responsibility on the shareholders to ensure that company directors are doing their duty. She also recognises the untapped opportunity for trade unions to use CRISA to, amongst other things, force fund managers to vote on remuneration. This will start sending strong messages and create pushback where currently there is none. Coupled with activism by the Government Employee Pension Fund, trade unions would have a much stronger voice within the corporate community "so they don't have to march and throw stones. They can just attend AGMs" (Crotty, 2012b).

Oliphant (2012b) placed strong emphasis on the need for collaboration across the private and public sectors. Whilst engaging with companies behind closed doors has its place, he sees publicly available information as an important measure not only for transparency, but also to drive changes in behaviour. Getting asset owners actively engaging on issues of responsible investment is going to be key. The industry bodies behind CRISA have ambitious plans to initiate the types of awareness raising required to get asset owners actively engaged.

Gordhan (2012a) asserted that the debate needs to begin in the investment community whereby actions aren't driven by codes but rather by awareness of one's environment, and the fact that both commercial and social returns are possible. Such measures require addressing the prevalent scepticism in the South African investment sectors around the (often politicised) issue of sustainability. Furthermore, he finds that "there is too much finger-pointing going on in South Africa, which is not helpful in creating an environment for better recognition of some of these imperatives and generating the right kind of momentum in order to make sustainability the dominant way of thinking".

## 6.5 Public sector governance

Whilst not an intrinsic focus area of the research, discussions on governance in the public sector also emerged with specific reference to the impact on corporate governance.

### Governance in the public sector

The first King Report was intended to be applicable to state-owned entities. However, few such organisations adopted King at the time, given the state of flux in the country at the time. Nelson Mandela raised these concerns and following the successful launch of King I, a commission was established that published a protocol on governance for state-owned enterprises largely based on King I. Following the protocol the Public Finance Management Act was issued for Government entities, reflecting the Government's commitment to governance principles, but the challenge of implementation remains (Wilkinson, 2012a).

### Corruption undermining corporate performance

> "South Africa has a real challenge with corruption and that's where credibility issues are coming in. In terms of King III, how can you have such an advanced comprehensive code in a market

environment that is increasingly seen as corrupt? South Africa is a small economy by international standards and the Government is a huge sector of the South African economy – both as a major customer and supplier. You can't but help work with Government if you want to be in business and there is a real concern around the fact of governance. Can you really apply good corporate governance principles in an environment which is largely perceived to be corrupt" (Armstrong, 2012a).

Payne (2012a) echoed these sentiments and felt there was little point in discussing corporate governance without addressing corruption in the public sector: "I don't think you can apply King III to the state environment until you go and fix the ethical leadership, the human capital aspects. The state environment needs real leadership. Corporate governance in South Africa has become extremely difficult where corruption has become institutionalised and boards only have one choice: not doing anything dishonest. Bribery, corruption and anti-competitive behaviour are absolutely unacceptable and must not be practiced. You are going to have to accept that you might not be able to do business with the state. Well, so be it." (Payne, 2012b).However, Yawitch points to the fact that businesses have a role to play in engaging on corruption issues, and that part of the problem is reinforced by businesses "trying to accommodate everybody and being too diplomatic, or not courageous enough to stand up and raise the real problems and what they should do about them" (Yawitch, 2012a).

## 7. The state of corporate governance in South Africa today

Minister of Finance, Pravin Gordhan, reflected on South Africa's progress over the past two decades: South Africa's financial systems, audit practices and legal faculties are in good shape and rank exceptionally well internationally. Contributing to this progress is the codification of transparency, accountability, responsibility and stakeholder awareness. He felt that it was beneficial to the business sector as a whole to follow evolving standards that aim to keep in touch with unfolding realities, domestically and internationally.

While South Africa's financial and legal systems are held in high regard, we ought to further explore the state of corporate governance in South Africa by reflecting on the robustness of the principles, and the extent to which such principles are working to inculcate practices of good corporate governance in South African companies. An interesting diversity of opinions emerged on the state of corporate governance in South Africa today.

