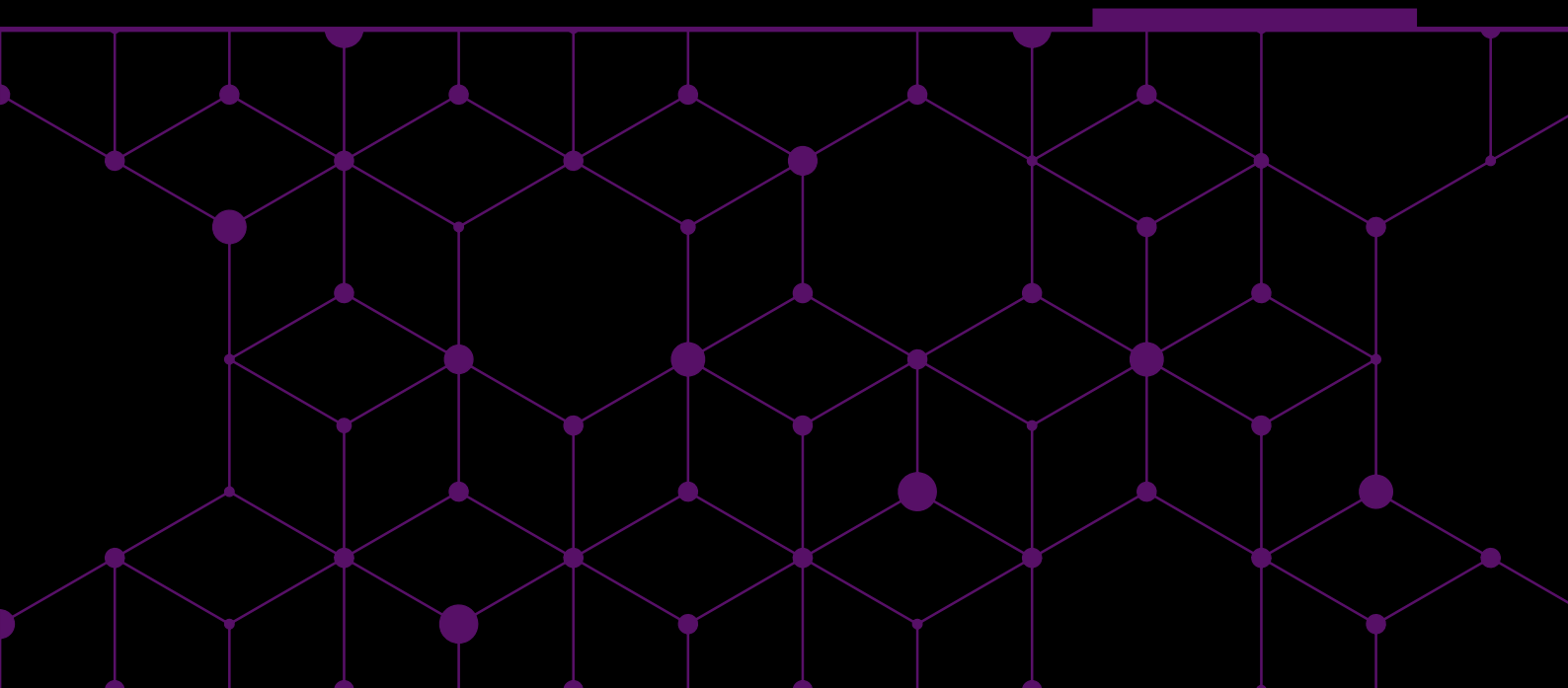


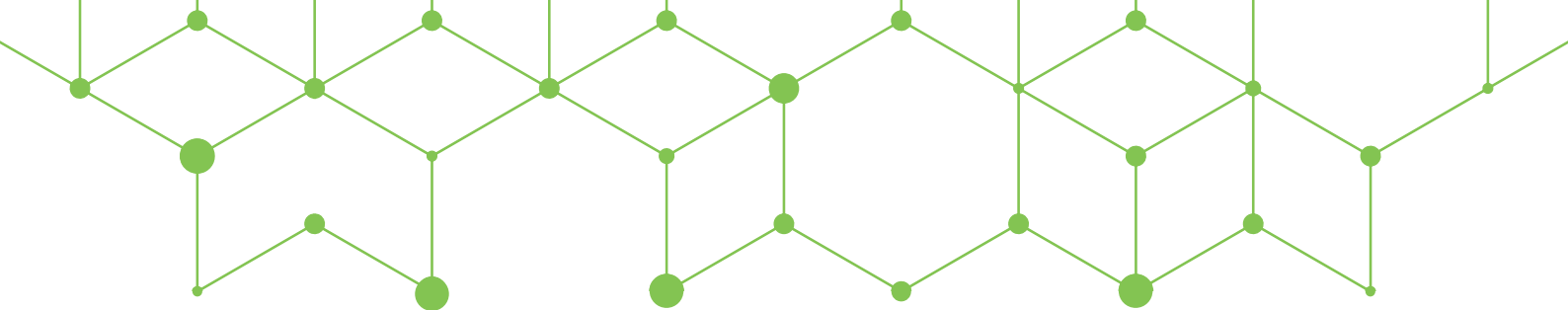


INSTITUTE OF DIRECTORS  
SOUTHERN AFRICA



**KING IV**

REPORT ON CORPORATE  
GOVERNANCE FOR  
SOUTH AFRICA 2016



# » ACKNOWLEDGEMENTS

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The King IV Report is dedicated to all those from the King Committee and outside it, even beyond the borders of South Africa, who so generously gave of their time and knowledge to contribute to the development of its content.



**Ansie Ramalho**

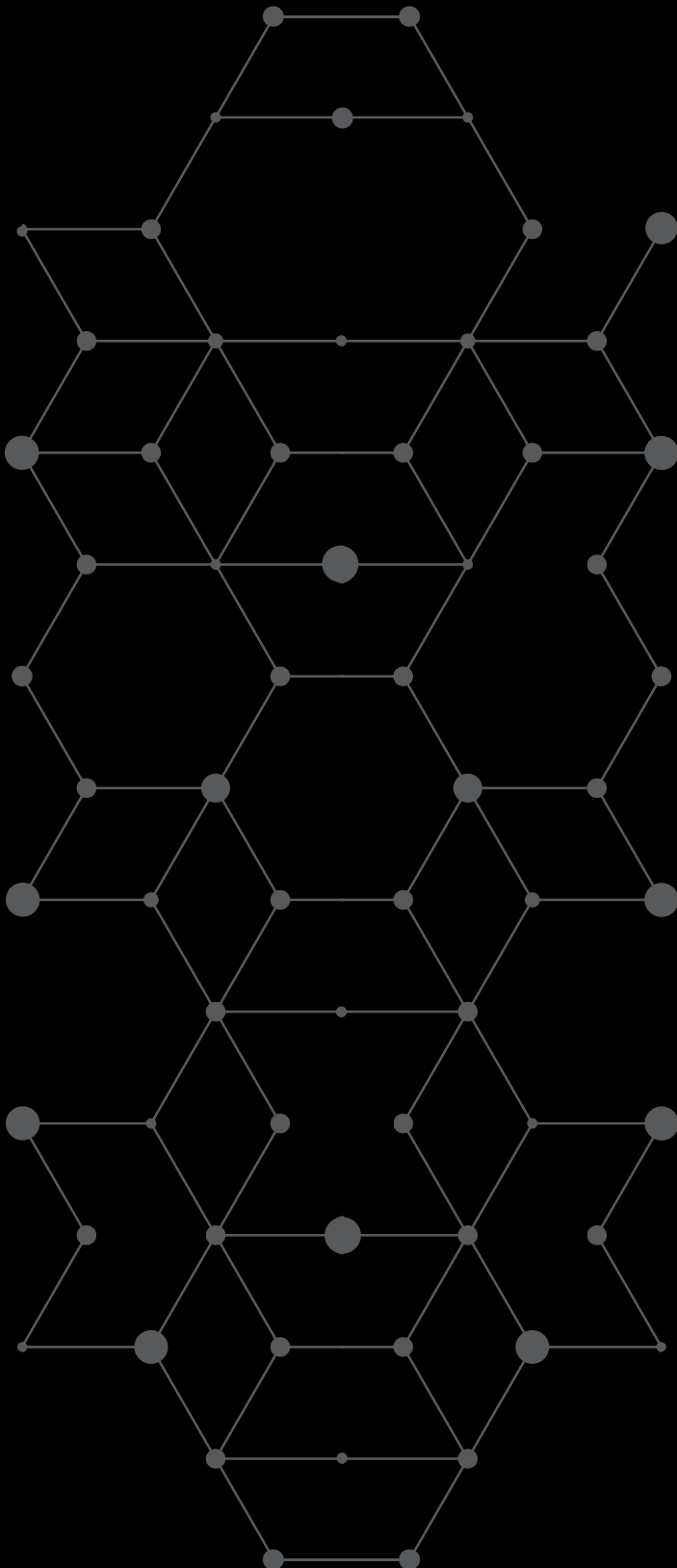
King IV Project Lead, Institute of Directors in Southern Africa

1 November 2016



INSTITUTE OF DIRECTORS  
SOUTHERN AFRICA

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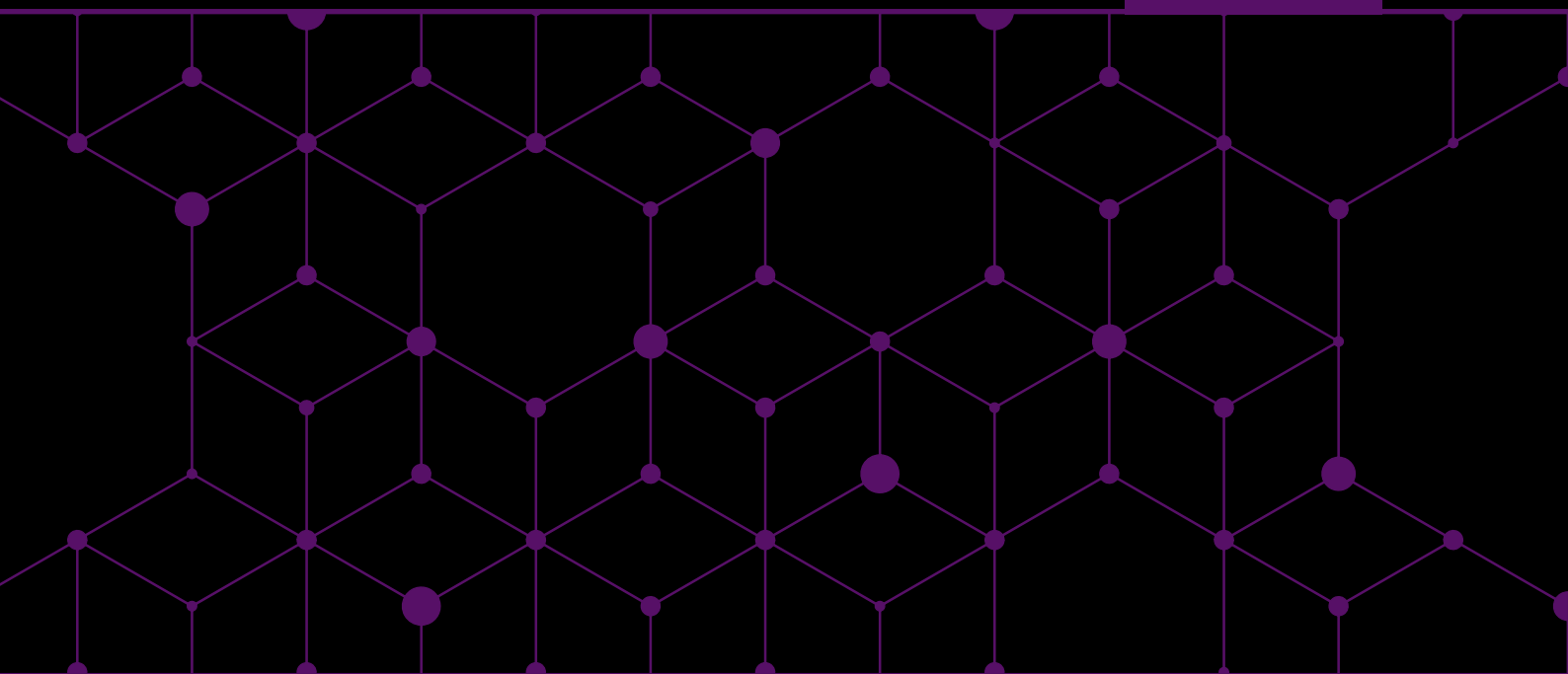
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## FOREWORD



# » FOREWORD

## INTRODUCTION

The 21st Century has been characterised by fundamental changes in both business and society. These fundamental changes provided the context within which the King Committee set out to draft King IV, and have influenced both its content and approach.

New global realities are testing the leadership of organisations on issues as diverse as inequality, globalised trade, social tensions, climate change, population growth, ecological overshoot, geopolitical tensions, radical transparency and rapid technological and scientific advancement.

The United Nations Sustainable Development Goals, which were agreed by all governments in 2015, the Africa 2063 Agenda and the (South African) National Development Plan 2030 (NDP) have a common theme of value creation that is accomplished in a sustainable manner. This is a fundamental concept of King IV.

## THE CHANGED WORLD

Financial instability is one driver of these changes. Financial crises arising out of the capital crisis in the United States of America and the Sovereign Fund crisis in the European Union have still not been resolved. Brexit created further uncertainty for financial systems.

Another change driver is climate change. Even those who are skeptical about the scientific evidence for climate change, or who question whether climate change is attributable to human agency or simply part of a longer-term cycle, have to acknowledge that the world has experienced extreme weather conditions that pose new risks in the last several years.

It is a reality that organisations and individuals are using natural assets faster than nature is regenerating them. This ecological overshoot will be exacerbated by continued population growth on the African and Asian continents. The global population is currently at 7.5 billion, and could reach 9.3 billion by 2045 according to the United Nations. Consequently, the pressure on natural assets will increase, as they are finite; continuing business as usual is no longer an option.

Ubiquitous social media platforms are creating a world characterised by radical transparency. Corporations can no longer conceal their actions or secrets. Technological advances, including the emergence of the Internet of things, are generating huge amounts of data; more importantly, sophisticated analytics is converting that data into deep insight into the behaviour of humans and their organisations.

Technology's disruptions continue. At present, advances in robotics, artificial intelligence, 3D printing, nanotechnology and biotechnology are accelerating the transformation of production and supply chains – and forcing professions like law and accounting to reinvent themselves.

Indeed, so profound are the disruptions to industries and business models that many believe we are in the midst of the Fourth Industrial Revolution.

There are greater expectations from stakeholders than ever before. Activism by civil society and shareholders have rocked companies over the last few years. The Millennial Generation (Millennials), roughly those born since 1980, is now the most numerous age cohort. Their concerns are beginning to set the global agenda. Millennials have shown that they are concerned about the global environmental crunch much more than the global financial crises. They are consequently attracted to companies who have integrated the six capitals into their business models. (The six capitals, as set out in the International Integrated Reporting Council's (IIRC) Integrated Reporting <IR> Framework, are financial, manufactured, human, intellectual, natural and social and relationship capital.)

# FOREWORD CONTINUED

In a similar vein, it is now accepted that organisations operate in the triple context of the economy, society and the environment. How they make their money does have an impact on these three elements and, in turn, they impact on organisations.

In the context of all the above, governing bodies have the challenge of steering their organisations to create value in a sustainable manner, making more but with less to meet the needs of a growing population and the reality of dwindling natural resources.

One corollary is that the duty of care has become both more complex and more necessary. No governing body today can say it is not aware of the changed world in which it is directing an organisation. Consequently, a business judgement call that does not take account of the impacts of an organisation's business model on the triple context could lead to a decrease in the organisation's value.

Milton Friedman's epigram, "The social responsibility of business is to increase its profits", must now be interpreted in the light of the view that an organisation is a part of society in its own right. It can no longer be seen as existing in its own narrow universe (or "society") of internal stakeholders and the resources needed to create value – it also operates in, and forms part of, general society. In this view, the licensor of an organisation is not just those individuals and entities within its narrowly defined value chain, but society as a whole.

## **THE THREE SHIFTS IN THE CORPORATE WORLD**

Certain concepts form the foundation stones of King IV. They are: ethical leadership, the organisation in society, corporate citizenship, sustainable development, stakeholder inclusivity, integrated thinking and integrated reporting. These concepts are relevant to three connected paradigm shifts in the corporate world.

### ***From financial capitalism to inclusive capitalism***

There is now general acceptance that the employment, transformation and provision of financial capital represent only a fraction of an organisation's activities. Instead, inclusive capitalism takes account of the employment, transformation and provision of all sources of capital – the six capitals – in order to reposition capitalism as the engine of shared prosperity. It gives parity to the sources of value creation.

Financial performance alone can no longer serve as proxy for holistic value creation. As stated by Jonathan Labrey from the IIRC: "Long-term financial performance depends on the efficient and productive management of resources not currently measured by traditional accounting methodologies – human, intellectual, social and relationship, and natural capitals. The financial capital market system is insufficient to guard against the multi-faceted and interconnected risks of the future and hence an inclusive market system should be adopted."<sup>1</sup>

This new way of thinking, known as inclusive capitalism, has the potential to trigger profound change. One is that, instead of simply providing aid to developing countries, developed country companies that are operating in more developing countries should focus on adopting the model of inclusive capitalism in the developing country, and thereby create value in a sustainable manner. The more an organisation's business model positively impacts on society and the environment, the more the quality of life in developing economies will improve. This improvement, in turn, will positively affect the prospects for those organisations.

### ***From short-term capital markets to long-term, sustainable capital markets***

The shift from short-term to long-term thinking arises from the need to create value in a sustainable manner. In essence, sustainable capitalism refers to an economic system in which value is created in a sustainable manner. The period indicated by long term or longer term would depend on the strategic objectives of the organisation and the risks and opportunities presented by its external environment, including its material stakeholders.

<sup>1</sup> Jonathan Labrey, Three shifts toward better decision-making (posted 26 May 2015, available at <http://integratedreporting.org/news/three-shifts-towards-better-decision-making/>)



Another element of this trend is the growing sense that the financial crisis of 2008, and others, were to a large degree caused by a narrow focus on short-term objectives with little or no consideration of the long-term effects on either the organisations concerned, or the economy as a whole. This opinion is prompting renewed focus on the unintended consequences of performance incentives, but also on ways to encourage investors and finance providers to extend their investment horizons.

In short, then, performance in terms of all-inclusive value should be assessed over the longer term. The capital market system must reward long-term decision-making.

#### ***From siloed reporting to integrated reporting***

We live in an era of radical transparency, which is prompting a rethink on corporate reporting. This is evidenced by the European Union's directive on environmental, social and governance (ESG) reporting, the United Kingdom's strategic report, the context of reports filed with the United States Securities and Exchange Commission, the Operating Financial Review in Australia and the listing requirements of several stock exchanges, including the Johannesburg Bourse.

The traditional financial reporting system was a revolutionary development when it was instituted. It has since had to respond to market regulators, standards boards, ever more complex legislation and the regulation of accounting and corporate reporting. It is accepted that, while fully compliant and duly audited financial statements are critical, they are insufficient to discharge the duty of accountability. Similarly, a sustainability report is critical but insufficient. The reality is that the resources or capitals used by organisations constantly interconnect and interrelate. The organisation's reporting should reflect this interconnectedness, and indicate how its activities affect, and are affected by, the six capitals it uses and the triple context in which it operates.

The move from siloed reporting to integrated reporting is consistent with the concept of an inclusive, sustainable capital market system. It has been given impetus by acceptance of the triple context in which organisations operate and the evolution of integrated thinking. The International Federation of Accountants has promoted integrated reporting to the G20 countries.

King IV takes cognisance of all three these shifts.

In response to these, leading organisations have begun to change the way they operate, stakeholder management, technology and strategy being three such areas:

**Stakeholder management:** In order to know and understand the legitimate and reasonable needs, interests and expectations of an organisation's major stakeholders, management needs an ongoing relationship with those stakeholders. Some organisations have appointed a corporate stakeholder relationship officer whose sole task is to communicate with stakeholders and inform management of their legitimate and reasonable needs, interests and expectations. This officer will also inform stakeholders what the organisation expects of them.

Understanding stakeholders' expectations will greatly assist the executive to develop better strategy. Stakeholder relationships should be a recurring item on the governing body's agenda so that the board can be kept apprised of the current state of the relationships between the organisation and its stakeholders.