### An international benchmark

There was strong agreement that the principles as embodied by the King Reports are consistently progressive and have become an international benchmark for principles of good corporate governance. Armstrong (2012b) recognises that South Africa is certainly the leader by emerging market standards with regards to both how key governance issues have been conceptualised, as well as for the broad perspectives it has adopted. South Africa's governance standards have without a doubt become a point of reference for developing and advanced markets alike. Andersen (2012a) attributes this to the seriousness of corporate governance as well as the courage South Africa displayed in taking the lead. Armstrong (2012b) further attributes international interest in the King Reports to the detailed guidance and supplementary support it provides, in supporting the codified principles, and promoting motivation and integration of sustainability aspects as central to good governance.

What can be acknowledged is the 'creative pioneering thinking' that the King Reports set through the aspirational codes – a path towards where we should be (Adam, 2012b). Godsell supports the notion that the evolution of thinking in South Africa has been exceptional:

> "With regard to King I to III, South Africa was leading – or amongst the leaders – in re-thinking the role of company boards in defining the different roles of non-executive directors and executive management, and thinking about the stakeholder. The words and ideas are very good but applying those concepts meaningfully is going to take new boards with new capacities and new disciplines. I think we are in a rather early stage of talking the talk, and walking the vision" (Godsell, 2012b).

## Good principles, but what about the practice?

Owing in large part to the King Reports, there is certainly a high level of awareness of governance in South Africa. Andersen (2012a) put forward that "particularly from 1994, we've certainly as a country embraced the concept of corporate governance – good corporate governance – a lot more than what we see in other countries". Furthermore, according to the Global Competitiveness Surveys, South Africa ranks consistently well for its performance in corporate governance-related areas. Adam (2012b) acknowledges this, but also points out that:

> "When it comes to implementation I don't know if it matches the level of our thinking. I think it lags. There are pockets of excellence and some examples of companies that are doing superbly. Generally I don't think we are there yet, though I am encouraged. People are aware, and they are starting to think about these issues and grapple with these issues. Most importantly, the leadership is becoming aware of them. What we need to try and do is move away from the tick box approach to governance and really internalise what it means to lead in today's environment" (Adam, 2012b).

Building on South Africa's good principles and conducive environment for exploring the role of business in society, it certainly appears that South Africans are open to talking about good governance. Several thought leaders shared the perspective that there is still considerable work to be done in internalising and expressing these principles in practice.

> Where are the gaps in governance? "Well I think the biggest area is the question of ethics. King III has tried to do that, focusing governance on ethics. Unfortunately, as in this country and many others, ethics is more often applied in the letter rather than the spirit" (Wilkinson, 2012b).

## Governance has become too complex

While there was general agreement that the principles are world class, some felt that the Commission had in fact gone too far. "Messy and confusing" were the terms used by Crotty (2012a) to describe the state of corporate governance in South Africa today. She felt that with all the information out there, the reality has become buried in the detail. Whilst Crotty acknowledges significant changes over the past two decades, she questions whether this is really progress or merely a process of densification. Wilkinson (2012b) refers to the difference between King I and King III as a Volkswagen versus a Mercedes – and perhaps both have different benefits and limitations.

Botha (2012b) was adamant that the move from King II to King III has left companies in a position where they now need to comprehend 76 principles – a task that has become onerous and, in many cases, outsourced to audit firms at significant cost to the company. This, he felt, is what has resulted in the tick box mentality approach to governance. Yawitch (2012a) agreed that whilst many had adopted the tick box compliance approach, the core question was not whether companies were only adhering to rules and regulations, but rather if they understood the value that corporate governance added.

## Crowding out the key issues

These sentiments were echoed by Payne (2012b), who raised concerns that boards today may be spending too much time on governance compliance (also partly due to the New Companies Act), and not enough time on critical issues such as strategy and risk management. Directors have become overly cautious in complying with all relevant regulations instead of focusing on a few critical principles. This would mean that "you've probably done 80% of your job" (Payne, 2012b).

## If you are ticking the boxes, you do not understand the principles…

Some critics felt that the confusion and compliance mindsets stemmed from the length and detail of the codes themselves. Others were strongly of the opinion that companies which had fallen into a tick box mindset do not understand the primary intention of the principles.

> "I think the problem is many people haven't read any of the principles and they've heard rumours and they stand on those rumours. If you read King III, particularly the introductory chapter and then read the Companies Act, you will see these are two completely different things. The Companies Act is the law, or the what. King III is the how to – and the starting point of how to are the principles" (Payne, 2012b).

> "Those people are not applying themselves to the best interests of their company with regards to the best process for a particular issue. They are perfectly entitled to adopt another process, but they must explain it. As I've said time and time

again, the ultimate test of compliance of South Africa lies in your stakeholders. As a director of a company, they may well tell you that you are not justified in that process. They may well question your judgment, or no longer support your company – as a customer or as a provider of capital. The King reports were not and never will be intended to be a rule-based document. This is principle based." (King, 2012b)."

## It's about effective leadership

"Corporate governance is not just a compliance issue. It very much rests on how you identify the standards and principles and practices required for your day-to-day operations. Governance should just be part of your business process. It shouldn't be something that you do just because it is required to be done – but there should be some business sense in following those principles, as a part of your corporate DNA" (Armstrong, 2012b).

Adam (2012a) supports these positions and affirms that so long as compliance is outsourced to departments within an organisation, boards will fail to fundamentally internalise and apply the principles in their strategy and performance. This process of compliance also needs to be reported more clearly to stakeholders, which is one area of improvement for many companies.

"The bottom line of King is that it asks you to apply yourself in leadership, think broader than the financial bottom line. How you do it and adapt it to your own business is a leadership choice, but be transparent about the choices you make. Be courageous about your choices, and if you believe you don't want to apply King in certain aspects, it's absolutely fine" (Adam, 2012b).

Nxasana (2012b) suggested the need for a refinement of the codes in order to more clearly articulate the key principles that should be required of any business. He raises the concern that if companies fail to embrace the fundamentals "of a more sustainable environment and society – I think we might just lose the game in terms of what we are trying to do, which is to improve the level of accountability, not just to shareholders but to product stakeholders" (Nxasana, 2012b).

## Principles that are too progressive?

A concern raised by Armstrong (2012a) is that South African companies may in fact be bearing the brunt of a set of principles that are part of an advanced code with high expectations. South African companies are expected to realise high standards of corporate governance. In this respect, it may have been a bridge too far. Instead, Armstrong argues we need to focus on what is not working – and fix it.

## No value without investor interest and action

South Africa's understanding of corporate governance is advanced. However, an increasing concern is that companies are insufficiently pressured to adhere to the principles in a significant way (beyond those companies which are active internationally). What remains is an issue of compliance rather than one of a substantive commitment, owing in part to a lack of investor interest.

## Are there sufficient minimum standards?

Gordhan raised an important question regarding whether the progress and evolution of corporate governance to date is "sufficient in order to inhibit the worst of human behaviour, the greed, stealth factor, the tendency to take advantage of lapses within systems. At the end of the day it's only practice which tells us whether we are moving in the right direction. There are a few areas, such as remuneration practices, the power of audit committees, and internal and external auditors which will be ongoing areas of... let's call it creative tension" (Gordhan, 2012b). Similar sentiments were echoed by other interviewees.

*"The question I ask myself with corporate governance: Are the good getting better? The answer is yes. Are the bad getting better? Possibly" (Andersen, 2012a).*

# 8. Corporate governance going forward

## 8.1 Recommendations

Some interesting recommendations emerged, giving shape to perspectives on how corporate governance in South Africa could continue to develop.

### A call for simplification

> "If I have no more than five things to remember I am likely to remember them. You have to keep it simple and understandable to a lot of people. People must live by corporate governance principles as directed by their leaders, and adopt them within their companies" (Nxasana, 2012a).

Botha (2012a) shared his sentiments on the need for simplification of the corporate governance principles. He felt these could be distilled into four primary values of fairness, accountability, awareness and transparency which should inform a further 18 main principles and perhaps 20 supporting principles. Simplicity, he felt, would make their application more effective: "At the end of the day the board of directors should be able to look at the principles and say 'I can sign off on those principles'".