# FOREWORD CONTINUED

**Technology governance and security:** Technology governance and security have become critical issues. Technology is no longer simply an enabler; the systems created by an organisation provide the platform on which it does business, and technology is now both the source of many of an organisation's future opportunities and of potential disruption – an excellent example of how risk and opportunity are increasingly two sides of the same coin.

Technology is now part of the corporate DNA. Thus, the security of information systems has become critical. Technology governance and security should become another recurring item on the governing body's agenda.

**Strategy:** As the world moves from siloed to integrated thinking, people are increasingly realising that organisations need to broaden the way they consider strategy. It is now apparent that strategy does not just involve a consideration of the inputs into the business models and the resulting outputs; the outcomes of the organisation's products or services must also be taken into account. In particular, organisations need to assess what impact they are having on critical aspects of society and the environment. Consequently, every meeting of the governing body should have an agenda item for the consideration of the full sequence from inputs to outcomes. This will enable the governing body to discuss what the outcomes of its products are, and if they are causing a positive or negative impact on value creation. It will be appreciated that an outcome which is contrary to that which society expects is inconsistent with good corporate citizenship, and will result in the diminution of an organisation's reputation, the trust in which it is held and the confidence society as a whole feels in it. Such a situation could well threaten the organisation's operational legitimacy. The end result would be a destruction in the value of the organisation.

## UNIVERSAL APPLICABILITY

King I, II and III had as their foundation ethical and effective leadership. King IV is no different. Clearly, good leadership, which is underpinned by the principles of good governance, is equally valuable in all types of organisations, not just those in the private sector. Similarly, the principles of good governance are equally applicable, and equally essential, in both public and private entities.

This link is implicit in King I, II and III; King IV seeks to make it explicit. Specifically, the King Committee was requested by many entities outside the private sector to draft King IV in such a way as to make it more easily applicable to all organisations: public and private, large and small, for-profit and not-for-profit.

King IV has been drafted with this in mind. Thus, for example, it talks of organisations and governing bodies, rather than simply companies and boards of directors. Another innovation aimed at making it easier for all organisations to use the King IV Report as a guide for good governance is the inclusion of sector supplements.

## THE GLOSSARY

To obtain maximum benefit from this Report, the Code and the supplements, the user should read Part 1: *Glossary of Terms* following this foreword so that the meanings given to technical terms are consistently understood.

## **FROM “APPLY OR EXPLAIN” TO “APPLY AND EXPLAIN”**

King IV has moved from “apply or explain” to “apply and explain”, but has reduced the 75 principles in King III to 17 basic principles in King IV, one of which applies to institutional investors only. 16 of these principles can be applied by any organisation, and all are required to substantiate a claim that good governance is being practised. The required explanation allows stakeholders to make an informed decision as to whether or not the organisation is achieving the four good governance outcomes required by King IV. Explanation also helps to encourage organisations to see corporate governance not as an act of mindless compliance, but something that will yield results only if it is approached mindfully, with due consideration of the organisation’s circumstances.

This outcomes-based approach for a corporate governance code, and the “apply and explain” regime are the original intellectual thinking of the King Committee.

## **APPRECIATION AND CONCLUSION**

I record my thanks and appreciation to my committee and the task team, who jointly and severally devoted so much time and effort in the interests of corporate (in its broadest sense) South Africa, without remuneration or reimbursement of expenses. In particular, I thank Ansie Ramalho, who led the task team, convened meetings with commentators, collated the comments to the draft report, and convened the working sessions which comprised experts on each of the essential topics contained in this report. I must pay special tribute to her patience in dealing with all of my comments without complaint. My thanks and appreciation also are due to our editors, and to those who contributed to the layout of the report.

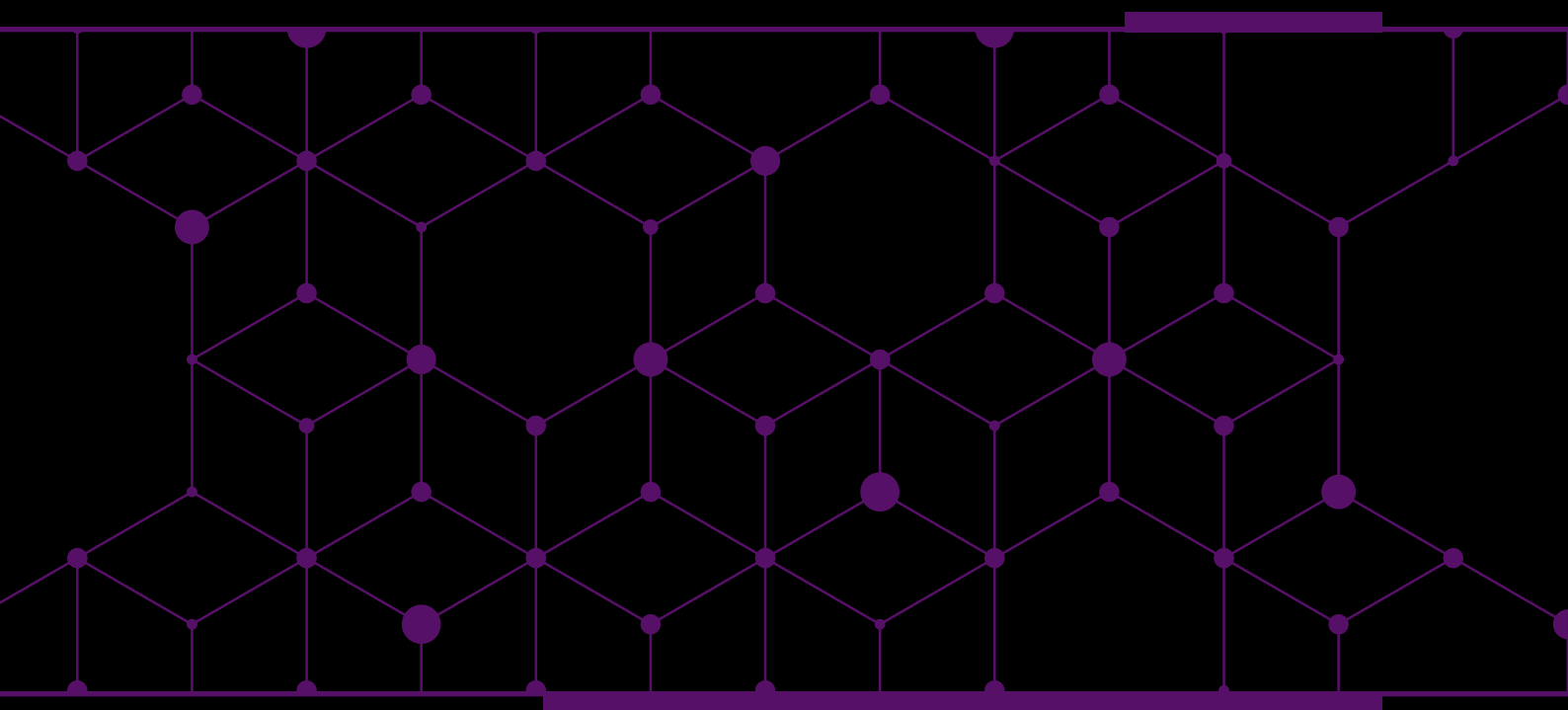
The King Committee believes that this fourth iteration will reinforce global recognition of the King Committee’s reports on governance.



**Mervyn E King SC**  
Chair of the King Committee

1 November 2016

# PART 1



## GLOSSARY OF TERMS

The following words carry the meaning as indicated for purposes of interpreting and applying King IV.

# » GLOSSARY OF TERMS

Accountability	The obligation to answer for the execution of responsibilities. Accountability cannot be delegated, whereas responsibility can be delegated without abdicating accountability for that delegated responsibility.
Accounting authority	As defined in terms of section 1 of the PFMA, it “means a body or person mentioned in section 49 of the PFMA”.
AGM	AGM is the abbreviation of annual general meeting as defined in the Companies Act or, for organisations other than companies, it means the meeting that serves a similar purpose as the AGM of a company.
Arrangement	The way that people and things are organised for a particular purpose, activity or function, including frameworks, structures, systems and methods.
Assurance	<p>The diligent application of mind to evidence, resulting in a statement or declaration concerning an identified subject matter or subject matter information, and that is made for the purpose of enhancing confidence in that subject matter or subject matter information.</p> <p>Assurance includes, but is not limited to, assurance engagements performed by independent, external assurance service providers (such as the external auditor) in accordance with the International Auditing and Assurance Standards Board’s International Engagement Standards. Such assurance “means an engagement in which a practitioner expresses a conclusion designed to enhance the degree of confidence of the intended users other than the responsible party about the outcome of the evaluation or measurement of a subject matter against criteria”<sup>1</sup>.</p> <p>Assurance furthermore includes, but is not limited to, assurance provided in terms of the International Standards for the Professional Practice of Internal Auditing, namely, “an objective examination of evidence for the purpose of providing an independent assessment on governance, risk management and control processes for the organization”<sup>2</sup>.</p> <p>Assurance service providers and functions may include the following:</p> <ol style="list-style-type: none"> <li>a. The organisation’s line functions that own and manage risks.</li> <li>b. The organisation’s specialist functions that facilitate and oversee risk management and compliance.</li> <li>c. Internal auditors, internal forensic fraud examiners and auditors, safety and process assessors, and statutory actuaries.</li> <li>d. Independent external assurance service providers such as external auditors.</li> <li>e. Other external assurance providers such as sustainability and environmental auditors, external actuaries, and external forensic fraud examiners and auditors.</li> <li>f. Regulatory inspectors.</li> </ol>

1 International Auditing and Assurance Standards Board, *The International Framework for Assurance Engagements*, (Effective for assurance reports issued on or after January 1, 2005)

2 The Institute of Internal Auditors, *International Standards for the Professional Practice of Internal Auditing*, (2012), p 19

## GLOSSARY OF TERMS CONTINUED

Audit firm tenure	The length of the audit firm-client relationship. It should be calculated as the number of uninterrupted financial years that an audit firm has acted as external auditor of an organisation, up to and including the organisation's last audited financial year.
Beneficiary	In the context of a retirement fund "means a nominee of a member or a dependant who is entitled to a benefit, as provided for in the rules of the relevant fund", as defined in section 1 of the Pension Funds Act.
Board	If it is used in the context of a company, "means the board of directors of a company", as defined in section 1 of the Companies Act.  If it is used in the context of a retirement fund, "means a board of a fund as contemplated in terms of Section 7A of this Act", as defined in section 1 of the Pension Funds Act.  Boards form a subset of the wider term "governing bodies".
Business model	"An organization's system of transforming inputs through its business activities into outputs and outcomes that aims to fulfil the organization's strategic purposes and create value over the short, medium and long term." <sup>3</sup>
CAE	Chief audit executive.
Capitals or six capitals	"The capitals are stocks of value on which all organizations depend for their success as inputs to their business model, and which are increased, decreased or transformed through the organization's business activities and outputs." <sup>4</sup> In accordance with the six capitals model, these capitals consist of financial, manufactured, intellectual, human, social and relationship, and natural capital. Each of these capitals are described in the International <IR> Reporting Framework <sup>5</sup> .
CEO	Chief executive officer or the highest ranking employee in an organisation regardless of naming convention.
CFO	Chief finance officer.
Character	Character describes the attributes that make up and distinguish an individual or a group. It is a way of being rather than a way of doing.
Code	Part 5 of the King IV Report on Corporate Governance for South Africa, 2016.
Combined assurance model	A combined assurance model incorporates and optimises all assurance services and functions so that, taken as a whole, these enable an effective control environment; support the integrity of information used for internal decision-making by management, the governing body and its committees; and support the integrity of the organisation's external reports.
Companies Act	Companies Act, No 71 of 2008, as amended.

<sup>3</sup> The International Integrated Reporting Council, *The International <IR> Framework* (13 December 2013), p 33, available at <http://integratedreporting.org/resource/international-ir-framework/>

<sup>4</sup> The International Integrated Reporting Council; *The International <IR> Framework*, (13 December 2013), p 33, available at <http://integratedreporting.org/resource/international-ir-framework/>

<sup>5</sup> The International Integrated Reporting Council, *The International <IR> Framework* (13 December 2013), p 11-12, available at <http://integratedreporting.org/resource/international-ir-framework/>

Company	A juristic person incorporated in terms of the Companies Act.
Competence	Possessing the skills and attributes, and exhibiting the conduct that are used to define and measure suitability for a certain role or function.
Conflict of interest	A conflict of interest, used in relation to members of the governing body and its committees, occurs when there is a direct or indirect conflict, in fact or in appearance, between the interests of such member and that of the organisation. It applies to financial, economic and other interests in any opportunity from which the organisation may benefit, as well as use of the property of the organisation, including information. It also applies to the member's related parties holding such interests. (See also "related party" and "independence".)
Constitution	Constitution of the Republic of South Africa, 1996.
Corporate citizenship	Corporate citizenship is the recognition that the organisation is an integral part of the broader society in which it operates, affording the organisation standing as a juristic person in that society with rights but also responsibilities and obligations. It is also the recognition that the broader society is the licensor of the organisation.
Corporate governance	<p>For the purposes of King IV, is defined as the exercise of ethical and effective leadership by the governing body towards the achievement of the following governance outcomes:</p> <ul style="list-style-type: none"> <li>• Ethical culture</li> <li>• Good performance</li> <li>• Effective control</li> <li>• Legitimacy.</li> </ul> <p>The use of "corporate" in the term "corporate governance" is used to differentiate it from other forms of governance, for example national or political governance. "Corporate" refers to organisations that are incorporated to form legal entities separate from their founders and therefore applies to all forms of incorporation whether as company, voluntary association, retirement fund, trust, legislated entity or others.</p>
Council	"Municipal council' or 'council' means the council of a municipality as referred to in section 18 of the Municipal Structures Act", as defined in section 1 of the MFMA.
Creation of value	The positive consequences of the organisation's business activities and outputs on the triple context in which the organisation operates, and the capitals it uses and affects.
CRISA	Code for Responsible Investing in South Africa, 2011.
Culture	In an organisational context, "the way in which members of an organisation relate to each other, their work and the outside world in comparison to other organisations" <sup>6</sup> . It is generally described as "the way we do things around here, even when no one is watching".

6 The Hofstede Centre, itim International, *The Hofstede Multi-Focus Model on Organisational Culture* (2016), available at <https://geert-hofstede.com/organisational-culture.html>

## GLOSSARY OF TERMS CONTINUED

Director	“Means a member of the board of a company, as contemplated in section 66, or an alternate director of a company and includes any person occupying the position of a director or alternate director, by whatever name designated”, as defined in section 1 of the Companies Act.
Diversity	Diversity should be understood as the varied perspectives and approaches offered by members of different identity groups. For the purposes of King IV, it includes diversity in terms of fields of knowledge, skills and experience as well as age, culture, race and gender.
Effective or effectively	The adequate accomplishment of the desired objective or a pursuit with the minimum expenditure of time, resources, waste and effort.
Ensure	Ensure, where it is used in relation to the responsibilities of the governing body, means to direct and oversee in good faith and with best reasonable effort towards achieving the desired result.
ESG	Environmental, social and governance.
Ethics	Considering what is good and right for the self and the other, and can be expressed in terms of the golden rule, namely, to treat others as you would like to be treated yourself. In the context of organisations, ethics refers to ethical values applied to decision-making, conduct, and the relationship between the organisation, its stakeholders and the broader society.
Executive authority	“In relation to a national public entity, means the Cabinet member who is accountable to Parliament for that public entity or in whose portfolio it falls” and “in relation to a provincial public entity, means the member of the provincial Executive Council who is accountable to the provincial legislature for that public entity or in whose portfolio it falls”, as defined in section 1(c) and (d) of the PFMA.
Fairness	Fairness refers to the equitable and reasonable treatment of the sources of value creation, including relationship capital as portrayed by the legitimate and reasonable needs, interests and expectations of material stakeholders of the organisation.
FSB Circular PF 130	Financial Services Board Circular PF 130.
Good performance	Good performance is an organisation achieving its strategic objectives, and positive outcomes in terms of its effects on the capitals it uses and affects and on the triple context in which it operates. (See also “performance”.)
Governance outcomes	The positive effects or benefits of good corporate governance for the organisation. These positive effects include: ethical culture, good performance, effective control, and legitimacy.
Governing body	The governing body is the structure that has primary accountability for the governance and performance of the organisation. Depending on context, it includes, among others, the board of directors of a company, the board of a retirement fund, the accounting authority of a state-owned entity and a municipal council.  “Members of the governing body” (also referred to as “those charged with governance duties”) are those who are duly appointed to serve on the governing body and/or its committees.



GRI	Global Reporting Initiative.
Group of companies	“Means a holding company and all of its subsidiaries”, as defined in section 1 of the Companies Act.
Holding company	“Means in relation to a subsidiary, a juristic person that controls that subsidiary as a result of any circumstances contemplated in section 2(2)(a) or 3(1)(a)”, as defined in terms of section 1 of the Companies Act.
Independence	Independence generally means the exercise of objective, unfettered judgement. When used as the measure by which to judge the appearance of independence, or to categorise a non-executive member of the governing body or its committees as independent, it means the absence of an interest, position, association or relationship which, when judged from the perspective of a reasonable and informed third party, is likely to influence unduly or cause bias in decision-making. (See also “conflict of interest”.)
Information	Includes all data, records and knowledge in electronic or any other format, which form part of the intellectual capital used, transformed or produced by the organisation.
Inputs	“The capitals (resources and relationships) that the organization draws upon for its business activities.” <sup>7</sup>
Integrated report	“A concise communication about how an organization’s strategy, governance, performance and prospects, in the context of its external environment, lead to the creation of value in the short, medium and long term.” <sup>8</sup>
Integrated reporting	“A process founded on integrated thinking that results in a periodic integrated report by an organization about value creation over time. It includes related communications regarding aspects of value creation.” <sup>9</sup>
Integrated thinking	“Integrated thinking is defined as the active consideration by an organization of the relationships between its various operating and functional units and the capitals that the organization uses or affects.” <sup>10</sup>
Institutional investor	Any juristic person or institution referred to in the definition of financial institution in section 1 of the Financial Services Board Act, No 97 of 1990, to the extent that these juristic persons or institutions are the holders of beneficial interest in the securities of a company. It includes retirement funds and insurance companies as well as the custodians, nominees and service providers who act under mandate in respect of any investment decisions and investment activities exercised in relation to these securities. <sup>11</sup>

7 The International Integrated Reporting Council, *The International <IR> Framework*, (13 December 2013) available at <http://integratedreporting.org/resource/international-ir-framework/> – <http://integratedreporting.org/resource/international-ir-framework/>

8 The International Integrated Reporting Council, *The International <IR> Framework*, (13 December 2013) available at <http://integratedreporting.org/resource/international-ir-framework/> – <http://integratedreporting.org/resource/international-ir-framework/>

9 The International Integrated Reporting Council, *The International <IR> Framework*, (13 December 2013) available at <http://integratedreporting.org/resource/international-ir-framework/>

10 The International Integrated Reporting Council, *The International <IR> Framework* (13 December 2013) available at <http://integratedreporting.org/resource/international-ir-framework/> – <http://integratedreporting.org/resource/international-ir-framework/>

11 Adapted from the definition “institutional investor” used by the Committee for Responsible Investing South Africa, *The Code for Responsible Investing in South Africa* (Institute of Directors in Southern Africa 2011), p 9, available at [www.iodsa.co.za](http://www.iodsa.co.za)

## GLOSSARY OF TERMS CONTINUED

Integrity	<p>In the context of governance and ethics, integrity is possessing the quality of being honest and having strong moral principles. It encompasses consistency between stated moral and ethical standards, and actual conduct.</p> <p>Integrity, in relation to the annual financial statements and other external reports issued by the organisation, refers to the reliability and usefulness of these reports. (In this context, “reliability” means validity, accuracy and completeness, while “usefulness” means consistency, relevance and measurability.)</p>
International <IR> Framework	International Integrated Reporting Framework.
King Committee	King Committee on Corporate Governance in South Africa.
King III	King III Report on Governance for South Africa, 2009.
King IV	King IV Report on Corporate Governance for South Africa, 2016. It refers to the complete document that includes all of its parts.
King IV Code	Part 5 of the King IV Report.
King IV Report	King IV Report on Corporate Governance for South Africa, 2016. It refers to the complete document that includes all of its parts.
Management	<p>Management includes senior management and executive management.</p> <p>“Senior management” is the level of management reporting to executive management.</p> <p>“Executive management” is, after the governing body, the highest decision-making authority in the organisation.</p> <p>“Executive managers” are the members of the executive management team and include executive members of the governing body and prescribed officers as defined in the Companies Act or, in respect of organisations other than companies, those who exercise general executive control over, and management of, the whole or significant portions of the business and activities of the organisation.</p>
Material or materiality	<p>As used generally in King IV, it is a “measure of the estimated effect that the presence or absence of an item of information [or identified subject matter] may have on the accuracy or validity of a statement [or decision]. Materiality is judged in terms of its inherent nature, impact (influence) value, use value, and the circumstances (context) in which it occurs”<sup>12</sup>.</p> <p>Materiality in relation to the inclusion of information in an integrated report refers to matters that “could substantively affect the organization’s ability to create value over the short, medium and long term”<sup>13</sup>.</p>
May	In King IV, “may” is used to describe a recommendation that is permissible but not considered essential. (See also “should” and “must”.)