Godsell felt that we have the right amount of governance, but the key message is that we are on a journey: "At the early stage of a journey we need the right aspirations but the right behaviours as well. So we're very much in the aspirational state, the vision state. Most corporate governance codes, including King III, are aspirational. We've got to close the gap between how we want to behave and how we do behave. I think closing that gap is the next phase" (Godsell, 2012b).

### Getting the existing frameworks to work

Armstrong (2012a) believed that the real challenge is not in creating more principles and rules, but rather in getting the existing frameworks to work. This means moving away from more regulation in favour of a wider engagement of dialogue across all sectors that investigates what isn't working – and how to make it work. Botha (2012b) supported this notion and calls for research with the companies themselves to find out what changes need to be made.

### Further King Reports?

The interviewees displayed a diversity of opinion on whether further King Reports are warranted. While all agreed that the evolution of corporate governance was a journey, some felt that the focus should be on getting the existing codes to work better before revising and introducing new codes. The King Committee would play a central role with such modifications, but the focus should first be on strengthening the implementation of existing frameworks (Armstrong, 2012a). Others called for King IV in light of the disconnect between King III and the New Companies Act, although subsequent practice statements have been issued by the King Committee to address some of these issues (King, 2012a).

> "Personally I don't believe that you will reach your destination. It is an evolving journey. I believe we have been able to articulate what is essential for corporate governance in theory, principle and practice and we've gone somewhere. But the only way that you actually stay on your feet is visiting and revisiting that which you have been able to achieve, refining and fine-tuning forever. It's a pursuit of excellence that never really ends. So whether you call it King IV or rename it as a process, it has to continue as an evolving process of refinement and improvement" (Khoza, 2012a).

### Ongoing director education

Ultimately, the responsibility lies with the boards to understand, internalise and apply what corporate governance means to their company (Payne, 2012a). Such a task requires understanding a range of issues, beyond a director's duties as a compliance issue, to appreciate and make wise decisions on aspects like employee safety and environmental stewardship. The Institute of Directors in Southern Africa (IoDSA) offers extensive training programmes and these were felt to be important for ongoing director education.

Photos: Bobby Godsell (left), Philip Armstrong (right)

## Transparency: Clearly explain where you apply or don't

Crotty (2012a) called for a clear and transparent summary on the first page of any annual or integrated report to simply state where the company has applied King III and include explanations where they have not done so. King (2012a) supports this approach and is working to have companies undertake a register to clearly stipulate where they apply the code and explain where not. He referred to King III, where the ultimate compliance officer is not an internal individual – but rather the stakeholders – who should determine whether the adopted processes are justified or not. Stakeholder compliance ultimately relies on an active citizenry.

> "Transparency is critical. Engagement is critical, as is understanding reputational risk" (Botha, 2012a).

## Real shareholder activism

Many felt that corporate governance should be driven more actively by the investor side. Good companies will continue to implement good corporate governance, and investor activism should raise the standard of expectation for those companies that don't. Real shareholder activism calls for public transparency, the effective implementation of the CRISA code and much broader engagement beyond the handful of shareholder activists currently campaigning for more responsible leadership.

> "The processes shouldn't be Theo Botha [i.e driven by individuals]; the processes should be the PIC and Government employers' pension fund. They are the biggest investors on the JSE. They need to accept what their responsibility is – and they need to drive that process." (Botha, 2012a).

Some specific recommendations also emerged, including that disclosure of voting results, as contained in CRISA, should be legislated such that every fund manager reveals their vote within 24 hours of an AGM. Even if they work through proxies, fund managers need to be held accountable to their beneficiaries and display a clear commitment to engagement (Crotty, 2012a). Companies should also publicly disclose the number of votes with which a resolution was passed as opposed to the current practice of merely declaring that resolutions were passed 'with the required majority'. This kind of practice will help reveal when there is no clear engagement on an issue (as with cases of a 99% majority) and also show when an issue was contentious for the shareholders (Crotty, 2012a).

Oliphant (2012a) called for greater education, training and awareness around responsible investment in South Africa, especially when considering the critical role of the media to the CRISA code's survival.

## Broader dialogues

> "We don't have enough debate. The only time we have debate is when I attend an AGM and I raise the issues in the public domain" (Botha, 2012a).

Regulation, Armstrong (2012b) argued, can only play a role to a certain point. Once the frameworks and structures are in place there will always be an ongoing process of modification, but taking corporate governance to the next level will require much broader engagement, beyond regulation. There are a number of critical role players in this discussion, beyond the companies themselves, and these need to be brought into the conversation. Role players include the institutional investors, pension funds and the media – as well as the regulators themselves. Many aspects of the market remain that still need to be addressed.

## Linking strategy to opportunity

Terry (2012a) identified the changing dynamic of strategy in the context of sustainability challenges and opportunities going forward: "The key thing is to actually understand what is happening and to adapt strategy to take that into account. Companies must look long term as well; if you are looking long term your strategy can be vastly different because you want to be around here in twenty or thirty years' time. The environmental and social issues are going to become more and more important as we go into the future. So you need to be aware of what those impacts are, and be aware of what those drivers are that dictate these impacts". The challenge remains for companies to internalise sustainability issues and inform strategy accordingly. King III provides a starting point for addressing these issues by pushing companies in the direction of integrated reporting. The intensifying drivers around social and environmental issues in years to come will certainly provide a further push.

## Incentivising the right behaviour

Gordhan (2012a) recognised that codes such as King III and CRISA have an important role to play in identifying aspirational value sets, but that translating such values into behaviour is quite another matter.

"There are many more complex drivers which determine consumerism and patterns of saving and the short-termism that we are talking about. Sometimes such drivers can't be resolved within a country but require a global solution. On the other hand, some Scandinavian countries display a different kind of balance, where social obligation is an important part of what they do. Such societies show better balancing acts between the space of the self and the individual on the one hand, and the common good of the society on the other hand. The balance should be tilted towards the common good and more ethical behaviour, both of which need to become stronger and further institutionalised. You need a system of incentives and disincentives, rewards and penalties, which reinforce the right kind of behaviour, but if you look at our media for example there is a serious lack of awareness around these issues. There is probably one writer who raises these issues" (Gordhan, 2012a).

**Levelling the playing fields?**

"What we actually need is a bit of a hybrid, more on 'apply and explain' but in some ways we need incentives". Adam shared a reflection on the customer and citizen in each of us. He says "all of us want good for the world and don't want child labour and abuse of human rights – that's the citizen in you. At the same time you are the customer, who will always beat the citizen in you. Basically what the theory says is that until you get to level the playing field in some way, or you get some minimum level of regulation you are not going to beat the cycle of the customer." (Adam, 2012a).

"What we need to do is to ask: what does society recognise and reward? If we recognise good people more, if we reward values-based conduct more, then more people will move in that direction. If, however, we look at numbers and very narrow bottom lines and celebrate those through the media and other mechanisms exclusive of the values element, then we provide incentives for the wrong kind of behaviour" (Gordhan, 2012b).

Gordhan (2012a) further sees the opportunity for the role that universities can play: "It's a discourse that I think our universities can play a bigger role in positively influencing our students while they don't have any serious commitments to BMWs and houses. As a former activist, I see a lot of scope for taking these excellent ideas, giving them social currency and making them part of social activism in some form". Gordhan is calling for a new type of social activism around values and ethical behaviour.

## Redefining measures of success

A discussion on values cannot take place without questioning our measures of success. This issue relates directly to concerns around executive pay, for example, but also to the deeper question of the role of business in society. Godsell shares a valuable perspective on the meaning of wealth:

"I do think that modern societies – and these are a product of industrial and post-industrial societies – have misunderstood the word wealth which is quite interesting because it's an old English word[1]. To me, to create wealth in the world you need to work with the world's resources in a way that makes them more useful. Employment for me seems to be as fundamental a part in creating wealth, as does producing products" (Godsell, 2012a).

The King Codes of Governance Principles may be interpreted as a radical re-imagining of how we define our measures of success: "My favourite phrase in King is where they talk about 'organisations should find commercial success in terms of positive lasting benefits for the company, society, and the environment" (Adam, 2012a).