<sup>12</sup> The Business Dictionary, available at <http://www.businessdictionary.com/definition/materiality.html>

<sup>13</sup> The International Integrated Reporting Council, *The International <IR> Framework* (13 December 2013), p 5, available at <http://integratedreporting.org/resource/international-ir-framework/>

Member	<p>When used in reference to a non-profit company, “means a person who holds membership in, and specified rights in respect of, that non-profit company, as contemplated in Schedule 1”, as defined in section 1 of the Companies Act.</p> <p>When used in reference to a retirement fund “means a person who belongs or belonged to a class of persons for whose benefit that fund has been established, but does not include any person who has received all the benefits which may be due to that person from the fund and whose membership has thereafter been terminated in accordance with the rules of the fund”, as defined in section 1 of the Pension Funds Act.</p>
MFMA	Municipal Finance Management Act, No 56 of 2003, as amended.
Municipal entity or ME	“Means a) a company, co-operative trust, fund or any other corporate entity established in terms of any applicable national or provincial legislation and which operates under the ownership control of one or more municipalities, and includes, in the case of a company under such ownership control, any subsidiary of that company; or b) a service utility”, as defined in section 1 of the Municipal Systems Act.
Municipal Structures Act	Municipal Structures Act, No 117 of 1998, as amended.
Municipal Systems Act	Municipal Systems Act, No 32 of 2000, as amended.
Must	In King IV, “must” is used specifically to indicate a legal obligation. (See also “may” and “should”.)
NGO	Non-governmental organisation.
NPO	Non-profit organisation.
Non-Profit Organisations Act	Non-Profit Organisations Act, No 71, of 1997, as amended.
Organisation	A company, retirement fund, non-profit organisation, state-owned entity, municipality, municipal entity, trust, voluntary association and any other juristic person regardless of its manner of incorporation.
Outcomes	Outcomes in the context of the outcomes of the activities and outputs of an organisation means “the internal and external consequences (positive and negative) for the capitals as a result of an organization’s business activities and outputs” <sup>14</sup> . It also refers to the internal and external consequences of the business activities and outputs on the triple context in which the organisation operates.
Outputs	“The products, services, by-products and waste that are produced by an organization.” <sup>15</sup>

14 Adapted from The International Integrated Reporting Council, *The International <IR> Framework* (13 December 2013), available at <http://integratedreporting.org/resource/international-ir-framework/>

15 Adapted from The International Integrated Reporting Council, *The International <IR> Framework* (13 December 2013), available at <http://integratedreporting.org/resource/international-ir-framework/> and Reporting on Outcomes: An Information Paper, Integrated Reporting Committee South Africa, “Reporting on Outcomes: An Information Paper” 2015, available at [www.integratedreportingsa.org](http://www.integratedreportingsa.org)

## GLOSSARY OF TERMS CONTINUED

PBO	Public Benefit Organisation.
Pension Funds Act	Pension Funds Act, No 24 of 1956, as amended.
Performance	“An organization’s achievements relative to its strategic objectives, and its outcomes in terms of its effects on the capitals.” <sup>16</sup> It includes the organisation’s outcomes in terms of its effects on the triple context in which the organisation operates. Performance is therefore the result (positive and negative) of the value creation process. (See also “good performance”.)
PFMA	Public Finance Management Act, No 1 of 1999, as amended.
Policy	Policy gives effect to strategy and strategic direction by defining the frameworks, standards and plans that establish the scope or spheres within which judgement is exercised, decisions are made and actions are taken.
PRI	United Nations supported Principles for Responsible Investment.
Principal officer	The principal executive officer to be appointed by every registered fund in terms of section 8 of the Pension Funds Act.
Providers of financial capital	Equity and debt holders and others who provide financial capital including, lenders and other creditors.
Related party	A related party is a person or entity as set out in section 2(1) of the Companies Act. It applies <i>mutatis mutandis</i> to organisations other than companies. (See also “conflict of interest”.)
Responsibility	Taking ownership of a duty, obligation or liability.
Responsible investment	“An approach to investing that aims to incorporate environmental, social and governance factors into investment decision-making, to better manage risk and generate sustainable long-term returns.” <sup>17</sup>
Risk	Risk is about the uncertainty of events; including the likelihood of such events occurring and their effect, both positive and negative, on the achievement of the organisation’s objectives. Risk includes uncertain events with a potential positive effect on the organisation (i.e. opportunities) not being captured or not materialising. <sup>18</sup>
Sector supplements	Part 6 of the King IV Report.
Sensitive information	Information that is likely to compromise competitiveness, privilege or commercial advantage.
Shareholders	“Subject to section 57(1) of the Act, means the holder of a share issued by a company and who is entered as such in the certificated or uncertificated securities register, as the case may be” as defined in section 1 of the Companies Act.  Depending on context, references to shareholders in King IV may also apply to the members of non-profit companies.

<sup>16</sup> The International Integrated Reporting Council, *The International <IR> Framework* (13 December 2013), p 33 available at – <http://integratedreporting.org/resource/international-ir-framework/>

<sup>17</sup> Principles for Responsible Investing available <https://www.unpri.org/about/what-is-responsible-investment>

<sup>18</sup> Broadly based of definition of risk by the International Organization for Standardization; ISO Guide 73:2009; available at <https://www.iso.org/obp/ui/#iso:std:iso:guide:73:ed-1:v1:en>

Should	<p>When used in King IV with reference to the principles, it indicates an aspiration or ideal state. When used with reference to the recommended practices in King IV, it indicates a recommended course of action that is particularly suitable, without mentioning or excluding other possibilities.</p> <p>“Should not” indicates that a certain course of action is not recommended but not prohibited either. (See also “may” and “must”.)</p>
SME	Small and medium enterprise.
Society	Refers principally to the broader society or community as part of the triple context in which the organisation operates, and the social and relationship capital that the organisation uses and affects. Society includes the organisation’s internal and external stakeholders, which in turn form part of the broader society as a whole.
SOE	State-owned entity.
Stakeholder inclusivity	<p>An approach in which the governing body takes into account the legitimate and reasonable needs, interests and expectations of all material stakeholders in the execution of its duties in the best interests of the organisation over time.</p> <p>By following this approach, instead of prioritising the interests of the providers of financial capital, the governing body gives parity to all sources of value creation, including, among others, social and relationship capital as embodied by stakeholders. Consequently, this is an inclusive, stakeholder-centric approach which stands in contrast with a shareholder-centric approach.</p>
Stakeholders	<p>“Those groups or individuals that can reasonably be expected to be significantly affected by an organization’s business activities, outputs or outcomes, or whose actions can reasonably be expected to significantly affect the ability of the organization to create value over time.”<sup>19</sup></p> <p>“Internal stakeholders” are directly affiliated with the organisation and include its governing body, management, employees and shareholders.</p> <p>“External stakeholders” could include trade unions, civil society organisations, government, customers and consumers.</p> <p>Internal stakeholders are always material stakeholders, but external stakeholders may or may not be material.</p>
Strategy	The setting of the organisation’s short, medium and long-term direction towards realising its core purpose and values.
Subsidiary	As defined in terms of section 1 of the Companies Act “has the meaning determined accordance with section 3 of the Act”.
Sustainability	Sustainability is the ultimate, long-term goal of sustainable development. (See also “sustainable development”.)

19 The International Integrated Reporting Council, *The International <IR> Framework* (13 December 2013), p 33 available at <http://integratedreporting.org/resource/international-ir-framework/>

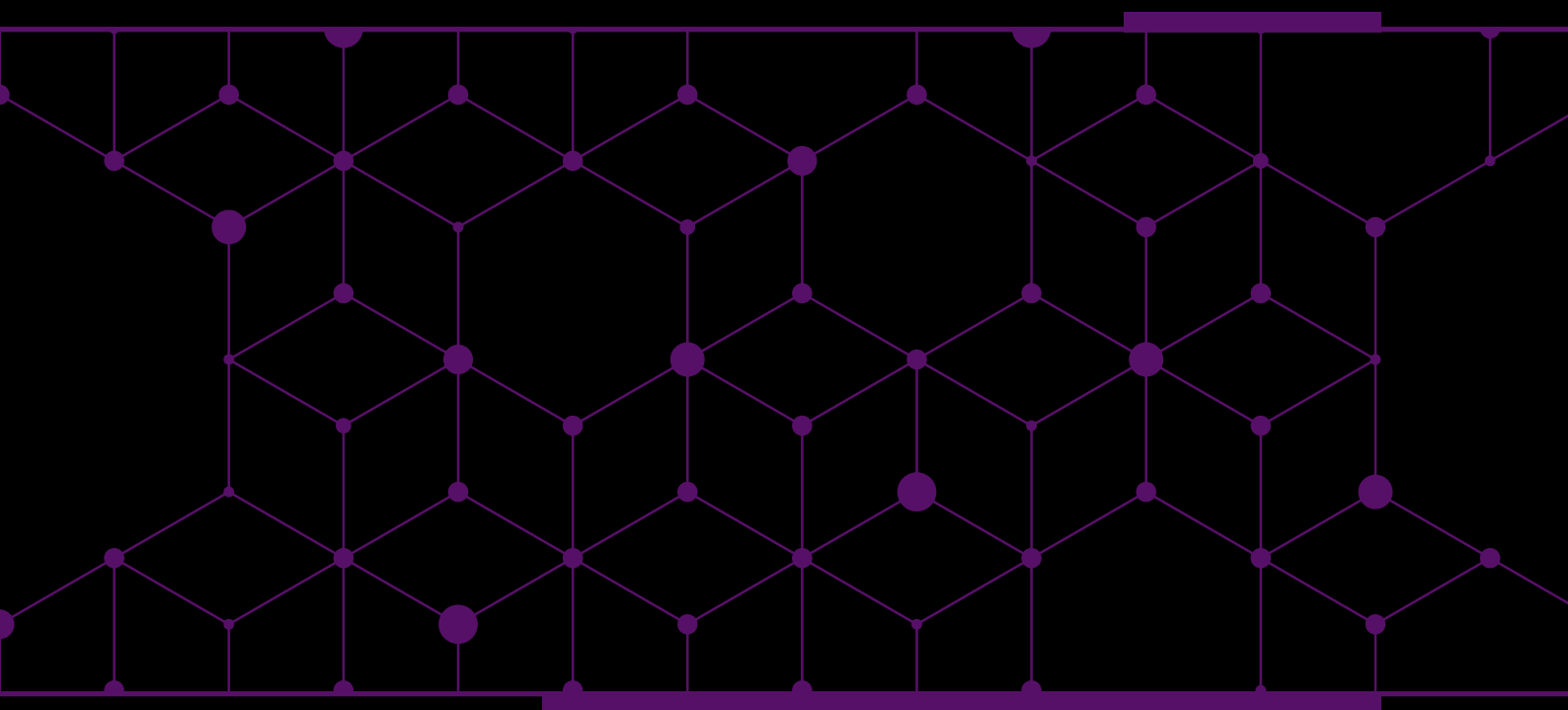
# GLOSSARY OF TERMS CONTINUED

Sustainable development	<p>In general, “development that meets the needs of the present without compromising the ability of future generations to meet their needs”<sup>20</sup>.</p> <p>At the level of organisations’ participation in sustainable development, it means organisations intentionally interacting with, and responding to, the opportunities and challenges presented by the dynamic system of the triple context in which the organisation operates and the capitals that the organisation uses and affects, with the aim to achieve the creation of value over time. Sustainable development is not confined to individual matters, such as the economic viability of the organisation, the natural environment or corporate social responsibility. Rather, it refers to an integrated approach that includes these and other considerations as represented by the triple context (see also “triple context”) and the capitals (see also “capitals”).</p>
Technology	Technology comprises the infrastructure, devices, systems and software that generate, use or carry information and enable transactions.
Transparency	The unambiguous and truthful exercise of accountability such that decision-making processes and business activities, outputs and outcomes (both positive and negative) are easily able to be discerned and compared with ethical standards.
Triple context	The combined context of the economy, society and environment in which the organisation operates.
Value creation or value creation process	“The process that results in increases, decreases or transformations of the capitals caused by the organization’s business activities and outputs.” <sup>21</sup> The value creation process therefore has neutral, positive and negative outcomes.
Values	Convictions and beliefs about how the organisation and those who represent it should conduct themselves; how resources and stakeholders should be treated; what the core purpose and objectives of the organisation should be; and how work duties should be performed.

<sup>20</sup> United Nations, “Report of the World Commission on Environment and Development: Our Common Future”, (Oxford, Great Britain: Oxford University Press, 1987), p 8. Also known as the Brundtland Report after Gro Harlem Brundtland, Chairman of the Commission and available at <http://www.un-documents.net/our-common-future.pdf>

<sup>21</sup> The definition of “value creation” as per: The International Integrated Reporting Council, *The International <IR> Framework* (13 December 2013), p 33 available at <http://integratedreporting.org/resource/international-ir-framework/>

# PART 2



## FUNDAMENTAL CONCEPTS



# » FUNDAMENTAL CONCEPTS

## INTRODUCTION

Since the publication of the first King report, South Africa has maintained a proud tradition of corporate governance. King IV is the fourth iteration of that report, and sets out the philosophy, principles, practices and outcomes which serve as the benchmark for corporate governance in South Africa.

Part 2 contains the fundamental concepts and philosophy on which King IV is based, the distinguishing features of King IV and how the various developments in corporate governance, locally and internationally, since King III came into effect in 2009, have influenced the principles and practices in the Code. A firm grasp of the content in this part is necessary for effective application of King IV.

## DEFINITION OF CORPORATE GOVERNANCE

Corporate governance, for the purposes of King IV, is defined as the exercise of ethical and effective leadership by the governing body towards the achievement of the following governance outcomes:

- Ethical culture
- Good performance
- Effective control
- Legitimacy.

Ethical and effective leadership should complement and reinforce each other.

**Ethical leadership** is exemplified by integrity, competence, responsibility, accountability, fairness and transparency. It involves the anticipation and prevention, or otherwise amelioration, of the negative consequences of the organisation's activities and outputs on the economy, society and the environment and the capitals that it uses and affects.

**Effective leadership** is results-driven. It is about achieving strategic objectives and positive outcomes. Effective leadership includes, but goes beyond, an internal focus on effective and efficient execution.



The governing body’s primary governance role and responsibilities are depicted below as part of the dynamic of the organisation’s business cycle<sup>1</sup>. This role and responsibilities include to steer the organisation and set its strategic direction, on the basis of which management will develop the strategy which is to be approved by the governing body. To give effect to the organisation’s strategy, management formulates policy and operational plans, also to be approved by the governing body. Management then, implements and executes strategy in accordance with policy and plans which are overseen and supervised by the governing body. The governing body finally ensures that there is accountability for organisational performance through, among others, reporting and disclosure. The latter in turn forms the basis for reviewing strategic direction which starts the business cycle anew.



The governing body’s primary governance role and responsibilities, as described above, are replicated and incorporated as the structural basis for the recommended practices under each of the governance areas (for example ethics, risk, compliance, remuneration and stakeholder relationships) covered by the Code. Thus, the practices are organised in accordance with the following series of responsibilities: The governing body assumes responsibility for providing the direction for how each governance area should be approached, addressed and conducted. This is followed by formulation of policy in the form of frameworks, standards and plans by management to be approved by the governing body. The governing body oversees and monitors implementation and execution by management, and finally ensures that there is accountability for the performance in respect of each of these governance areas through reporting and disclosure.

<sup>1</sup> Adapted from Bob Tricker, *Corporate Governance Principles, Policies and Practices*; Second edition, (Oxford University Press, 2012), p 174

## FUNDAMENTAL CONCEPTS CONTINUED

By organising the recommended practices in accordance with the governance role and responsibilities as explained above, King IV provides governing bodies with a model for the way in which any area that is subject to their governance should be approached.

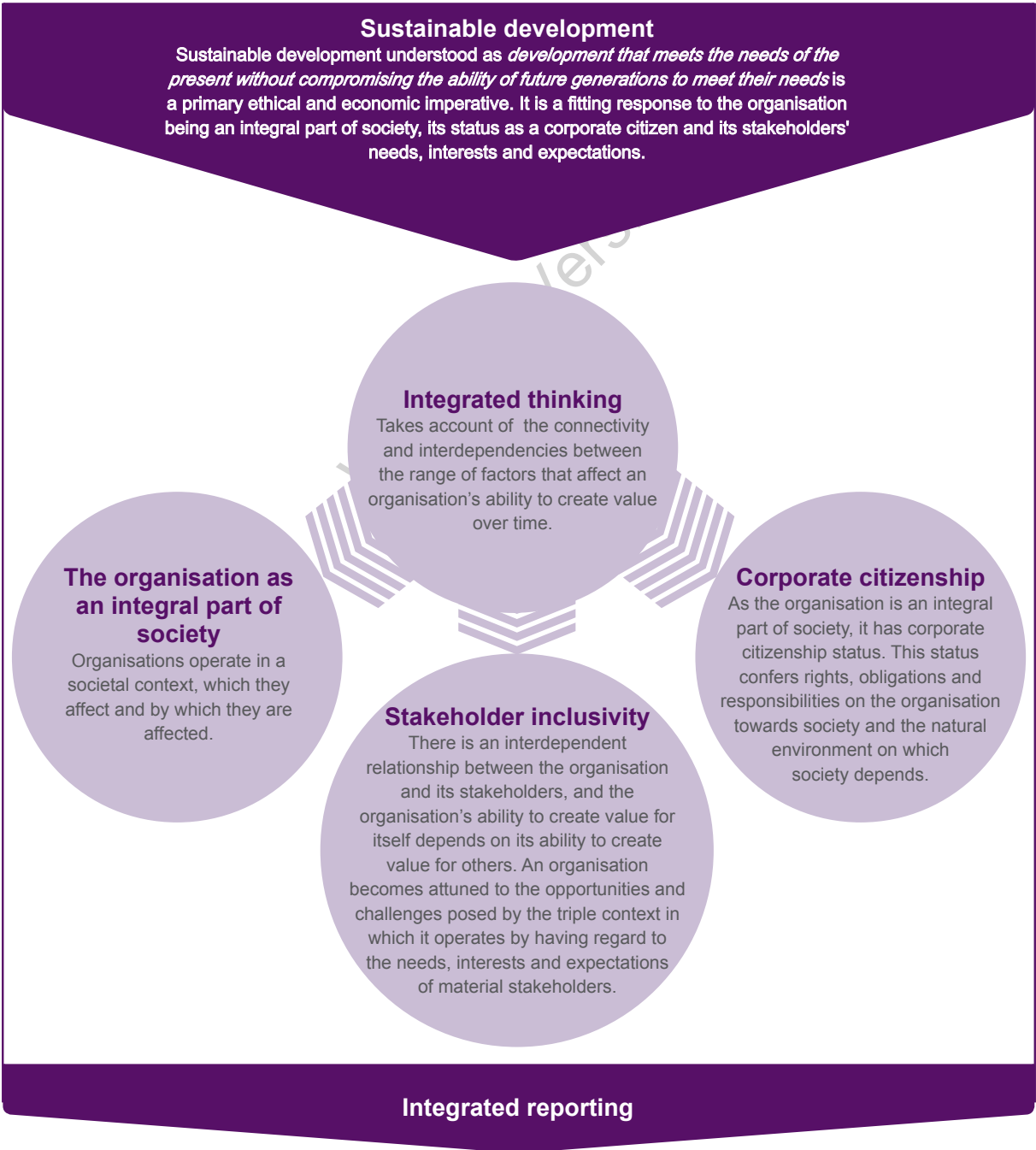
### OBJECTIVES OF KING IV

King IV's objectives are to:

- Promote corporate governance as integral to running an organisation and delivering governance outcomes such as an ethical culture, good performance, effective control and legitimacy.
- Broaden the acceptance of the King IV by making it accessible and fit for implementation across a variety of sectors and organisational types.
- Reinforce corporate governance as a holistic and interrelated set of arrangements to be understood and implemented in an integrated manner.
- Encourage transparent and meaningful reporting to stakeholders.
- Present corporate governance as concerned with not only structure and process, but also with an ethical consciousness and conduct.