[1]Denoting the conditions of general well-being, rather than monetary wealth

## 8.2 A vision for the future

We asked a few of the thought leaders what their vision might be for a South Africa in 2030, and what would need to change between now and then in order for such a vision to be realised. We asked for radical and honest reflections. What emerged was a call to address the crisis of capitalism that appears to have taken hold both in South Africa and globally. The reality of South Africa's inequality coupled with limits to growth was apparent, but presented an opportunity for defining a new role for business in society. What resonated strongly was a sense of hope, laid on the foundations of South Africa's optimism, given the strength that can be gained from diversity and adversity.

> "What is it about the structure of the markets, or the philosophy that informs the markets, or that which informs the business sector which doesn't allow them to overcome the limitations which actually caused the severe crisis all around the world? That's what you need to change. In as much as everyone else is required to change, there is certainly a case for transformation in this area. If you go back to the G20 concept of sustainability, balance, growth – there is a critique of that in short-termism, in the way in which the financial sector grew disconnected from the real economy. […] So looking back from 2030, corporations have a senior executive very close to the status of a CFO who is responsible for what we call in today's terms social responsibility. Secondly, there would be a codified part of any business strategy which incorporates any assessment of social impact as well as a 10-year plan in terms of intended and committed actions taken by a corporation, whether it's to the environment, social upliftment or to the key priorities of society at that time. These remain issues of competitiveness, innovation, opportunities for young people and so on" (Gordhan, 2012a).

> "Communities are going to get much more involved. When you are looking at resources and what is likely to happen I guess South Africa is in an interesting position because we have a lot of poor people in this country and a lot of people expecting the new Government to have progressed further than they have. We've got all of those questions, so it's perhaps more pronounced here than in Europe or the US. As the population increases globally, resources are not increasing at the same rate, or not at all. In more instances we are actually running out of things. As a result of that, you are going to value those resources to a greater extent. Communities naturally are going to get more involved and you are going to see more legislation. As a result of that, companies are going to have greater obligations not only to their owners but to society. We've got huge poverty problems in this country and unless we address those adequately we are going to have political problems" (Terry, 2012a).

> "This notion of moving towards the long-term essence of Africa and what it takes to get there is a very important topic. South Africa is a very short-term society. We've got a frontier kind of culture. We are all living for the moment and sort of either in the depth of despair or heights of delight. We are very up and down. We need to become a little bit more of an even country that enables you to move forward with this sort of unbelievable level of emotion that surrounds everything that we do. We need change and people who are going to come in and show us how to think about it differently. We need examples and push" (Yawitch, 2012a).

> "Everything starts small. If you read the Forward to Let Africa Lead written by Nelson Mandela, he mentions that things begin with small ideas. The idea of Ubuntu might appear to be small but it is ultimately a big idea, one which may yet lead to a worldview that ultimately triumphs. Because its primary thrust is inclusivity, when all is done and dusted Ubuntu effectively means 'I am because you are, you are because we are'. We have no independent existence. Ultimately, we are an social species. If you talk about inclusivity in a corporation like this and you are inclusive of every segment of this establishment, you have a greater chance of generating the requisite synergies and co-operative behaviours that actually lead to greater achievements. If you look at it from that vantage point, clearly the concept of Ubuntu cannot be neglected. You might say that the African interpretation as I try to advocate is just one interpretation, but the idea of a human-based approach to co-habitation, co-operation and co-existence is in fact the main thing. Exclusivity was what made Apartheid as vicious as it was, more so than it was politics of oppression. Apartheid was more about the economics of exclusion. Now, African humanism or Ubuntu is about inclusivity." (Khoza, 2012a).

**The potential for African humanism**

"Inclusivity is a key principle in Ubuntu. With inclusivity you have wholesome values such as integrity, honesty, humility, humanity and, very importantly, also probity. Inclusivity involves behaving in a way that evidences integrity, essentially in a manner that is beyond reproach. That might sound idealistic but I believe that it is by way of asserting the ideal that humanity continues to strive to improve" (Khoza, 2012b).