# THE UNDERPINNING PHILOSOPHIES OF KING IV

Although King IV does not represent a significant departure from the philosophical underpinnings of King III, concepts have developed and been refined. The concepts used in King IV are depicted below.



# FUNDAMENTAL CONCEPTS CONTINUED

## Integrated thinking

King IV advocates integrated thinking which takes account of the connectivity and interdependencies between the range of factors that affect an organisation's ability to create value over time. Integrated thinking underpins all of the following:

- seeing the organisation as an integral part of society and thus as a corporate citizen;
- the stakeholder-inclusive approach;
- sustainable development; and
- integrated reporting.

## The organisation as an integral part of society

Organisations operate in a societal context which they affect and by which they are affected.

An organisation has a society specific to itself, which includes its internal and external stakeholders with a material stake in its activities. But the organisation is also a juristic person in the broader society in which it operates. Organisations are dependent on this broader society to, for instance, provide a conducive operating environment, a viable customer base and the skills that the organisation requires. In turn, organisations contribute to the broader society as creators of wealth; providers of goods, services and employment; contributors to the fiscus; and developers of human capital.

This idea of interdependency between organisations and society is supported by the African concept of *Ubuntu* or *Botho*, captured by the expressions *uMuntu ngumuntu ngabantu* and *Motho ke motho ka batho* – I am because you are; you are because we are. *Ubuntu* and *Botho* imply that there should be a common purpose to all human endeavours (including corporate endeavours) which is based on service to humanity.

As a logical consequence of this interdependency, one person benefits by serving another. This is also true for a juristic person, which benefits itself by serving its own society of internal and external stakeholders, as well as the broader society.

In line with this ethos, organisations should also take responsibility for the environmental outcomes of their activities and outputs, as those affect society as a whole.

## TRIPLE CONTEXT AND THE SIX CAPITALS

King IV refers to the '**triple context**' or the combined context of the economy, society and environment in which the organisation operates. The reference in King IV to 'context' is in the singular as these three dimensions are intertwined and should be viewed as an integrated whole.

The triple context is portrayed in more granular fashion by the forms of capital that the organisation uses or affects. The '**six-capitals**' model, identifies financial, manufactured, intellectual, human, social and relationship, and natural capitals. The model proposes these six forms of capital, but it is at the discretion of each organisation to identify the important physical and intangible resources that it uses or affects.

The triple context and the six capitals are concepts which are used in King IV as alternative lenses. Both are pathways to integrated thinking and sustainable development.

In King IV, the choice to use either concept is dictated by its setting but generally, triple context is used to denote the combined external environment in which the organisation operates, while six capitals is used when a more detailed or nuanced perspective is recommended.

## Corporate citizenship

As the organisation is an integral part of society, it has corporate citizenship status. This status confers rights, obligations and responsibilities on the organisation towards society and the natural environment on which society depends. The notion of corporate citizenship recognises that the organisation is licensed to operate by its internal and external stakeholders, and by society in the broad sense.

The Companies Act also reflects the company having obligations to society. For example, it states in section 7 that the purposes of the act include to “promote compliance with the Bill of Rights as provided for in the Constitution” and it “reaffirms the concept of the company as a means of achieving economic and social benefits”. Further support for the idea of corporate citizenship is offered by the obligation in the Companies Act for certain companies to establish a social and ethics committee.

## Stakeholder-inclusive approach

There is an interdependent relationship between the organisation and its stakeholders, and the organisation’s ability to create value for itself depends on its ability to create value for others.<sup>2</sup> An organisation becomes attuned to the opportunities and challenges posed by the triple context in which it operates by having regard to the needs, interests and expectations of material stakeholders. When using the six capitals model as an alternative lens, it is evident that each of the forms of capital has one or more stakeholders with an interest in it.<sup>3</sup>

King IV (like its predecessors) advocates a stakeholder-inclusive approach, in which the governing body takes account of the legitimate and reasonable needs, interests and expectations of all material stakeholders in the execution of its duties in the best interests of the organisation over time. By following this approach, instead of prioritising the interests of the providers of financial capital, the governing body gives parity to all sources of value creation, including among others, social and relationship capital as embodied by stakeholders.

Stakeholder inclusivity involves the balancing of interests over time by way of prioritising and, in some instances, trading off interests. A decision on how to achieve this balance is made on a case-by-case basis as current circumstances and exigencies require, but should always be done in the best interests of the organisation over the longer term. Balancing the needs, interests and expectations of stakeholders is a dynamic and ongoing process. The quality of stakeholder relationships indicates how effectively an organisation is able to strike this balance in making its decisions.

Part 5.5 in the King IV Code contains the principles and practices that deal with relationships in accordance with the stakeholder-inclusive approach.

<sup>2</sup> The International Integrated Reporting Council, *The International <IR> Framework*, (13 December 2013), p 10, available at <http://integratedreporting.org/resource/international-ir-framework/>

<sup>3</sup> Robert G. Eccles and Tim Youmans, “Materiality in Corporate Governance: The Statement of Significant Audiences and Materiality”, *Harvard Business School, Working Paper 16 – 023*, September 3, 2015

## FUNDAMENTAL CONCEPTS CONTINUED

### Shareholders, members and the stakeholder-inclusive approach

Adopting the stakeholder-inclusive approach means that the best interests of the company are not necessarily always equated to the best interests of shareholders. It also means that shareholders do not necessarily have a predetermined precedence over other stakeholders. Consequently, this is an inclusive, stakeholder-centric approach that stands in contrast to a shareholder-centric approach. Stakeholder inclusivity means that the board considers other stakeholders not merely as instruments to serve the interests of shareholders, but as having intrinsic value for decision-making in the best interests of the company over time.

The position taken in King IV is that, “directors owe their duties to the company and the company alone as the company is a separate legal entity from the moment it is registered until it is deregistered... The company is represented by several interests and these include the interests of shareholders, employees, consumers, the community and the environment. Thus requiring directors to act in good faith in the interest of ‘the company’ cannot nowadays mean anything other than a blend of all these interests, but first and foremost they must act in the best interest of the company as separate legal entity... An interest that may be primary at one particular point in time in the company’s existence may well become secondary at a later stage”<sup>4</sup>.

The interests of shareholders and stakeholders are interdependent; thus, following a stakeholder-inclusive approach maximises this symbiosis to promote the company’s long-term sustainability.

The above position is put forward in respect of companies, but also applies to other organisations, including retirement funds and non-profit organisations. Those charged with governance duties in these organisations should similarly recognise the interdependent nature of the relationship between members and other stakeholders and its consequences for decision-making in the best interests of the organisation over time.

### Sustainable development

Sustainable development, understood as “development that meets the needs of the present without compromising the ability of future generations to meet their needs”<sup>5</sup>, is a primary ethical and economic imperative. It is a fitting response to the organisation being an integral part of society, its status as a corporate citizen and its stakeholders’ needs interests and expectations.

The survival and success of organisations are intertwined with, and related to, three interdependent sub-systems: the triple context of the economy, society and the natural environment. In the South African setting, addressing inequality in society through economic transformation is a good example of a challenge that affects all three these sub-systems in which organisations operate.

Organisations and their leadership need to intentionally interact with, and respond to, the challenges and opportunities presented by the dynamic system of the triple context in which it operates and the capitals that the organisation uses and affects, with the aim to achieve the creation of value over time. Such an integrated approach is a hallmark of sustainable development and it is for this reason that the organisation’s core purpose, its risks and opportunities, strategy, business model, performance and sustainability are presented in King IV as inseparable elements of the value creation process.

<sup>4</sup> Esser I, Du Plessis JJ, “The Stakeholder Debate and Directors’ Fiduciary Duties”, SA Merc LJ 346-36, p360, 2007 (19) . See also Esser I, Delpont PA “Shareholder protection philosophy in terms of the Companies Act 71 of 2008 THRHR 2016 (79), p 1–29 where the authors state: “It is our view that the inclusive approach should be followed in interpreting section 76(3)(b). As mentioned above, in terms of the inclusive approach, directors must consider the interests of various stakeholders on a case-by-case basis. In the end the decision must be in the best interests of the company, even if it is to the detriment of the shareholders.”

<sup>5</sup> United Nations, “Report of the World Commission on Environment and Development: Our Common Future”, (Oxford, Great Britain: Oxford University Press, 1987), p 8. Also known as the Brundtland Report after Gro Harlem Brundtland, Chairman of the Commission and available at <http://www.un-documents.net/our-common-future.pdf>

## DISTINGUISHING FEATURES OF KING IV

The following are the features of King IV that distinguish it from its predecessors:

- King IV advocates an outcomes-based approach. Achieving the principles, and therefore ultimately good governance, optimises the organisation to realise the intended governance outcomes: ethical culture, good performance, effective control and legitimacy. (Refer to Part 3: *King IV Application and Disclosure* for further explanation and to Part 4: *King IV on a Page*.)
- Clear differentiation is made between principles and practices. Principles are achieved by mindful consideration and application of the recommended practices. (Refer to Part 3: *King IV Application and Disclosure* for further explanation.)
- King IV has been designed and drafted to make it more accessible to users, and also to reinforce governance as a holistic and integrated set of arrangements. (Refer to Part 4: *King IV on a Page* as a demonstration of this point.)
- Broader forms of address are used in King IV, namely “organisations”, “governing body” and “those charged with governance duties”.
- Supplements are provided to help organisations across a variety sectors and organisational types to interpret and implement King IV as is suited to their particular circumstances. (Refer to Part 6: *Sector Supplements*.)
- King IV provides guidance on how to apply the recommended practices proportionally in line with the organisation’s size and resources, and extent and complexity of the organisation’s activities. (Refer to Part 3: *King IV Application and Disclosure* for more guidance on proportionality.)
- To balance the less prescriptive approach adopted in King IV, there is greater emphasis on transparency with regards to how judgement was exercised when considering the practice recommendations contained in King IV. To reinforce this qualitative application of its principles and practices, King IV proposes an “apply and explain” regime, in contrast to “apply or explain” in King III. (Refer to Part 3: *King IV Application and Disclosure* for more detail and guidance on the application regime of King IV.)

# FUNDAMENTAL CONCEPTS CONTINUED

## HIGHLIGHTS OF THE KING IV CODE

The following is a summary of how emerging issues and corporate governance developments since the issue of King III in 2009 are addressed in the principles and practices contained in the Code. It also highlights specific areas of focus and some of the differences between King III and King IV.

### Integrated reporting

The notion of integrated reporting was introduced in King III, but the understanding of it has significantly evolved since then. Integrated reporting is an outcome of integrated thinking and is presented as such in King IV. Reporting, including integrated reporting, is dealt with in Part 5.2 of the Code, where it is positioned as the culmination of a series of leadership responsibilities executed by the governing body. The governing body steers and sets the direction of the organisation, approves policy and planning, oversees and monitors management and then, finally, provides for accountability on organisational performance through, among others, reporting and disclosure.

In order to clarify the standing of the integrated report in relation to other reports, King IV deals with it as one of the many reports that may be issued by the organisation, as is necessary, to comply with legal requirements, and/or to meet the particular information needs of material stakeholders. These other reports include the financial statements, the sustainability report, the social and ethics committee report, or other online or printed information or reports.

An integrated report could be a standalone report which connects the more detailed information in other reports and which addresses, at a high level and in a complete, concise way, the matters that could significantly affect the organisation's ability to create value. It could also be a distinguishable, prominent and accessible part of another report which also includes the financial statements and other reports issued in compliance with legal requirements.<sup>6</sup>

When drafting King IV, reliance was placed on the International <IR> Framework as issued by the International Integrated Reporting Council<sup>7</sup>. The Integrated Reporting Committee of South Africa<sup>8</sup> has endorsed the International <IR> Framework as good practice on how to prepare an integrated report and the committee's further guidance on integrated reporting should be followed.

### Balanced composition of governing bodies and independence

Having members of the governing body who are independent in appearance is an essential element in most governance codes. King IV seeks to contextualise the relevance of independence correctly, namely that:

- All members of the governing body, whether they are categorised as executive, non-executive or independent non-executive have, as a matter of law, a duty to act with independence of mind in the best interests of the organisation.
- Although important, independence in appearance is but one consideration in achieving balance in the composition of the governing body.

The overriding concern (as reflected by Principle 7 which deals with the composition of the governing body) is whether the governing body is knowledgeable, skilled, experienced, diverse and independent enough to discharge fully its governance role and responsibilities.

The need for the governing body to set and disclose progress towards targets for race and gender diversity has specifically been included in the Code.

<sup>6</sup> Integrated Reporting SA available at <http://www.integratedreportingsa.org/Home/Theoctopusmodel.aspx>

<sup>7</sup> The International Integrated Reporting Council, *The International <IR> Framework* (13 December 2013), available at <http://integratedreporting.org/resource/international-ir-framework/>

<sup>8</sup> Integrated Reporting SA available at [www.integratedreportingsa.org](http://www.integratedreportingsa.org)



## Delegation to management

The King IV Code provides for the governing body to delegate the implementation and execution of approved strategy, through policy and operational plans, to management via the chief executive officer (CEO). Rather than dealing with the establishment of specific management positions for functional areas as was done in King III, the practices in the King IV Code contain recommendations for the governing body to oversee that key functional areas are headed by competent individuals and are adequately resourced.

## Delegation to committees

King IV, like King III, deals with delegation by the governing body within its own structures. Principle 8 of King IV now clarifies the objectives for these delegation arrangements, which are to promote independent judgement; to assist with balance of power; and to assist with the effective discharge of its duties by the governing body.

In accordance with the drafting convention adopted for King IV, the recommended practices do not prescribe which committees should be established by the governing body – the governing body should judge what is appropriate for the organisation. The practices furthermore recommend that the allocation of roles and responsibilities, and the composition of committees, should be considered holistically. The aim here is to promote effective collaboration among committees with minimal overlap and fragmentation of duties, as well as a balanced distribution of power.

## Corporate governance services to the governing body

Rather than dealing with the office of the company secretary in isolation, the premise of the King IV Code is that the governing body should ensure that it has access to professional and independent guidance on corporate governance. For most companies, this will be provided by the company secretary. The Code recommends that even those companies and other organisations not obliged to appoint a company secretary should, as a matter of leading practice, consider appointing a company secretary or other professional to provide such services to the governing body.

## Performance evaluations of the governing body

King III recommended that an evaluation of the governing body, its committees and its individual members be conducted every year. To provide for sufficient time to appropriately respond to the results of such performance evaluations, the King IV Code recommends for a formal evaluation process to be conducted at least every two years. Every alternate year, the governing body should schedule an opportunity for consideration, reflection and discussion of its performance.

## Social and ethics committees

Regulation 43 of the Companies Act was issued after King III and does not address the ethics role of the social and ethics committee beyond mentioning ethics in the name of the committee. King IV seeks to expand on this, and the role ascribed to the social and ethics committee is that of oversight and reporting on organisational ethics, responsible corporate citizenship, sustainable development and stakeholder relationships.

This role includes organisational ethics and cover the statutory duties, but the intent is to encourage leading practice by having the social and ethics committee progress beyond mere compliance to contribute to the creation of value. Accordingly, King IV urges organisations that are not legally required to establish a social and ethics committee, nevertheless to consider creating a structure that would achieve the aims of such a committee.

# FUNDAMENTAL CONCEPTS CONTINUED

## Social and ethics committees (continued)

King IV also recommends a higher standard for the composition of this committee than what is provided for in the Companies Act. The recommended practices thus include that a majority of the members should be non-executive members of the governing body so as to ensure that independent judgement is brought to bear.

## Risk and opportunity

The definition for risk used in King IV consists of three parts, namely *uncertainty* of events, the *likelihood* of such events occurring and their *effect*, both positive and negative.

King IV's understanding of risk thus balances the traditional, negative view of risk with one that recognises the potential opportunities inherent in some risks. Thus, an opportunity may present itself as the potential upside of a risk that could adversely affect the achievement of organisational objectives.

However, it is also recognised in King IV that opportunities do not always originate from the current risks of the organisation. This is particularly true of the strategic opportunities that should be considered when setting the organisation's strategic direction. Consideration of the risks associated with such strategic opportunities affect whether the opportunity will be captured by the organisation or not.

Due to the rising complexity of risk and hence the need to strengthen oversight, the King IV Code recommends that the risk committee comprises a majority of non-executive members of the governing body. This recommendation goes beyond what was required in King III.

## Technology and information

In King IV, cognisance had to be taken of the advances in technology that are revolutionising businesses and societies, and transforming products, services and business models. So profound are these effects that many believe they herald the dawn of a Fourth Industrial Revolution.

These advances happen quickly and can cause significant disruption, opportunities and risks. Organisations should strengthen the processes that help them to anticipate change and to respond by capturing new opportunities and managing emerging risks. The practices under Principle 12 are designed to assist the governing body to do so.

Information, like technology, is a growing source of competitive advantage for the enhancement of the intellectual capital of an organisation.

In King IV, it is recognised that information and technology overlap but are also distinct sources of value creation which pose individual risks and opportunities. It is to reinforce this distinction that this section in the King IV Code now refers to technology and information instead of information technology.

## Compliance

As in King III, the King IV Code recommends that those charged with governance should ensure that compliance is understood, not only as an obligation, but also as a source of rights and protection. A holistic view is needed on how applicable laws and non-binding rules, codes and standards relate to one another. This includes how corporate governance codes relate to applicable legislation.

The Code further recommends that governing bodies should ensure continual monitoring of the regulatory environment, and that developments are responded to as necessary.

## Remuneration

Many international regulators and institutional investors are paying additional attention to disclosure and voting on remuneration. King IV had to consider the appropriate means of dealing with these developments, taking into account that South Africa is a participant in the global investment market but with its own unique set of circumstances.

King IV aims to foster enhanced accountability on remuneration. One of the ways that it addresses this is by including more definitive disclosure requirements, among which, that remuneration should be disclosed in three parts, namely: a background statement; an overview of the remuneration policy; and an implementation report.

It also recommends that shareholders of companies be provided the opportunity to pass separate non-binding advisory votes on the policy and the implementation report. The remuneration policy should record the measures that the board commits to in the event that either the remuneration policy or the implementation report, or both have been voted against by 25% or more of the voting rights exercised by shareholders. The Code recommends that such measures should include engagement and addressing objections and concerns.

King IV furthermore recommends the use of performance measures that support positive outcomes across the triple context in which the organisation operates, and/or all the capitals that the organisation uses or affects. This is a departure from linking remuneration to financial performance only. In respect of executive remuneration, it is also recommended that an account be provided of the performance measures and targets used as a basis for awarding of variable remuneration.

An important introduction in King IV is that the remuneration of executive management should be fair and responsible in the context of overall employee remuneration. It should be disclosed how this has been addressed. This acknowledges the need to address the gap between the remuneration of executives and those at the lower end of the pay scale.

## Assurance and internal audit

King III introduced the combined assurance model, but this concept needed to evolve to become more useful and effective.

In King IV, the model assumes an understanding of assurance that goes beyond the technical definitions of assurance. A combined assurance model incorporates and optimises all assurance services and functions so that, taken as a whole, these enable an effective control environment; support the integrity of information used for internal decision-making by management, the governing body and its committees; and support the integrity of the organisation's external reports.

The King IV Code's recommendations do not prescribe the design of the model, but allow for the governing body to exercise its judgement in this regard.

Internal audit, as one of the assurance service providers to the organisation, remains pivotal to corporate governance. Its role has further evolved in recent years. It has become a trusted advisor that adds value by contributing insight into the activities of the organisation and, as a further enhancement, foresight. This is the ideal positioning that is envisaged for internal audit in King IV.