Khoza (2012a) has written extensively on African leadership and is himself an exemplary leader. He shared his perspectives on the potential for African humanism going forward:

"Everything starts small. If you read the Forward to Let Africa Lead written by Nelson Mandela, he mentions that things begin with small ideas. The idea of Ubuntu might appear to be small but it is ultimately a big idea, one which may yet lead to a worldview that ultimately triumphs. Because its primary thrust is inclusivity, when all is done and dusted Ubuntu effectively means 'I am because you are, you are because we are'. We have no independent existence. Ultimately, we are a social species. If you talk about inclusivity in a corporation like this and you are inclusive of every segment of this establishment, you have a greater chance of generating the requisite synergies and co-operational behaviours that actually lead to greater achievements. If you look at it from that vantage point, clearly the concept of Ubuntu cannot be neglected. You might say that the African interpretation as I try to advocate is just one interpretation, but the idea of a human-based approach to co-habitation, co-operation and co-existence is in fact the main thing. Exclusivity was what made Apartheid as vicious as it was, not so much that it was politics of oppression. Apartheid was more about the economics of exclusion. Now, African humanism or Ubuntu is about inclusivity. It's about integrity and being honest. But that's not quite adequate – it is about behaving in a manner that is beyond reproach and to be seen behaving in that manner. You can say this is idealistic, based on philosophies that are not descriptive. You have to set an ideal and actually reach out to people who are advocating that ideal. Hence, Ubuntu is actually a somewhat idealistic philosophy, and Ubuntu actually says this is a set of values. Let's strive for them. You want a situation that is wholesome, ethical –that says 'that is the good life and that is how I structurally define it'. The good life is that which is wholesome and worthy of being striven for in human co-existence" (Khoza, 2012a).

## 9. Conclusion

### An ever-evolving journey

> "I think we are at the leading edge. But we can't be complacent because corporate governance continually evolves. Sometimes it's not always proactive, it's reactive too" (Andersen, 2012a).

Corporate governance, Armstrong (2012a) reflected, should never be considered a regulatory instrument. Corporate governance should provide an incorporating framework and practical guidance for managing the expectations that society and shareholders have of a board of directors to properly discharge the responsibilities required by law. He fears that governance may have evolved into a range of expectations that have become impractical. This may be the challenge facing South Africa.

At the same time, Gordhan (2012a) called for imaginative leadership in the corporate sector, coupled with selective cohesion and will: "Corporations must also have leaders who can spell out a responsible social philosophy, who can persuade people to actually change the paradigms in which they work, who can show in practical terms what concrete things can be done to change and make a difference in one's social environment. There are many individuals that I know in the business sector who provide excellent leadership in the spectrum of different kinds of projects. The question one marvels at is 'What if one institutionalised that in some form'? What if that could be synergised to the point that you reach scale in the spectrum of some of those interventions? The benefits are unimaginable".

> "Good governance is essentially about good leadership, effective and responsible leadership. Responsible leadership is based on an ethical foundation and realising the ethical relationship that you have with society – and your impact on society (Adam, 2012b).

What lessons can be learned from the South African experience? Whilst the principles have been exceptionally progressive and certainly set South Africa as an international benchmark, the development of corporate governance should be viewed as an evolving journey with continuous scope for improvement. Perhaps a greater focus area for now should be for companies to internalise and apply these governance principles into strategy, process and reporting. An aspirational code such as the King Codes will always mean room for improvement, but the gap needs to be closed. It's up to companies, in an 'apply or explain' approach, to realise these improvements. Drivers of resource scarcity and growing stakeholder activism may well drive companies to re-evaluate the role of business in society, perhaps even more deeply than proposed by the King Reports.

*"Society has a very important role to play. What values and behaviours do you recognise and applaud and what is it that you condemn?" (Gordhan, 2012b).*

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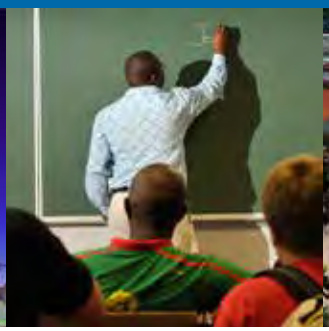
9. Crotty, A. 2012a. Verbal communication with the author on 25 May. Sandton. (Digital voice recording and transcription in possession of author).
10. Crotty, A. 2012b. Verbal communication with Bruce Whitfield on 25 May. Sandton. (Digital video recording and transcription in possession of author).
11. Godsell, R. M. 2012a. Verbal communication with the author on 4 April. Sandton. (Digital voice recording and transcription in possession of author).

12. Godsell, R. M. 2012b. Verbal communication with Bruce Whitfield on 4 April. Sandton. (Digital video recording and transcription in possession of author).
13. Gordhan, P. 2012a. Verbal communication with the author on 19 March. Pretoria. (Digital voice recording and transcription in possession of author).
14. Gordhan, P. 2012b. Verbal communication with Bruce Whitfield on 19 March. Sandton. (Digital video recording and transcription in possession of author).
15. Khoza, R. 2012a. Verbal communication with the author on 2 May. Sandton. (Digital voice recording and transcription in possession of author).
16. Khoza, R. 2012b. Verbal communication with Bruce Whitfield on 2 May. Sandton. (Digital video recording and transcription in possession of author).
17. King, M. E. 2012a. Verbal communication with the author on 13 March. Sandton. (Digital voice recording and transcription in possession of author). King, M. E. 2012b. Verbal communication with Bruce Whitfield on 13 March. Sandton. (Digital video recording and transcription in possession of author).
18. Loubser, R. 2012a. Verbal communication with the author on 16 February. Sandton. (Digital voice recording and transcription in possession of author).
19. Loubser, R. 2012b. Verbal communication with Bruce Whitfield on 16 February. Sandton. (Digital video recording and transcription in possession of author).
20. Nxasana, S. 2012a. Verbal communication with the author on 8 March. Sandton. (Digital voice recording and transcription in possession of author).
21. Nxasana, S. 2012b. Verbal communication with Bruce Whitfield on 8 March. Sandton. (Digital video recording and transcription in possession of author).
22. Oliphant, J. 2012a. Verbal communication with the author on 2 April. Sandton. (Digital voice recording and transcription in possession of author).
23. Oliphant, J. 2012b. Verbal communication with Bruce Whitfield on 2 April. Sandton. (Digital video recording and transcription in possession of author).
24. Payne, N. 2012a. Verbal communication with the author on 12 March. Sandton. (Digital voice recording and transcription in possession of author).
25. Payne, N. 2012b. Verbal communication with Bruce Whitfield on 12 March. Sandton. (Digital video recording and transcription in possession of author).
26. Terry, G. 2012a. Verbal communication with the author on 6 March. Sandton. (Digital voice recording and transcription in possession of author).
27. Terry, G. 2012b. Verbal communication with Bruce Whitfield on 6 March. Sandton. (Digital video recording and transcription in possession of author).
28. Wilkinson, R. 2012a. Verbal communication with the author on 23 March. Sandton. (Digital voice recording and transcription in possession of author).
29. Wilkinson, R. 2012b. Verbal communication with Bruce Whitfield on 23 March. Sandton. (Digital video recording and transcription in possession of author).
30. Yawitch, J. 2012a. Verbal communication with the author on 13 March. Sandton. (Digital voice recording and transcription in possession of author).
31. Yawitch, J. 2012b. Verbal communication with Bruce Whitfield on 13 March. Sandton. (Digital video recording and transcription in possession of author).

# Appendix A | Interviewee list

| Surname | Name | Professional Title |
|---|---|---|
| Adam | Mohamed | Member, King Committee |
| Andersen | Roy | Director of Companies, King Committee I, II & III |
| Armstrong | Philip | Head of Global Corporate Governance Forum, Washington DC |
| Botha | Theo | Director, CA Governance |
| Crotty | Ann | Journalist, Business Day |
| Godsell | Bobby | Chairman, Business Leadership |
| Gordhan | Pravin | South African Minister of Finance |
| Khoza | Reuel | Chairman, AKA Capital and The Nedbank Group |
| King | Mervyn | Chair, International Integrated Reporting Council |
| Loubser | Russell | Former CEO JSE, King Committee II & III |
| Nxasana | Sizwe | CEO, FirstRand Limited & FirstRand Bank |
| Oliphant | John | Chairman, CRISA |
| Payne | Nigel | Professional Non-Executive Director |
| Terry | Graham | Senior Executive, SAICA |
| Wilkinson | Richard | Previous CEO, IoD |
| Yawitch | Joanne | CEO, National Business Initiative |



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