# FUNDAMENTAL CONCEPTS CONTINUED

## Auditor and audit requirements

Mandatory rotation of audit firms and mandatory tendering have been introduced in some jurisdictions in an attempt to reinforce auditor independence and audit quality. King IV leaves the consideration and decision on whether to implement either to the audit committee and governing body, subject to legal requirements. The Code, however, makes certain practice recommendations with regard to auditor independence, amongst them that the tenure of an audit firm needs to be disclosed.

Following the UK Corporate Governance Code<sup>9</sup> and in the interest of more informative reporting on the auditing process, King IV recommends that the audit committee discloses significant matters considered by it in relation to the annual financial statements and how these were addressed by the committee. This provides users of the financial statements with three different perspectives on the annual financial statements:

- The governing body's perspective in preparing the annual financial statements – particularly significant assumptions that the governing body had made.
- The perspective of the auditor on why certain areas were considered to be of most significance in the audit and how they were addressed in the audit.
- The audit committee's perspective on the matters it regarded as significant and how it discharged its responsibilities in relation to those.

In King IV it is also recommended that the audit committee discloses its views on audit quality with reference to audit quality indicators.

## Tax

Tax has become a complex matter with various dimensions. The governing body should be responsible for a tax policy that is compliant with the applicable laws, but that is also congruent with responsible corporate citizenship, and that takes account of reputational repercussions. Hence, responsible and transparent tax policy is put forward as a corporate citizenship considerations in King IV.

## Shareholder activism

When it comes to the quality of an organisation's application of voluntary codes of governance principles and practices, it is said that its stakeholders are the ultimate compliance officers. Shareholders, as a particular sub-set of stakeholders, have certain rights that are enshrined in company legislation and that strengthen their ability to hold boards of companies to account. By virtue of this ability, shareholders also have the power to serve as proxies for wider stakeholder interests.

Institutional investors (in turn a sub-set of shareholders), particularly, are extremely influential. The types of investment decisions they make and how they exercise their rights as shareholders, either reinforce or weaken good governance in the companies in which they invest.

Commensurate with the rights and influence that shareholders have, it should be considered that shareholders have no legal or fiduciary responsibilities to the companies in which they invest. Furthermore, shareholders are in many instances transient and have the right to vote on matters that may have a longer-term impact than what the period of their shareholding may be.

<sup>9</sup> The Financial Reporting Council Limited; UK Code on Corporate Governance, (April 2016), p 19, available at [www.frc.org.uk](http://www.frc.org.uk)

Institutional investors owe their fiduciary duty to members of retirement funds, their dependants and beneficiaries and this has certain consequences for how institutional investors should exercise their rights. The Freshfields Report<sup>10</sup> published in 2005 stated that “integrating ESG considerations into an investment analysis so as to more reliably predict financial performance is clearly permissible and is arguably required in all jurisdictions”. This is supported by regulation 28(2)(c)(ix) of the Pension Funds Act: “before making an investment in and while invested in an asset [the fund and its board must] consider any factor which may materially affect the sustainable long-term performance of the asset including, but not limited to, those of an environmental, social and governance character”. This is also the position put forward by the Code for Responsible Investing in South Africa (CRISA)<sup>11</sup> which states in its first principle that institutional investors “should incorporate sustainability considerations, including ESG issues, into their investment process as part of the delivery of superior risk-adjusted returns to the ultimate beneficiaries”.

In consideration of the rights, influence and legal duties that institutional investors have, as described above, King IV sets out in Principle 17 that the governing body of an institutional investor organisation should ensure that responsible investment is practiced by the organisation to promote the good governance and the creation of value by the companies in which it invests. Responsible investing principles and practices are set out in the CRISA<sup>12</sup>, which accord with the Principles on Responsible Investing<sup>13</sup> and the International Corporate Governance Network Global Stewardship Code<sup>14</sup>.

## Dispute resolution

Since alternative dispute resolution mechanisms were introduced formally in King III, resolving disputes effectively has gained increased importance in light of labour strike action becoming protracted and, in some cases, hostile. Relationships are a form of capital on which all organisations rely. A dispute resolution process should be regarded as an opportunity not only to resolve the dispute at hand, but also to maintain and enhance the social and relationship capital of an organisation.

As a result, King IV in Part 5.5 recommends that dispute-resolution mechanisms and associated processes be adopted and implemented as part of the overall management of stakeholder relationships.

10 Freshfields Bruckhaus Deringer; “A Legal Framework for the Integration of Environmental, Social and Governance Issues into Institutional Investment”, *UNEP Finance Initiative*, 2005, p 13 available at [www.unepfi.org/fileadmin/documents/freshfields\\_legal\\_resp\\_20051123.pdf](http://www.unepfi.org/fileadmin/documents/freshfields_legal_resp_20051123.pdf)

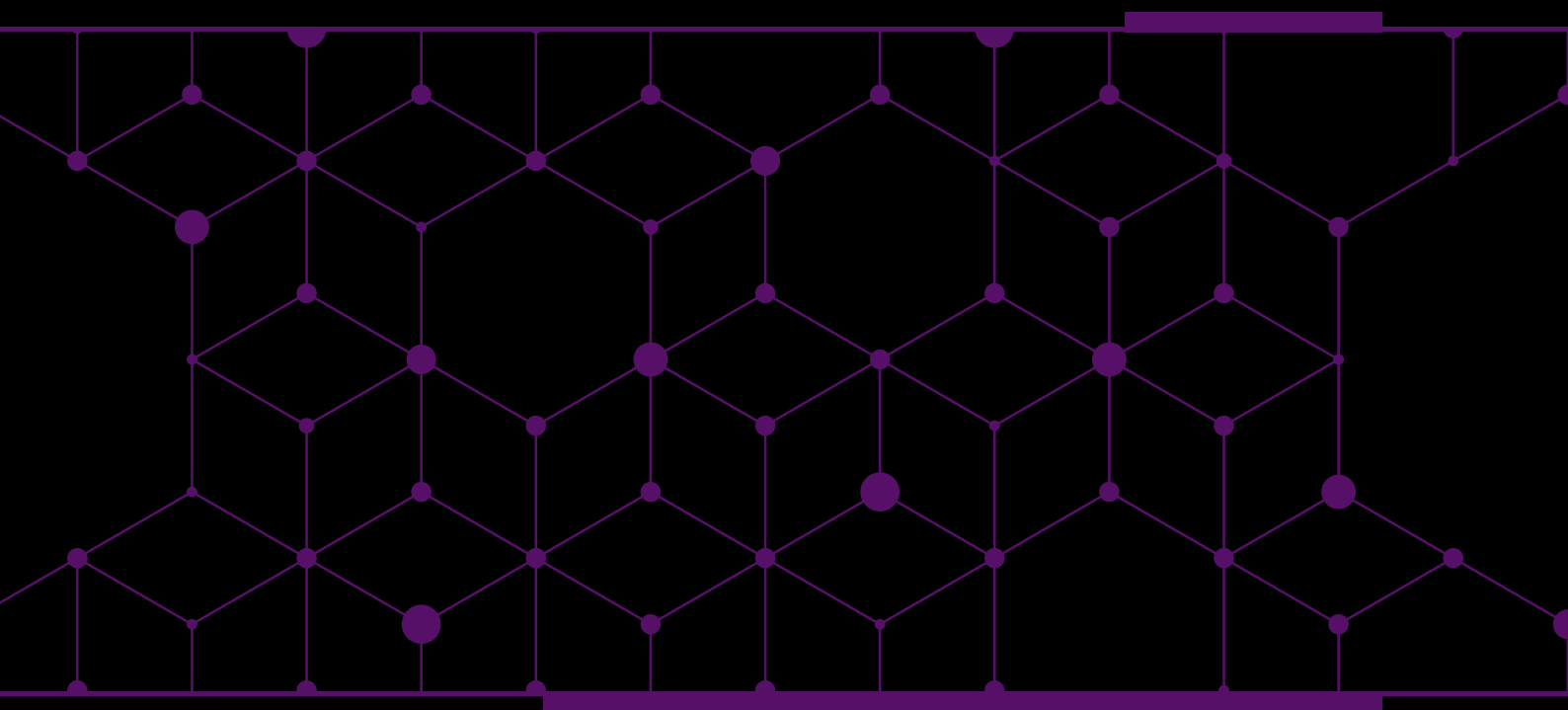
11 Committee for Responsible Investment in South Africa, *Code for Responsible Investment in South Africa* (Institute of Directors in Southern Africa, 2011), available at: [www.iodsa.co.za](http://www.iodsa.co.za)

12 Committee for Responsible Investment in South Africa, *Code for Responsible Investment in South Africa* (Institute of Directors in Southern Africa, 2011), available at: [www.iodsa.co.za](http://www.iodsa.co.za)

13 Principles for Responsible Investing available at: <https://www.unpri.org/about/the-six-principles>

14 International Corporate Governance Network, *International Corporate Governance Network Global Stewardship Code*, (2016), available at: <https://www.icgn.org/policy/stewardship-codes>

# PART 3



## KING IV APPLICATION AND DISCLOSURE



# » KING IV APPLICATION AND DISCLOSURE

## LEGAL STATUS OF KING IV

The legal status of King IV, as with its predecessors, is that of a set of voluntary principles and leading practices. Corporate governance could apply on a statutory basis as rules, as a voluntary code of principles and practices, or as a combination of the two. In South Africa, as in many jurisdictions around the world, a hybrid system of corporate governance has developed as, over time, some practices of good governance have been legislated in parallel with the voluntary King codes of governance. If there is a conflict between legislation and King IV, now or in the future, the law prevails.

There is an important argument against the mandatory “comply or else” framework: A one-size-fits-all approach cannot logically be suitable, because the types of businesses and activities carried out by organisations are so varied. There is also a danger that the governing body may become focused on mindless compliance instead of applying its mind to the best governance practice for the particular issue before it.

Good governance does not exist separately from the law, and a corporate governance code that applies on a voluntary basis may also trigger legal consequences. A court considers all relevant circumstances in determining the appropriate standard of conduct for those charged with governance duties, including what the generally accepted practices for a particular setting and situation are. Voluntary governance codes such as King IV recommend leading practices for how governance duties should be discharged, and therefore influence and affect what practices are considered and eventually adopted and implemented by governing bodies. The more widely certain recommended practices in codes of governance are adopted, the more likely it is that a court would regard conduct that conforms to these practices as meeting the required standard of care. In this way the provisions of voluntary codes of governance find their way into jurisprudence to become part of the common law. Consequently, failure to meet an established corporate governance practice, albeit not legislated, may invoke liability.

For directors of companies, adopting good corporate governance practice will be especially important if they were to rely on the protection afforded by the business judgement rule as provided for in the Companies Act in the course of litigation. In the absence of robust and sound governance structures and processes, it will be difficult, if not impossible, for a director to show that reasonably diligent steps have been taken to become informed; that material financial interests were absent or dealt with appropriately; and that there was a rational basis for believing – and that the director did believe – that a decision was in the best interests of the company.

## SCOPE OF APPLICATION OF KING IV

Codes of corporate governance are concerned with the role and responsibilities of the governing body and its interaction with management and other material stakeholders. The governing body is the focal point of corporate governance in an organisation, and hence the primary audience of King IV.

Furthermore, the King IV Report aspires to apply to all organisations, regardless of their form of incorporation. A main objective of the King IV Report is to broaden acceptance of corporate governance by making it accessible and fit for application across a variety of sectors and organisational types.

In pursuit of this goal, the King IV Report includes supplements for specific sectors. In addition, the Code itself has been drafted to be suitable for application by all organisations. This was done by phrasing principles and intended governance outcomes so that they embody the essence of the Code and can be applied with the necessary changes in terminology. The principles and intended outcomes being the essence, the practices can be then adapted and modified as suitable for the sector and in accordance with proportionality considerations as outlined below.

# KING IV APPLICATION AND DISCLOSURE CONTINUED

## PRACTICES, PRINCIPLES AND GOVERNANCE OUTCOMES

A major challenge in the implementation of codes of corporate governance is that recommended practices could be mindlessly implemented as if they were rules, resulting in corporate governance becoming a mere compliance burden. This inflexibility also leads to an inability to interpret and apply codes of corporate governance in a way that is appropriate for the organisation and the sector in which it operates. Mindful application, on the other hand, harnesses the benefits of corporate governance in the interests of the organisation and applying the governance code comes to be seen as a process of adding rather than subtracting value.

Understanding the relationship between governance outcomes, principles and practices as depicted below is key to mindful application of the King IV Code. It also supports one of the objectives of King IV, namely to reinforce corporate governance as a holistic and integrated set of arrangements.





## PROPORTIONALITY

Implementing King IV on a proportional basis means that the principles find application as they stand; they embody the aspirations of, and are fundamental to the journey towards good governance. The practices as recommended in the Code, however, are positioned at the level of leading practices, and may therefore not be suitable and appropriate for all organisations. Mindless compliance and a quantitative approach is not the aim. Instead, King IV strives to instil a qualitative approach in which recommended practices are implemented to achieve the principles and realise the intended governance outcomes.

Even where not expressly stated in the Code, practices are meant to be scaled in accordance with the following proportionality considerations particular to the organisation:

- Size of turnover and workforce.
- Resources.
- Extent and complexity of activities, including impact on the triple context in which it operates.

Application of practices on a proportional basis is subject to legal provisions and giving effect to the principle that the practices are associated with.

## DISCLOSURE ON APPLICATION OF KING IV

### King IV application regime

The application regime for King IV is “apply and explain”:

Apply principles	Explain practices
All principles are phrased as aspirations and ideals that organisations should strive for in their journey towards good governance and realising the governance outcomes. The principles are basic and fundamental to good governance, and application thereof is therefore assumed.	Explanation should be provided in the form of a narrative account, with reference to practices that demonstrate application of the principle. The explanation should address which recommended or other practices have been implemented, and how these achieve or give effect to the principle.

### What should be disclosed on the application of King IV?

Specific disclosure recommendations are included under each principle of the King IV Code. These recommendations are intended as guidance and a starting point for disclosure on the particular principle.

The detail of information to be provided in the narrative should be guided by materiality, and should enable stakeholders to make an informed assessment of the quality of the organisation’s governance.

There is no need to disclose whether each practice has been implemented or not, as this is quantitative and does not necessarily add to the quality of disclosure. There is also no need to disclose against the outcomes, as it can be left to the user to draw inferences from the narrative provided.

# KING IV APPLICATION AND DISCLOSURE CONTINUED

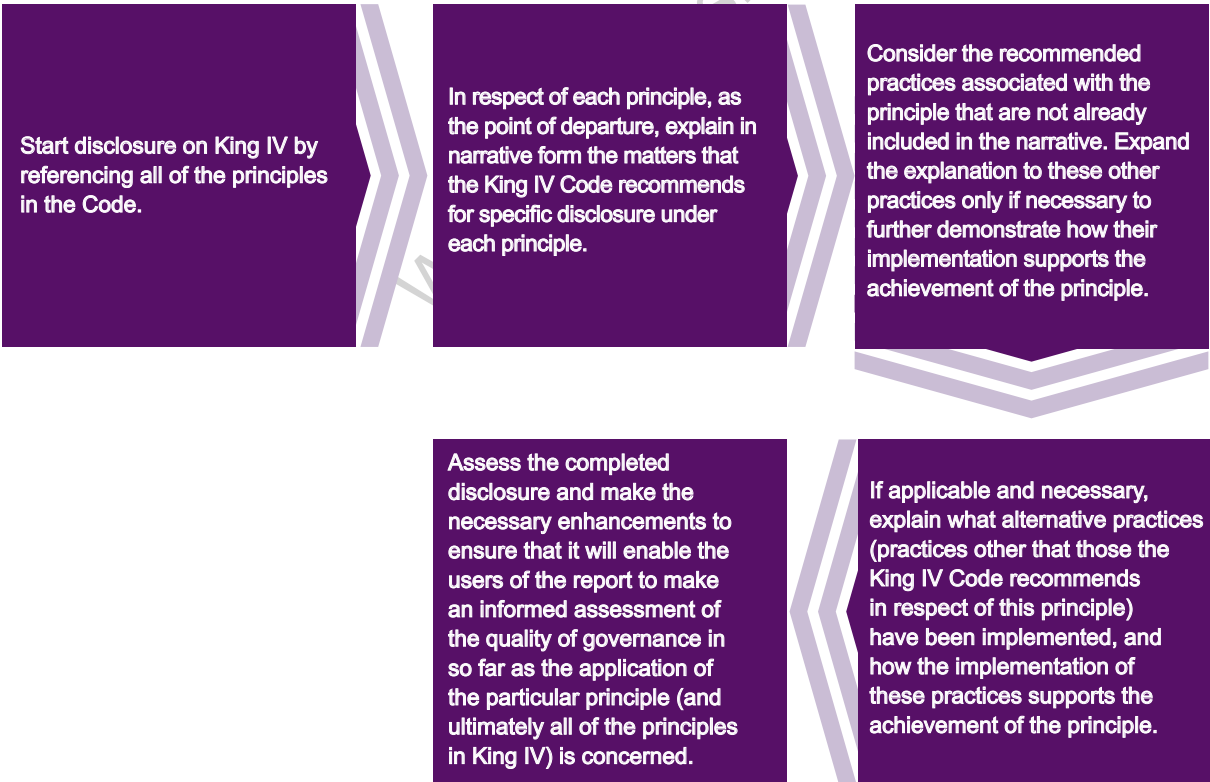
## Where should King IV disclosure be made?

The governing body has the discretion to determine where the King IV disclosures will be made; for example, in the integrated report, sustainability report, social and ethics committee report, or other online or printed information or reports.

The governing body may also choose to disclose its application of King IV in more than one of these reports. Duplication of King IV disclosures should be avoided by making use of cross-referencing. Group companies should also make use of cross-referencing to avoid duplicate disclosures.

King IV disclosure should be updated at least annually, formally approved by the governing body and be publicly accessible.

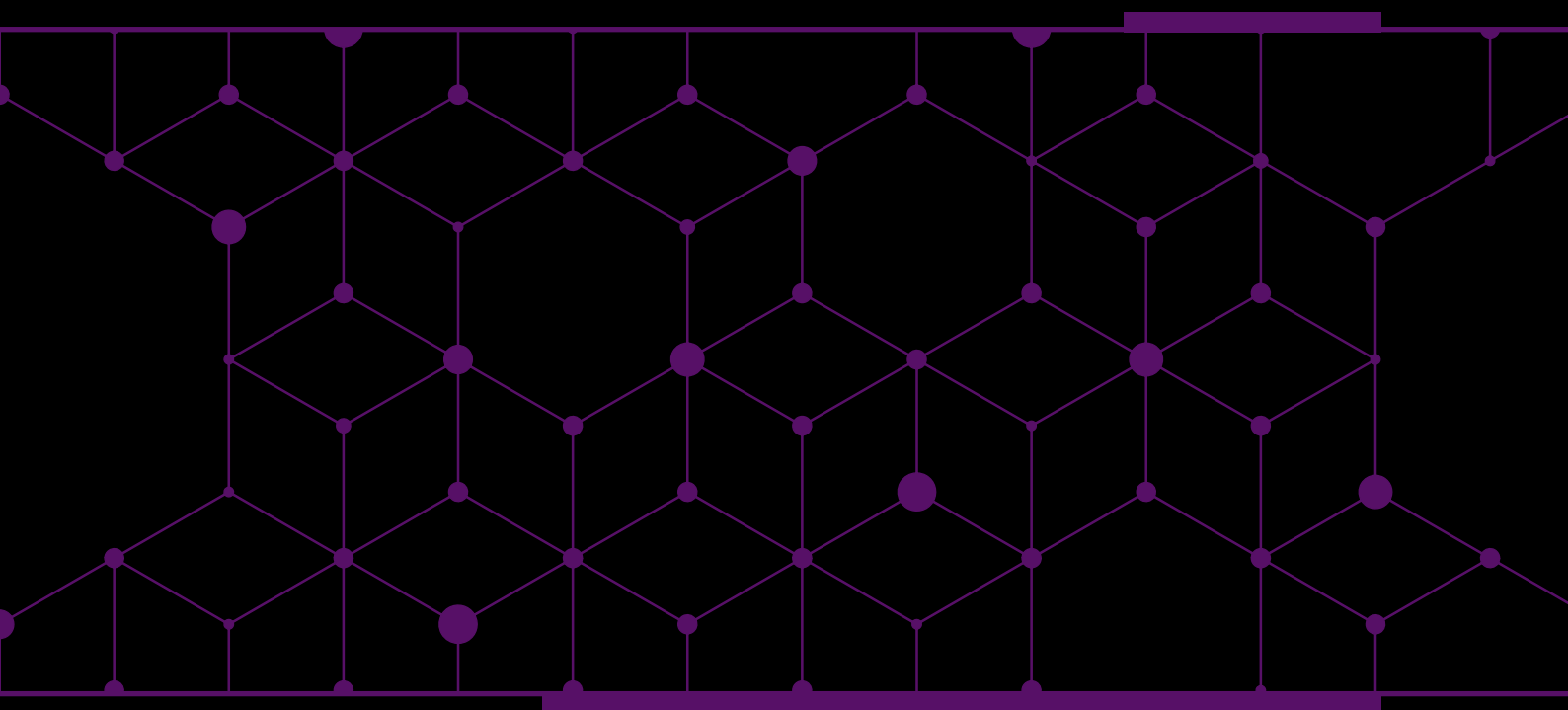
## Roadmap to disclosure on the application of King IV



## EFFECTIVE DATE

Disclosure on the application of King IV is effective in respect of financial years starting on or after 1 April 2017, but immediate transition is encouraged. King IV replaces King III in its entirety.

# PART 4



**KING IV ON A PAGE**

# » KING IV ON A PAGE

## LEADERSHIP BY THE GOVERNING BODY

These are the governing body's primary governance role and responsibilities.

Steers and sets strategic direction

Approves policy and planning

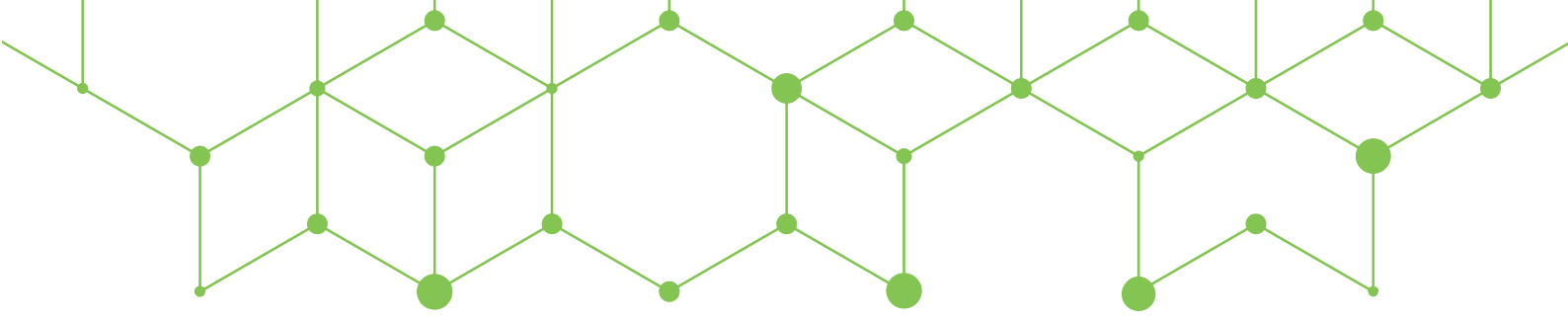
Oversees and monitors

Ensures accountability

## PRINCIPLES

Principles embody the aspirations of the journey towards good corporate governance.

- Principle 1: The governing body should lead ethically and effectively.
- Principle 2: The governing body should govern the ethics of the organisation in a way that supports the establishment of an ethical culture.
- Principle 3: The governing body should ensure that the organisation is and is seen to be a responsible corporate citizen.
- Principle 4: The governing body should appreciate that the organisation's core purpose, its risks and opportunities, strategy, business model, performance and sustainable development are all inseparable elements of the value creation process.
- Principle 5: The governing body should ensure that reports issued by the organisation enable stakeholders to make informed assessments of the organisation's performance and its short, medium and long-term prospects.
- Principle 6: The governing body should serve as the focal point and custodian of corporate governance in the organisation.
- Principle 7: The governing body should comprise the appropriate balance of knowledge, skills, experience, diversity and independence for it to discharge its governance role and responsibilities objectively and effectively.
- Principle 8: The governing body should ensure that its arrangements for delegation within its own structures promote independent judgement, and assist with balance of power and the effective discharge of its duties.
- Principle 9: The governing body should ensure that the evaluation of its own performance and that of its committees, its chair and its individual members, support continued improvement in its performance and effectiveness.



## PRINCIPLES

They guide on what organisations should strive to achieve by the application of governance practices.

- Principle 10:** The governing body should ensure that the appointment of, and delegation to, management contribute to role clarity and the effective exercise of authority and responsibilities.
- Principle 11:** The governing body should govern risk in a way that supports the organisation in setting and achieving its strategic objectives.
- Principle 12:** The governing body should govern technology and information in a way that supports the organisation setting and achieving its strategic objectives.
- Principle 13:** The governing body should govern compliance with applicable laws and adopted, non-binding rules, codes and standards in a way that supports the organisation being ethical and a good corporate citizen.
- Principle 14:** The governing body should ensure that the organisation remunerates fairly, responsibly and transparently so as to promote the achievement of strategic objectives and positive outcomes in the short, medium and long term.
- Principle 15:** The governing body should ensure that assurance services and functions enable an effective control environment, and that these support the integrity of information for internal decision-making and of the organisation's external reports.
- Principle 16:** In the execution of its governance role and responsibilities, the governing body should adopt a stakeholder-inclusive approach that balances the needs, interests and expectations of material stakeholders in the best interests of the organisation over time.
- Principle 17:** The governing body of an institutional investor organisation should ensure that responsible investment is practiced by the organisation to promote the good governance and the creation of value by the companies in which it invests.

Practices support and give effect to the principles.

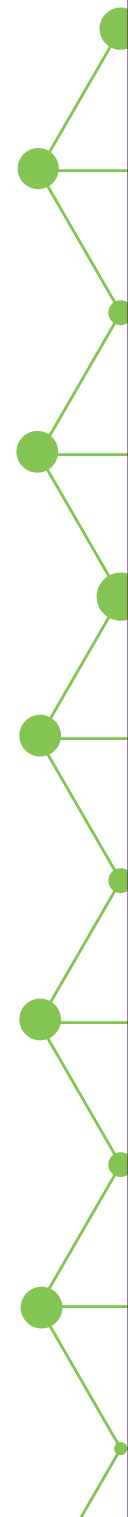


## PRACTICES

## GOVERNANCE OUTCOMES

These are the benefits that organisations could realise through good governance.

- Ethical culture
- Good performance
- Effective control
- Legitimacy



# PART 5



## KING IV CODE ON CORPORATE GOVERNANCE

**Part 5.1:** Leadership, ethics and corporate citizenship

**Part 5.2:** Strategy, performance and reporting

**Part 5.3:** Governing structures and delegation

**Part 5.4:** Governance functional areas

**Part 5.5:** Stakeholder relationships



Ethical culture

Good performance

Effective control

Legitimacy

# » KING IV CODE ON CORPORATE GOVERNANCE

## PART 5.1: LEADERSHIP, ETHICS AND CORPORATE CITIZENSHIP

### Leadership

Principle 1: The governing body should lead ethically and effectively.

#### RECOMMENDED PRACTICES

1. Members of the governing body should individually and collectively cultivate the following characteristics and exhibit them in their conduct:

**a. Integrity:**

- i. Members of the governing body must act in good faith and in the best interests of the organisation.
- ii. Members of the governing body should avoid conflicts of interest. In cases where a conflict cannot be avoided, it should be disclosed to the governing body in full at the earliest opportunity, and then proactively managed as determined by the governing body and subject to legal provisions.
- iii. Members of the governing body should act ethically beyond mere legal compliance.
- iv. Members of the governing body should set the tone for an ethical organisational culture.

**b. Competence:**

- i. Members of the governing body should take steps to ensure that they have sufficient working knowledge of the organisation, its industry, the triple context in which it operates, the capitals it uses and affects as well as of the key laws, rules, codes and standards applicable to the organisation.
- ii. Members of the governing body must act with due care, skill and diligence, and take reasonably diligent steps to become informed about matters for decision.
- iii. Members of the governing body should continuously develop their competence to lead effectively.

**c. Responsibility:**

- i. Members of the governing body should assume collective responsibility for steering and setting the direction of the organisation; approving policy and planning; overseeing and monitoring of implementation and execution by management; and ensuring accountability for organisational performance.
- ii. Members of the governing body should exercise courage in taking risks and capturing opportunities, but do so in a responsible manner and in the best interests of the organisation.
- iii. Members of the governing body should take responsibility for anticipating, preventing or otherwise ameliorating the negative outcomes of the organisation's activities and outputs on the triple context in which it operates, and the capitals that it uses and affects.
- iv. Members of the governing body should attend meetings of the governing body and its committees, and devote sufficient time and effort to prepare for those meetings.

**d. Accountability:**

Members of the governing body should be willing to answer for the execution of their responsibilities, even when these were delegated.

# KING IV CODE ON CORPORATE GOVERNANCE CONTINUED

## **e. Fairness:**

- i. Members of the governing body should adopt a stakeholder-inclusive approach in the execution of their governance role and responsibilities.
- ii. Members of the governing body should direct the organisation in such a way that it does not adversely affect the natural environment, society or future generations.

## **f. Transparency:**

Members of the governing body should be transparent in the manner in which they exercise their governance role and responsibilities.

2. The governing body should embody the above ethical characteristics in order to offer effective leadership that results in achieving strategic objectives and positive outcomes over time.
3. The arrangements by which the members of the governing body are being held to account for ethical and effective leadership should be disclosed. These arrangements would include, but are not limited to, codes of conduct and performance evaluations of the governing body and its members.

## **Organisational ethics**

Principle 2: The governing body should govern the ethics of the organisation in a way that supports the establishment of an ethical culture.

### **RECOMMENDED PRACTICES**

4. The governing body should assume responsibility for the governance of ethics by setting the direction for how ethics should be approached and addressed by the organisation.
5. The governing body should approve codes of conduct and ethics policies that articulate and give effect to its direction on organisational ethics.
6. The governing body should ensure that codes of conduct and ethics policies:
  - a. encompass the organisation's interaction with both internal and external stakeholders and the broader society; and
  - b. address the key ethical risks of the organisation.
7. The governing body should ensure that the codes of conduct and ethics policies provide for arrangements that familiarise employees and other stakeholders with the organisation's ethical standards. These arrangements should include:
  - a. publishing the organisation's codes of conduct and policies on the organisation's website, or on other platforms or through other media as is appropriate;
  - b. the incorporation by reference, or otherwise, of the relevant codes of conduct and policies in supplier and employee contracts; and
  - c. including the codes of conduct and ethics policies in employee induction and training programmes.
8. The governing body should delegate to management the responsibility for implementation and execution of the codes of conduct and ethics policies.





Ethical culture

Good performance

Effective control

Legitimacy

9. The governing body should exercise ongoing oversight of the management of ethics and, in particular, oversee that it results in the following:
  - a. Application of the organisation's ethical standards to the processes for the recruitment, evaluation of performance and reward of employees, as well as the sourcing of suppliers.
  - b. Having sanctions and remedies in place for when the organisation's ethical standards are breached.
  - c. The use of protected disclosure or whistle-blowing mechanisms to detect breaches of ethical standards and dealing with such disclosures appropriately.
  - d. The monitoring of adherence to the organisation's ethical standards by employees and other stakeholders through, among others, periodic independent assessments.
10. The following should be disclosed in relation to organisational ethics:
  - a. An overview of the arrangements for governing and managing ethics.
  - b. Key areas of focus during the reporting period.
  - c. Measures taken to monitor organisational ethics and how the outcomes were addressed.
  - d. Planned areas of future focus.

## Responsible corporate citizenship

Principle 3: The governing body should ensure that the organisation is and is seen to be a responsible corporate citizen.

### RECOMMENDED PRACTICES

11. The governing body should assume responsibility for corporate citizenship by setting the direction for how it should be approached and addressed by the organisation.
12. The governing body should ensure that the organisation's responsible corporate citizenship efforts include compliance with the Constitution of South Africa (including the Bill of Rights), the law, leading standards, and adherence to its own codes of conduct and policies.
13. The governing body should oversee that the organisation's core purpose and values, strategy and conduct are congruent with it being a responsible corporate citizen.
14. The governing body should oversee and monitor, on an ongoing basis, how the consequences of the organisation's activities and outputs affect its status as a responsible corporate citizen. This oversight and monitoring should be performed against measures and targets agreed with management in all of the following areas:
  - a. Workplace (including employment equity; fair remuneration; and the safety, health, dignity and development of employees).
  - b. Economy (including economic transformation; prevention, detection and response to fraud and corruption; and responsible and transparent tax policy).
  - c. Society (including public health and safety; consumer protection; community development; and protection of human rights).
  - d. Environment (including responsibilities in respect of pollution and waste disposal; and protection of biodiversity).

## KING IV CODE ON CORPORATE GOVERNANCE CONTINUED

15. The following should be disclosed in relation to corporate citizenship:

- a. An overview of the arrangements for governing and managing responsible corporate citizenship.
- b. Key areas of focus during the reporting period.
- c. Measures taken to monitor corporate citizenship and how the outcomes were addressed.
- d. Planned areas of future focus.

Website Version



Ethical culture

Good performance

Effective control

Legitimacy

## PART 5.2: STRATEGY, PERFORMANCE AND REPORTING

### Strategy and performance

Principle 4: The governing body should appreciate that the organisation's core purpose, its risks and opportunities, strategy, business model, performance and sustainable development are all inseparable elements of the value creation process.

#### RECOMMENDED PRACTICES

1. The governing body should assume responsibility for organisational performance by steering and setting the direction for the realisation of the organisation's core purpose and values through its strategy.
2. The governing body should delegate to management the formulation and development of the organisation's short, medium and long-term strategy.
3. The organisation's short, medium and long-term strategy as formulated and developed by management should be approved by the governing body. When considering the proposed strategy for approval, the governing body should challenge it constructively with reference to, among others, the following:
  - a. The timelines and parameters which determine the meaning of short, medium and long term respectively.
  - b. The risks, opportunities and other significant matters connected to the triple context in which the organisation operates.
  - c. The extent to which the proposed strategy depends on the resources and relationships connected to the various forms of capital.
  - d. The legitimate and reasonable needs, interests and expectations of material stakeholders.
  - e. The increase, decrease or transformation of the various forms of capitals that may result from the execution of the proposed strategy.
  - f. The interconnectivity and inter-dependence of all of the above.
4. The governing body should ensure that it approves the policies and operational plans developed by management to give effect to the approved strategy. These should include the key performance measures and targets for assessing the achievement of strategic objectives and positive outcomes over the short, medium and long term.
5. The governing body should delegate to management the responsibility to implement and execute the approved policies and operational plans.
6. The governing body should exercise ongoing oversight of the implementation of strategy and operational plans by management against agreed performance measures and targets.
7. The governing body should oversee that the organisation continually assesses, and responsibly responds to, the negative consequences of its activities and outputs on the triple context in which it operates, and the capitals which it uses and affects.
8. As part of its oversight of performance, the governing body should be alert to the general viability of the organisation with regard to its reliance and effects on the capitals, its solvency and liquidity, and its status as a going concern.

# KING IV CODE ON CORPORATE GOVERNANCE CONTINUED

In respect of disclosure on strategy and performance, refer to Reporting below.

## Reporting

**Principle 5:** The governing body should ensure that reports issued by the organisation enable stakeholders to make informed assessments of the organisation's performance, and its short, medium and long-term prospects.

### RECOMMENDED PRACTICES

9. The governing body should assume responsibility for the organisation's reporting by setting the direction for how it should be approached and conducted.
10. The governing body should approve management's determination of the reporting frameworks (including reporting standards) to be used, taking into account legal requirements and the intended audience and purpose of each report.
11. The governing body should oversee that reports such as the annual financial statements, sustainability reports, social and ethics committee reports, or other online or printed information or reports are issued, as is necessary, to comply with legal requirements, and/or to meet the legitimate and reasonable information needs of material stakeholders.
12. The governing body should oversee that the organisation issues an integrated report at least annually, which is either:
  - a. a standalone report which connects the more detailed information in other reports and addresses, at a high level and in a complete, concise way, the matters that could significantly affect the organisation's ability to create value; or
  - b. a distinguishable, prominent and accessible part of another report which also includes the annual financial statements and other reports that must be issued in compliance with legal provisions.
13. The governing body should approve management's bases for determining materiality for the purpose of deciding which information should be included in external reports.
14. The governing body should ensure the integrity of external reports as provided for in Part 5.4, Assurance of External Reports.
15. The governing body should oversee that the following information is published on the organisation's website, or on other platforms or through other media as is appropriate for access by stakeholders:
  - a. Corporate governance disclosures required in terms of this Code (refer to Part 3: *King IV Application and Disclosure* for more detail).
  - b. Integrated reports.
  - c. Annual financial statements and other external reports.



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## PART 5.3: GOVERNING STRUCTURES AND DELEGATION

### Primary role and responsibilities of the governing body

Principle 6: The governing body should serve as the focal point and custodian of corporate governance in the organisation.

#### RECOMMENDED PRACTICES

1. The governing body should exercise its leadership role by:
  - a. steering the organisation and setting its strategic direction;
  - b. approving policy and planning that give effect to the direction provided;
  - c. overseeing and monitoring of implementation and execution by management; and
  - d. ensuring accountability for organisational performance by means of, among others, reporting and disclosure.
2. The governing body should ensure that its role, responsibilities, membership requirements and procedural conduct are documented in a charter which it regularly reviews to guide its effective functioning.
3. The governing body should approve the protocol to be followed in the event that it or any of its members or committees need to obtain independent, external professional advice at the cost of the organisation on matters within the scope of their duties.
4. The governing body should approve the protocol to be followed by its non-executive members for requisitioning documentation from, and setting up meetings with, management.
5. The following should be disclosed in relation to the primary role and responsibilities of the governing body:
  - a. The number of meetings held during the reporting period, and attendance at those meetings.
  - b. Whether the governing body is satisfied that it has fulfilled its responsibilities in accordance with its charter for the reporting period.

# KING IV CODE ON CORPORATE GOVERNANCE CONTINUED

## Composition of the governing body

Principle 7: The governing body should comprise the appropriate balance of knowledge, skills, experience, diversity and independence for it to discharge its governance role and responsibilities objectively and effectively.

### RECOMMENDED PRACTICES

#### *Composition*

6. The governing body should assume responsibility for its composition by setting the direction and approving the processes for it to attain the appropriate balance of knowledge, skills, experience, diversity and independence to objectively and effectively discharge its governance role and responsibilities.
7. When determining the requisite number of members of the governing body, the following factors should be considered:
  - a. The appropriate mix of knowledge, skills and experience, including the business, commercial and industry experience, needed to govern the organisation.
  - b. The appropriate mix of executive, non-executive and independent non-executive members.
  - c. The need for a sufficient number of members that qualify to serve on the committees of the governing body.
  - d. The need to secure a quorum at meetings.
  - e. Regulatory requirements.
  - f. Diversity targets relating to the composition of the governing body.
8. The governing body should comprise a majority of non-executive members, most of whom should be independent.
9. As a minimum, the chief executive officer (CEO) and at least one other executive should be appointed to the governing body to ensure that it has more than one point of direct interaction with management. The executive other than the CEO appointed to the governing body may be the chief finance officer (CFO) or another designated executive as is appropriate for the organisation.
10. The governing body should promote diversity in its membership across a variety of attributes relevant for promoting better decision-making and effective governance, including field of knowledge, skills and experience as well as age, culture, race and gender.
11. The governing body should set targets for race and gender representation in its membership.
12. The governing body should establish arrangements for periodic, staggered rotation of its members so as to invigorate its capabilities by introducing members with new expertise and perspectives while retaining valuable knowledge, skills and experience and maintaining continuity.
13. The governing body should establish a succession plan for its membership which should include the identification, mentorship and development of future candidates.



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### ***Nomination, election and appointment of members to the governing body***

14. The nomination of candidates for election as members of the governing body should be approved by the governing body as a whole.
15. The processes for nomination, election and ultimately, the appointment of members to the governing body should be formal and transparent.
16. Before nominating a candidate for election, the governing body should consider the following:
  - a. The collective knowledge, skills and experience required by the governing body.
  - b. The diversity of the governing body.
  - c. Whether the candidate meets the appropriate fit and proper criteria.
17. Nomination for re-election of an incumbent of the governing body should be considered by the governing body on the basis of that member's performance, including attendance at meetings of the governing body and its committees.
18. A candidate for election as a non-executive member of the governing body should be requested to provide the governing body with details of professional commitments and a statement that confirms that the candidate has sufficient time available to fulfil the responsibilities as member of the governing body.
19. Prior to their nomination for election, candidates' backgrounds should be independently investigated, and their qualifications should be independently verified.
20. A brief professional profile of each candidate standing for election at the annual general meeting (AGM), including details of existing professional commitments, should accompany the notice of the AGM, together with a statement from the governing body confirming whether it supports the candidate's election or re-election.
21. Upon election, the terms and conditions for serving as a member of the governing body should be formalised in a letter of appointment.
22. The governing body should ensure that incoming members are inducted to enable them to make the maximum contribution within the shortest time possible.
23. Members of the governing body with no or limited governance experience should be provided with mentorship and encouraged to undergo training.
24. A programme of professional development and regular briefings on legal and corporate governance developments, and risks and changes in the external environment of the organisation, should be provided for members of the governing body.

### ***Independence and conflicts***

25. Subject to legal provisions, each member of the governing body should submit to the governing body a declaration of all financial, economic and other interests held by the member and related parties at least annually, or whenever there are significant changes.
26. At the beginning of each meeting of the governing body or its committees, all members should be required to declare whether any of them has any conflict of interest in respect of a matter on the agenda. Any such conflicts should be proactively managed as determined by the governing body and subject to legal provisions.
27. Non-executive members of the governing body may be categorised by the governing body as independent if it concludes that there is no interest, position, association or relationship which, when judged from the perspective of a reasonable and informed third party, is likely to influence unduly or cause bias in decision-making in the best interests of the organisation.

## KING IV CODE ON CORPORATE GOVERNANCE CONTINUED

28. The governing body should consider the following and other indicators holistically, and on a substance-over-form basis, when assessing the independence of a member of the governing body for purposes of categorisation. The member of the governing body:
- a. is a significant provider of financial capital, or ongoing funding to the organisation; or is an officer, employee or a representative of such provider of financial capital or funding;
  - b. if the organisation is a company, participates in a share-based incentive scheme offered by the company;
  - c. if the organisation is a company, owns securities in the company, the value of which is material to the personal wealth of the director;
  - d. has been in the employ of the organisation as an executive manager during the preceding three financial years, or is a related party to such executive manager;
  - e. has been the designated external auditor responsible for performing the statutory audit for the organisation, or a key member of the audit team of the external audit firm, during the preceding three financial years;
  - f. is a significant or ongoing professional adviser to the organisation, other than as a member of the governing body;
  - g. is a member of the governing body or the executive management of a significant customer of, or supplier to, the organisation;
  - h. is a member of the governing body or the executive management of another organisation which is a related party to the organisation; or
  - i. is entitled to remuneration contingent on the performance of the organisation.
29. A non-executive member of the governing body may continue to serve, in an independent capacity, for longer than nine years if, upon an assessment by the governing body conducted every year after nine years, it is concluded that the member exercises objective judgement and there is no interest, position, association or relationship which, when judged from the perspective of a reasonable and informed third party, is likely to influence unduly or cause bias in decision-making.
30. The following should be disclosed with regards to the composition of the governing body:
- a. Whether the governing body is satisfied that its composition reflects the appropriate mix of knowledge, skills, experience, diversity and independence.
  - b. The targets set for gender and race representation in the membership of the governing body, and progress made against these targets.
  - c. The categorisation of each member as executive or non-executive.
  - d. The categorisation of each non-executive member as independent or not and, when a non-executive member of the governing body has been serving for longer than nine years, a summary of the views of the governing body on the independence of the member.
  - e. The qualifications and experience of members.
  - f. Each member's period of service on the governing body.
  - g. The age of each member.
  - h. Other governing body and professional positions held by each member.
  - i. The reasons why any members of the governing body have been removed, resigned or retired.





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### ***Chair of the governing body***

31. The governing body should elect an independent non-executive member as chair to lead the governing body in the objective and effective discharge of its governance role and responsibilities.
32. The governing body should appoint an independent non-executive member as the lead independent to fulfil the following functions:
  - a. To lead in the absence of the chair.
  - b. To serve as a sounding board for the chair.
  - c. To act as an intermediary between the chair and other members of the governing body, if necessary.
  - d. To deal with shareholders' concerns where contact through the normal channels has failed to resolve concerns, or where such contact is inappropriate.
  - e. To strengthen independence on the governing body if the chair is not an independent non-executive member of the governing body.
  - f. To chair discussions and decision-making by the governing body on matters where the chair has a conflict of interest.
  - g. To lead the performance appraisal of the chair.
33. The chair's role, responsibilities and term in office, as well as that of the lead independent, should be documented in the charter of the governing body or elsewhere.
34. The CEO of the organisation should not also chair the governing body, and the retired CEO should not become the chair of the governing body until three complete years have passed after the end of the CEO's tenure.
35. In order to determine whether the chair is able to perform the duties of this office effectively, the chair, together with the governing body, should determine the number of outside professional positions that the chair is allowed to hold, taking into account the relative size and complexity of the organisations involved.
36. When determining which of its committees the chair of the governing body should serve on, either as member or chair, the governing body should consider how this affects the overall concentration and balance of power on the governing body. Generally, the following should apply:
  - a. The chair should not be a member of the audit committee.
  - b. The chair may be a member of the committee responsible for remuneration but should not be its chair.
  - c. The chair should be a member of the committee responsible for nominations of members of the governing body and may also be its chair.
  - d. The chair may be a member of the committee responsible for risk governance and may also be its chair.
  - e. The chair may be a member of the social and ethics committee but should not be its chair.
37. The governing body should ensure there is succession planning in place for the position of chair.
38. The following should be disclosed in relation to the chair:
  - a. Whether the chair is considered to be independent.
  - b. Whether or not an independent non-executive member of the governing body has been appointed as the lead independent, and the role and responsibilities assigned to the position.

# KING IV CODE ON CORPORATE GOVERNANCE CONTINUED

## Committees of the governing body

Principle 8: The governing body should ensure that its arrangements for delegation within its own structures promote independent judgement, and assist with balance of power and the effective discharge of its duties.

### RECOMMENDED PRACTICES

#### General

39. The governing body should determine if and when to delegate particular roles and responsibilities to an individual member or members of the governing body, or to standing or *ad hoc*-committees. The exercise of judgement by the governing body in this regard, is subject to legal requirements and should be guided by what is appropriate for the organisation and achieving the objectives of the delegation.
40. In the event that the governing body determines not to delegate all or some of the responsibilities dealt with in this Code as part of the responsibilities of a specific committee, the governing body should ensure that it fulfils those responsibilities itself.
41. Delegation to an individual member or members of the governing body should be recorded in writing and approved by the governing body. The record should set out the nature and extent of the responsibilities delegated, decision-making authority, the duration of the delegation, and the delegates' reporting responsibilities.
42. Delegation to committees should be recorded by means of a formal terms of reference that should be approved and reviewed annually by the governing body.
43. The terms of reference should, at a minimum, deal with the following:
  - a. The composition of the committee and, if applicable, the process and criteria for the appointment of any committee members who are not members of the governing body.
  - b. The committee's overall role and associated responsibilities and functions.
  - c. Delegated authority with respect to decision-making.
  - d. The tenure of the committee.
  - e. When and how the committee should report to the governing body and others.
  - f. The committee's access to resources and information.
  - g. The meeting procedures to be followed.
  - h. The arrangements for evaluating the committee's performance.
44. The governing body should consider the allocation of roles and associated responsibilities and the composition of membership across committees holistically, so as to achieve the following:
  - a. Effective collaboration through cross-membership between committees, where required; coordinated timing of meetings; and avoidance of duplication or fragmented functioning in so far as possible.
  - b. Where more than one committee has jurisdiction to deal with a similar matter, the specific role and positioning of each committee in relation to such matter are defined to ensure complementary rather than competing approaches.
  - c. A balanced distribution of power in respect of membership across committees, so that no individual has the ability to dominate decision-making, and no undue reliance is placed on any individual.



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45. The governing body should ensure that each committee, as a whole, has the necessary knowledge, skills, experience and capacity to execute its duties effectively.
46. Each committee should have a minimum of three members subject to legal provisions, where applicable.
47. Members of the executive and senior management should be invited to attend committee meetings either by standing invitation or on an *ad hoc*-basis to provide pertinent information and insights in their areas of responsibility.
48. Every member of the governing body is entitled to attend any committee meeting as an observer. However, unless that member is also a member of the committee, the member is not entitled to participate without the consent of the chair; does not have a vote; and is not entitled to fees for such attendance, unless payment of fees is agreed to by the governing body and shareholders.
49. Any delegation by the governing body of its responsibilities to a committee or a member of the governing body will not by or of itself constitute a discharge of the governing body's accountability. The governing body should apply its collective mind to the information, opinions, recommendations, reports and statements presented by the committee or the member.
50. The following should be disclosed in relation to each committee of the governing body:
  - a. Its overall role and associated responsibilities and functions.
  - b. Its composition, including each member's qualifications and experience.
  - c. Any external advisers or invitees who regularly attend committee meetings.
  - d. Key areas of focus during the reporting period.
  - e. The number of meetings held during the reporting period and attendance at those meetings.
  - f. Whether the committee is satisfied that it has fulfilled its responsibilities in accordance with its terms of reference for the reporting period.

#### **Audit committee**

51. The establishment of an audit committee is a statutory requirement for some organisations. As a matter of leading practice, the governing body of any organisation that issues audited financial statements should consider establishing an audit committee, the role of which should be to provide independent oversight of, among others:
  - a. the effectiveness of the organisation's assurance functions and services, with particular focus on combined assurance arrangements, including external assurance service providers, internal audit and the finance function; and
  - b. the integrity of the annual financial statements and, to the extent delegated by the governing body, other external reports issued by the organisation.
52. A statutory audit committee has the power to make decisions regarding its statutory duties, and is accountable for its performance in this regard. In addition to its statutory duties, the governing body may delegate other responsibilities to the audit committee, such as the approval of the annual financial statements, but the governing body remains ultimately accountable for such delegated responsibilities.
53. If the governing body delegates risk governance to the audit committee, the audit committee should satisfy itself that it dedicates sufficient time to this responsibility.
54. Whether or not the governance of risk is delegated to the audit committee, the audit committee should oversee the management of financial and other risks that affect the integrity of external reports issued by the organisation.

## KING IV CODE ON CORPORATE GOVERNANCE CONTINUED

55. The members of the audit committee should, as a whole, have the necessary financial literacy, skills and experience to execute their duties effectively.
56. All members of the audit committee should be independent, non-executive members of the governing body.
57. The governing body should appoint an independent, non-executive member to chair the audit committee.
58. The audit committee should meet annually with the internal and external auditors respectively, without management being present, to facilitate an exchange of views and concerns that may not be appropriate for discussion in an open forum.
59. In addition to required statutory disclosure and the disclosures recommended in paragraph 50, the following should also be disclosed in relation to the audit committee:
- a. A statement as to whether the audit committee is satisfied that the external auditor is independent of the organisation. The statement should specifically address:
    - i. the policy and controls that address the provision of non-audit services by the external auditor, and the nature and extent of such services rendered during the financial year;
    - ii. the tenure of the external audit firm and, in the event of the firm having been involved in a merger or acquisition, including the tenure of the predecessor firm;
    - iii. the rotation of the designated external audit partner; and
    - iv. significant changes in the management of the organisation during the external audit firm's tenure which may mitigate the attendant risk of familiarity between the external auditor and management.
  - b. Significant matters that the audit committee has considered in relation to the annual financial statements, and how these were addressed by the committee.
  - c. The audit committee's views on the quality of the external audit, with reference to audit quality indicators such as those that may be included in inspection reports issued by external audit regulators.
  - d. The audit committee's views on the effectiveness of the chief audit executive and the arrangements for internal audit.
  - e. The audit committee's views on the effectiveness of the design and implementation of internal financial controls, and on the nature and extent of any significant weaknesses in the design, implementation or execution of internal financial controls that resulted in material financial loss, fraud, corruption or error.
  - f. The audit committee's views on the effectiveness of the CFO and the finance function.
  - g. The arrangements in place for combined assurance and the committee's views on its effectiveness.

### ***Committee responsible for nominations of members of the governing body***

60. The governing body should consider allocating the oversight of the following to a dedicated committee, or adding it to the responsibilities of another committee as is appropriate for the organisation:
- a. The process for nominating, electing and appointing members of the governing body.
  - b. Succession planning in respect of governing body members.
  - c. Evaluation of the performance of the governing body.



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61. All members of the committee for nominations should be non-executive members of the governing body, and the majority should be independent.

Refer to paragraph 50 for the recommended disclosures in relation to the committee responsible for nominations.

***Committee responsible for risk governance***

62. The governing body should consider allocating the oversight of risk governance to a dedicated committee, or adding it to the responsibilities of another committee as is appropriate for the organisation.

63. If the committees for audit and risk are separate, the governing body should consider for one or more members to have joint membership of both committees for more effective functioning.

64. The committee for risk governance should have executive and non-executive members, with a majority being non-executive members of the governing body.

Refer to paragraph 50 for the recommended disclosures in relation to the committee responsible for risk.

***Committee responsible for remuneration***

65. The governing body should consider allocating oversight of remuneration to a dedicated committee, or adding it to the responsibilities of another committee as is appropriate for the organisation.

66. All members of the committee for remuneration should be non-executive members of the governing body, with the majority being independent non-executive members of the governing body.

67. The committee for remuneration should be chaired by an independent non-executive member.

Refer to paragraph 50 for the recommended disclosures in relation to the committee responsible for remuneration.

***Social and ethics committee***

68. For some companies, the establishment of a social and ethics committee is a statutory requirement. The governing body of any organisation not so obliged should consider allocating oversight of, and reporting on, organisational ethics, responsible corporate citizenship, sustainable development and stakeholder relationships to a dedicated committee, or adding it to the responsibilities of another committee as is appropriate for the organisation.

69. The responsibilities of the social and ethics committee should include its statutory duties (if applicable) and any other responsibilities delegated to it by the governing body.

70. The social and ethics committee should, subject to legal provisions, have executive and non-executive members, with a majority being non-executive members of the governing body.

Refer to paragraph 50 for the recommended disclosures in relation to the social and ethics committee.

# KING IV CODE ON CORPORATE GOVERNANCE CONTINUED

## Evaluations of the performance of the governing body

Principle 9: The governing body should ensure that the evaluation of its own performance and that of its committees, its chair and its individual members, support continued improvement in its performance and effectiveness.

### RECOMMENDED PRACTICES

71. The governing body should assume responsibility for the evaluation of its own performance and that of its committees, its chair and its individual members by determining how it should be approached and conducted.
72. The governing body should appoint an independent non-executive member to lead the evaluation of the chair's performance if a lead independent is not in place.
73. A formal process, either externally facilitated or not in accordance with methodology approved by the governing body, should be followed for evaluating the performance of the governing body, its committees, its chair and its individual members at least every two years.
74. Every alternate year, the governing body should schedule in its yearly work plan an opportunity for consideration, reflection and discussion of its performance and that of its committees, its chair and its members as a whole.
75. The following should be disclosed in relation to the evaluation of the performance of the governing body:
  - a. A description of the performance evaluations undertaken during the reporting period, including their scope, whether they were formal or informal, and whether they were externally facilitated or not.
  - b. An overview of the evaluation results and remedial actions taken.
  - c. Whether the governing body is satisfied that the evaluation process is improving its performance and effectiveness.

## Appointment and delegation to management

Principle 10: The governing body should ensure that the appointment of, and delegation to, management contribute to role clarity and the effective exercise of authority and responsibilities.

### RECOMMENDED PRACTICES

#### **CEO appointment and role**

76. The governing body should appoint the CEO.
77. The CEO should be responsible for leading the implementation and execution of approved strategy, policy and operational planning, and should serve as the chief link between management and the governing body.
78. The CEO should be accountable, and report to, the governing body.
79. The CEO should not be a member of the remuneration, audit or nomination committees, but should attend by invitation any meeting, or part thereof, if needed to contribute pertinent insights and information.



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80. The CEO and the governing body should agree on whether the CEO takes up additional professional positions, including membership of other governing bodies outside the organisation. Time constraints and potential conflicts of interest should be considered and balanced against the opportunity for professional development.
81. The governing body should satisfy itself that there is succession planning for the CEO position in place to provide continuity of executive leadership. Succession planning should be reviewed periodically, and should provide for both succession in emergency situations and succession over the longer term.
82. The governing body should formally evaluate the performance of the CEO against agreed performance measures and targets at least annually.
83. The following should be disclosed in relation to the CEO:
- The notice period stipulated in the CEO's employment contract and the contractual conditions related to termination.
  - Other professional commitments of the CEO, including membership of governing bodies outside the organisation.
  - Whether succession planning is in place for the CEO position.

#### **Delegation**

84. The governing body should set the direction and parameters for the powers which are to be reserved for itself, and those that are to be delegated to management via the CEO.
85. The governing body should approve a delegation of authority framework that articulates its set direction on reservation and delegation of power.
86. The governing body should ensure that the delegation of authority framework addresses the authority to appoint executives who will serve as *ex officio*-executive members of the governing body and to make other executive appointments.
87. The governing body should oversee that key management functions are:
- headed by an individual with the necessary competence and authority, and
  - adequately resourced.
88. The governing body should satisfy itself that there is succession planning in place for executive management and other key positions to provide continuity of leadership. Succession planning should be reviewed periodically, and provide for both succession in emergency situations and succession over the longer term.
89. A statement by the governing body on whether it is satisfied that the delegation of authority framework contributes to role clarity and the effective exercise of authority and responsibilities should be disclosed.

#### **Professional corporate governance services to the governing body**

90. The governing body should ensure that it has access to professional and independent guidance on corporate governance and its legal duties, and also that it has support to coordinate the functioning of the governing body and its committees.
91. For some companies, the appointment of a company secretary is a statutory requirement. In respect of those companies, the company secretary provides professional corporate governance services. The governing body of an organisation not so obliged should, as a matter of leading practice, consider appointing a company secretary or other professional, as is appropriate for the organisation, to provide professional corporate governance services to the governing body.

## KING IV CODE ON CORPORATE GOVERNANCE CONTINUED

92. The governing body should approve the arrangements for the provision of professional corporate governance services, including whether to outsource them to a juristic person, or to make a full-time or part-time appointment.
93. Regardless of the arrangements it has approved, the governing body should ensure that the office of the company secretary or other professional providing corporate governance services, is empowered and that the position carries the necessary authority.
94. The governing body should approve the appointment, including the employment contract and remuneration of the company secretary or other professional providing corporate governance services. The governing body should oversee that the person appointed has the necessary competence, gravitas and objectivity to provide independent guidance and support at the highest level of decision-making in the organisation.
95. The governing body should have primary responsibility for the removal of the company secretary or other professional providing corporate governance services.
96. The company secretary or other professional providing corporate governance services should have unfettered access to the governing body but, for reasons of independence, should maintain an arms-length relationship with it and its members; accordingly, the company secretary should not be a member of the governing body.
97. The company secretary or other professional providing corporate governance services should report to the governing body via the chair on all statutory duties and functions performed in connection with the governing body. Regarding other duties and administrative matters, the company secretary or other professional providing corporate governance services should report to the member of executive management designated for this purpose as is appropriate for the organisation.
98. The performance and independence of the company secretary or other professional providing corporate governance services should be evaluated at least annually by the governing body.
99. The arrangements in place for accessing professional corporate governance services and a statement on whether the governing body believes those arrangements are effective should be disclosed.





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## PART 5.4: GOVERNANCE FUNCTIONAL AREAS

### Risk governance

Principle 11: The governing body should govern risk in a way that supports the organisation in setting and achieving its strategic objectives.

#### RECOMMENDED PRACTICES

1. The governing body should assume responsibility for the governance of risk by setting the direction for how risk should be approached and addressed in the organisation. Risk governance should encompass both:
  - a. the opportunities and associated risks to be considered when developing strategy; and
  - b. the potential positive and negative effects of the same risks on the achievement of organisational objectives.
2. The governing body should treat risk as integral to the way it makes decisions and executes its duties.
3. The governing body should approve policy that articulates and gives effect to its set direction on risk.
4. The governing body should evaluate and agree the nature and extent of the risks that the organisation should be willing to take in pursuit of its strategic objectives. It should approve in particular:
  - a. the organisation's risk appetite, namely its propensity to take appropriate levels of risk; and
  - b. the limit of the potential loss that the organisation has the capacity to tolerate.
5. The governing body should delegate to management the responsibility to implement and execute effective risk management.
6. The governing body should exercise ongoing oversight of risk management and, in particular, oversee that it results in the following:
  - a. An assessment of risks and opportunities emanating from the triple context in which the organisation operates and the capitals that the organisation uses and affects.
  - b. An assessment of the potential upside, or opportunity, presented by risks with potentially negative effects on achieving organisational objectives.
  - c. An assessment of the organisation's dependence on resources and relationships as represented by the various forms of capital.
  - d. The design and implementation of appropriate risk responses.
  - e. The establishment and implementation of business continuity arrangements that allow the organisation to operate under conditions of volatility, and to withstand and recover from acute shocks.
  - f. The integration and embedding of risk management in the business activities and culture of the organisation.
7. The governing body should consider the need to receive periodic independent assurance on the effectiveness of risk management.
8. The nature and extent of the risks and opportunities the organisation is willing to take should be disclosed without compromising sensitive information.

# KING IV CODE ON CORPORATE GOVERNANCE CONTINUED

9. In addition, the following should be disclosed in relation to risk:
- a. An overview of the arrangements for governing and managing risk.
  - b. Key areas of focus during the reporting period, including objectives, the key risks that the organisation faces, as well as undue, unexpected or unusual risks and risks taken outside of risk tolerance levels.
  - c. Actions taken to monitor the effectiveness of risk management and how the outcomes were addressed.
  - d. Planned areas of future focus.

## Technology and information governance

Principle 12: The governing body should govern technology and information in a way that supports the organisation setting and achieving its strategic objectives.

### RECOMMENDED PRACTICES

10. The governing body should assume responsibility for the governance of technology and information by setting the direction for how technology and information should be approached and addressed in the organisation.
11. The governing body should approve policy that articulates and gives effect to its set direction on the employment of technology and information.
12. The governing body should delegate to management the responsibility to implement and execute effective technology and information management.
13. The governing body should exercise ongoing oversight of technology and information management and, in particular, oversee that it results in the following:
  - a. Integration of people, technologies, information and processes across the organisation.
  - b. Integration of technology and information risks into organisation-wide risk management.
  - c. Arrangements to provide for business resilience.
  - d. Proactive monitoring of intelligence to identify and respond to incidents, including cyber attacks and adverse social media events.
  - e. Management of the performance of, and the risks pertaining to, third-party and outsourced service providers.
  - f. The assessment of value delivered to the organisation through significant investments in technology and information, including the evaluation of projects throughout their life cycles and of significant operational expenditure.
  - g. The responsible disposal of obsolete technology and information in a way that has regard to environmental impact and information security.
  - h. Ethical and responsible use of technology and information.
  - i. Compliance with relevant laws.



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14. The governing body should exercise ongoing oversight of the management of information and, in particular, oversee that it results in the following:
  - a. The leveraging of information to sustain and enhance the organisation's intellectual capital.
  - b. An information architecture that supports confidentiality, integrity and availability of information.
  - c. The protection of privacy of personal information.
  - d. The continual monitoring of security of information.
15. The governing body should exercise ongoing oversight of the management of technology and, in particular, oversee that it results in the following:
  - a. A technology architecture that enables the achievement of strategic and operational objectives.
  - b. The management of the risks pertaining to the sourcing of technology.
  - c. Monitoring and appropriate responses to developments in technology, including the capturing of potential opportunities and the management of disruptive effects on the organisation and its business model.
16. The governing body should consider the need to receive periodic independent assurance on the effectiveness of the organisation's technology and information arrangements, including outsourced services.
17. The following should be disclosed in relation to technology and information:
  - a. An overview of the arrangements for governing and managing technology and information.
  - b. Key areas of focus during the reporting period, including objectives, significant changes in policy, significant acquisitions and remedial actions taken as a result of major incidents.
  - c. Actions taken to monitor the effectiveness of technology and information management and how the outcomes were addressed.
  - d. Planned areas of future focus.

## Compliance governance

**Principle 13:** The governing body should govern compliance with applicable laws and adopted, non-binding rules, codes and standards in a way that supports the organisation being ethical and a good corporate citizen.

### RECOMMENDED PRACTICES

18. The governing body should assume responsibility for the governance of compliance with applicable laws and adopted, non-binding rules, codes and standards by setting the direction for how compliance should be approached and addressed in the organisation.
19. The governing body should approve policy that articulates and gives effect to its direction on compliance, and that identifies which non-binding rules, codes and standards the organisation has adopted.

# KING IV CODE ON CORPORATE GOVERNANCE

## CONTINUED

20. The governing body should delegate to management responsibility for implementation and execution of effective compliance management.
21. The governing body should exercise ongoing oversight of compliance and, in particular, oversee that it results in the following:
  - a. Compliance being understood not only for the obligations it creates, but also for the rights and protections it affords.
  - b. Compliance management taking a holistic view of how applicable laws and non-binding rules, codes and standards relate to one another.
  - c. Continual monitoring of the regulatory environment and appropriate responses to changes and developments.
22. The governing body should consider the need to receive periodic independent assurance on the effectiveness of compliance management.
23. The following should be disclosed in relation to compliance:
  - a. An overview of the arrangements for governing and managing compliance.
  - b. Key areas of focus during the reporting period.
  - c. Actions taken to monitor the effectiveness of compliance management and how the outcomes were addressed.
  - d. Planned areas of future focus.
24. Material or repeated regulatory penalties, sanctions or fines for contraventions of, or non-compliance with, statutory obligations, whether imposed on the organisation or on members of the governing body or officers should be disclosed.
25. Details of monitoring and compliance inspections by environmental regulators, findings of non-compliance with environmental laws, or criminal sanctions and prosecutions for such non-compliance should be disclosed.

## Remuneration governance

**Principle 14:** The governing body should ensure that the organisation remunerates fairly, responsibly and transparently so as to promote the achievement of strategic objectives and positive outcomes in the short, medium and long term.

### RECOMMENDED PRACTICES

#### *Remuneration policy*

26. The governing body should assume responsibility for the governance of remuneration by setting the direction for how remuneration should be approached and addressed on an organisation-wide basis.
27. The governing body should approve policy that articulates and gives effect to its direction on fair, responsible and transparent remuneration.



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28. The remuneration policy should be designed to achieve the following objectives:
- To attract, motivate, reward and retain human capital.
  - To promote the achievement of strategic objectives within the organisation's risk appetite.
  - To promote positive outcomes.
  - To promote an ethical culture and responsible corporate citizenship.
29. The remuneration policy should address organisation-wide remuneration and include provision for the following specifically:
- Arrangements towards ensuring that the remuneration of executive management is fair and responsible in the context of overall employee remuneration in the organisation.
  - The use of performance measures that support positive outcomes across the economic, social and environmental context in which the organisation operates; and/or all the capitals that the organisation uses or affects.
  - If the organisation is a company, the voting by shareholders on the remuneration policy and implementation report, and for the implementation of related responding measures as outlined under Voting on Remuneration below.
30. All elements of remuneration that are offered in the organisation and the mix of these should be set out in the remuneration policy, including:
- base salary, including financial and non-financial benefits;
  - variable remuneration, including short and long-term incentives and deferrals;
  - payments on termination of employment or office;
  - sign-on, retention and restraint payments;
  - the provisions, if any, for pre-vesting forfeiture (*malus*) and post-vesting forfeiture (claw-back) of remuneration;
  - any commissions and allowances; and
  - the fees of non-executive members of the governing body.
31. The governing body should oversee that the implementation and execution of the remuneration policy achieves the objectives of the policy.

#### **Remuneration report**

32. The governing body should ensure that remuneration is disclosed by means of a remuneration report in three parts:
- A background statement.
  - An overview of the main provisions of the remuneration policy.
  - An implementation report which contains details of all remuneration awarded to individual members of the governing body and executive management during the reporting period.

# KING IV CODE ON CORPORATE GOVERNANCE

## CONTINUED

### *Background statement*

33. The background statement should briefly provide context for remuneration considerations and decisions, with reference to:
- a. internal and external factors that influenced remuneration;
  - b. the most recent results of voting on the remuneration policy and the implementation report and the measures taken in response thereto;
  - c. key areas of focus and key decisions taken by the remuneration committee during the reporting period, including any substantial changes to the remuneration policy;
  - d. whether remuneration consultants have been used, and whether the remuneration committee is satisfied that they were independent and objective;
  - e. the views of the remuneration committee on whether the remuneration policy achieved its stated objectives; and
  - f. future areas of focus.

### *Overview of remuneration policy*

34. The overview of the main provisions of the remuneration policy should address the objectives of the policy and the manner in which the policy seeks to accomplish these. The overview should include the following:
- a. The remuneration elements and design principles informing the remuneration arrangements for executive management and, at a high level, for other employees.
  - b. Details of any obligations in executive employment contracts which could give rise to payments on termination of employment or office.
  - c. A description of the framework and performance measures used to assess the achievement of strategic objectives and positive outcomes, including the relative weighting of each performance measure and the period of time over which it is measured.
  - d. An illustration of the potential consequences on the total remuneration for executive management, on a single, total figure basis, of applying the remuneration policy under minimum, on-target and maximum performance outcomes.
  - e. An explanation of how the policy addresses fair and responsible remuneration for executive management in the context of overall employee remuneration.
  - f. The use and justification of remuneration benchmarks.
  - g. The basis for the setting of fees for non-executive directors.
  - h. A reference to an electronic link to the full remuneration policy for public access.



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### *Implementation report*

35. The implementation report, which includes the remuneration disclosure in terms of the Companies Act, should reflect the following:
- a. The remuneration of each member of executive management, which should include in separate tables:
    - i. a single, total figure of remuneration, received and receivable for the reporting period, and all the remuneration elements that it comprises, each disclosed at fair value;
    - ii. the details of all awards made under variable remuneration incentive schemes in the current and prior years that have not yet vested, including the number of awards; the values at date of grant; their award, vesting and expiry dates (where applicable); and the fair value at the end of the reporting period; and
    - iii. the cash value of all awards made under variable remuneration incentive schemes that were settled during the reporting period.
  - b. An account of the performance measures used and the relative weighting of each, as a result of which awards under variable remuneration incentive schemes have been made, including: the targets set for the performance measures and the corresponding value of the award opportunity; and for each performance measure, how the organisation and executive managers, individually, performed against the set targets.
  - c. Separate disclosure of, and reasons for, any payments made on termination of employment or office.
  - d. A statement regarding compliance with, and any deviations from, the remuneration policy.

### ***Voting on remuneration (only applicable to companies)***

36. In terms of the Companies Act, fees for non-executive directors for their services as directors must be submitted for approval by special resolution by shareholders within the two years preceding payment.
37. The remuneration policy and the implementation report should be tabled every year for separate non-binding advisory votes by shareholders at the AGM.
38. The remuneration policy should record the measures that the board commits to take in the event that either the remuneration policy or the implementation report, or both have been voted against by 25% or more of the voting rights exercised. Such measures should provide for taking steps in good faith and with best reasonable effort towards the following at a minimum:
- a. An engagement process to ascertain the reasons for the dissenting votes.
  - b. Appropriately addressing legitimate and reasonable objections and concerns raised, which may include amending the remuneration policy, or clarifying or adjusting remuneration governance and/or processes.
39. In the event that either the remuneration policy or the implementation report, or both were voted against by 25% or more of the voting rights exercised, the following should be disclosed in the background statement of the remuneration report succeeding the voting:
- a. with whom the company engaged, and the manner and form of engagement to ascertain the reasons for dissenting votes; and
  - b. the nature of steps taken to address legitimate and reasonable objections and concerns.

# KING IV CODE ON CORPORATE GOVERNANCE CONTINUED

## Assurance

Principle 15: The governing body should ensure that assurance services and functions enable an effective control environment, and that these support the integrity of information for internal decision-making and of the organisation's external reports.

### RECOMMENDED PRACTICES

#### *Combined assurance*

40. The governing body should assume responsibility for assurance by setting the direction concerning the arrangements for assurance services and functions. The governing body should delegate to the audit committee, if in place, the responsibility for overseeing that those arrangements are effective in achieving the following objectives:
  - a. Enabling an effective internal control environment.
  - b. Supporting the integrity of information used for internal decision-making by management, the governing body and its committees.
  - c. Supporting the integrity of external reports.
41. The governing body should satisfy itself that a combined assurance model is applied which incorporates and optimises the various assurance services and functions so that, taken as a whole, these support the objectives for assurance.
42. The governing body should oversee that the combined assurance model is designed and implemented to cover effectively the organisation's significant risks and material matters through a combination of the following assurance service providers and functions as is appropriate for the organisation:
  - a. The organisation's line functions that own and manage risks.
  - b. The organisation's specialist functions that facilitate and oversee risk management and compliance.
  - c. Internal auditors, internal forensic fraud examiners and auditors, safety and process assessors, and statutory actuaries.
  - d. Independent external assurance service providers such as external auditors.
  - e. Other external assurance providers such as sustainability and environmental auditors, external actuaries, and external forensic fraud examiners and auditors.
  - f. Regulatory inspectors.
43. The governing body and its committees should assess the output of the organisation's combined assurance with objectivity and professional skepticism, and by applying an enquiring mind, form their own opinion on the integrity of information and reports, and the degree to which an effective control environment has been achieved.





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### **Assurance of external reports**

44. The governing body should assume responsibility for the integrity of external reports issued by the organisation by setting the direction for how assurance of these should be approached and addressed.
45. The governing body's direction in this regard should take into account legal requirements in relation to assurance, with the following additional considerations:
  - a. Whether assurance should be applied to the underlying data used to prepare a report, or to the process for preparing and presenting a report, or both.
  - b. Whether the nature, scope and extent of assurance are suited to the intended audience and purpose of a report.
  - c. The specification of applicable criteria for the measurement or evaluation of the underlying subject matter of the report.
46. The governing body should satisfy itself that the combined assurance model is effective and sufficiently robust for the governing body to be able to place reliance on the combined assurance underlying the statements that the governing body makes concerning the integrity of the organisation's external reports.
47. External reports should disclose information about the type of assurance process applied to each report, in addition to the independent, external audit opinions provided in terms of legal requirements. This information should include:
  - a. a brief description of the nature, scope and extent of the assurance functions, services and processes underlying the preparation and presentation of the report; and
  - b. a statement by the governing body on the integrity of the report and the basis for this statement, with reference to the assurance applied.

Refer to Part 5.3: *Audit committee* for recommended disclosures by the audit committee concerning the organisation's application of combined assurance.

### **Internal audit**

48. The governing body should assume responsibility for internal audit by setting the direction for the internal audit arrangements needed to provide objective and relevant assurance that contributes to the effectiveness of governance, risk management and control processes. The governing body should delegate oversight of internal audit to the audit committee, if in place.
49. The governing body should approve an internal audit charter that defines the role and associated responsibilities and authority of internal audit, including addressing its role within combined assurance and the internal audit standards to be adopted.
50. The governing body should ensure that the arrangements for internal audit provide for the necessary skills and resources to address the complexity and volume of risk faced by the organisation, and that internal audit is supplemented as required by specialist services such as those provided by forensic fraud examiners and auditors, safety and process assessors, and statutory actuaries.
51. If a chief audit executive (CAE) position is provided for in the arrangements for internal audit, the governing body should ensure that the position is set up to function independently from management who designs and implements the controls that are in place, and that the position carries the necessary authority.
52. The governing body should approve the appointment of the CAE, including the employment contract and remuneration of the CAE, and ensure that the person who fills the position has the necessary competence, gravitas and objectivity.

## KING IV CODE ON CORPORATE GOVERNANCE CONTINUED

53. For reasons of independence, the CAE should have access to the chair of the audit committee.
54. For reasons of independence, the CAE should not be a member of executive management, but should be invited to attend executive meetings, as necessary, to be informed about strategy and policy decisions and their implementation.
55. Where internal audit services are co-sourced or outsourced, the governing body should ensure that there is clarity on who fulfils the role of CAE.
56. The CAE should report to the chair of the audit committee on the performance of duties and functions that relate to internal audit. On other duties and administrative matters, the CAE should report to the member of executive management designated for this purpose as appropriate for the organisation.
57. The governing body should have primary responsibility for the removal of the CAE.
58. The governing body should monitor on an ongoing basis that internal audit:
- a. follows an approved risk-based internal audit plan; and
  - b. reviews the organisational risk profile regularly, and proposes adaptations to the internal audit plan accordingly.
59. The governing body should ensure that internal audit provides an overall statement annually as to the effectiveness of the organisation's governance, risk management and control processes.
60. The governing body should ensure that an external, independent quality review of the internal audit function is conducted at least once every five years.
61. The governing body should obtain confirmation annually from the CAE that internal audit conforms to a recognised industry code of ethics.

Refer to Part 5.3: *Audit committee* for recommended disclosures by the audit committee concerning internal audit arrangements and the internal control environment.



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## PART 5.5: STAKEHOLDER RELATIONSHIPS

### Stakeholders

Principle 16: In the execution of its governance role and responsibilities, the governing body should adopt a stakeholder-inclusive approach that balances the needs, interests and expectations of material stakeholders in the best interests of the organisation over time.

#### RECOMMENDED PRACTICES

##### *Stakeholder relationships*

1. The governing body should assume responsibility for the governance of stakeholder relationships by setting the direction for how stakeholder relationships should be approached and conducted in the organisation.
2. The governing body should approve policy that articulates and gives effect to its direction on stakeholder relationships.
3. The governing body should delegate to management the responsibility for implementation and execution of effective stakeholder relationship management.
4. The governing body should exercise ongoing oversight of stakeholder relationship management and, in particular, oversee that it results in the following:
  - a. Methodologies for identifying individual stakeholders and stakeholder groupings.
  - b. Determination of material stakeholders based on the extent to which they affect, or are affected by, the activities, outputs and outcomes of the organisation.
  - c. Management of stakeholder risk as an integral part of organisation-wide risk management.
  - d. Formal mechanisms for engagement and communication with stakeholders, including the use of dispute resolution mechanisms and associated processes.
  - e. Measurement of the quality of material stakeholder relationships, and appropriate responses to the outcomes.
5. The following should be disclosed in relation to stakeholder relationships:
  - a. An overview of the arrangements for governing and managing stakeholder relationships.
  - b. Key areas of focus during the reporting period.
  - c. Actions taken to monitor the effectiveness of stakeholder management and how the outcomes were addressed.
  - d. Future areas of focus.

# KING IV CODE ON CORPORATE GOVERNANCE CONTINUED

## **Shareholder relationships** *(Applicable to companies only)*

6. The board should oversee that the company encourages proactive engagement with shareholders, including engagement at the annual general meeting (AGM) of the company.
7. All directors should be available at the AGM to respond to shareholders' queries on how the board executed its governance duties.
8. The board should ensure that the designated partner of the external audit firm attends the AGM.
9. The board should ensure that shareholders are equitably treated, and that the interests of minority shareholders are adequately protected.
10. The minutes of the AGMs of listed companies should be made publicly available.

## **Relationships within a group of companies** *(Applicable to companies within a group)*

11. The board of the holding company should assume responsibility for governance across the group by setting the direction for how the relationships and exercise of power within the group should be approached and conducted.
12. The board should approve a group governance framework that articulates and gives effect to its direction on relationships and the exercise of authority across the group.
13. The adoption and implementation of the policies, structures and procedures of the holding company is a matter for consideration and approval by the board of the subsidiary company as a separate legal entity. The board of the holding company should therefore ensure that the boards of its subsidiaries are included in the development of the group governance framework.
14. The board of the holding company should ensure that the group governance framework does not conflict with the memoranda of incorporation, delegations of authority, shareholder agreements, board charters, board committee terms of reference, and related policies and agreements within the group.
15. The board of the holding company should ensure that the group governance framework recognises each subsidiary within the group as a separate and independent juristic person to whom its directors owe fiduciary duties.
16. The board of the holding company should ensure that the group governance framework addresses governance matters as is appropriate for the group, including the following:
  - a. Delineation of the rights and role of the holding company.
  - b. If applicable, delegation of certain responsibilities by the board of a subsidiary to a board committee of the holding company, without abdicating accountability, and subject to agreed reporting and information-sharing arrangements.
  - c. The extent to which governance and operational policies of the holding company have been adopted by subsidiary companies in the group.
  - d. Engagement by the holding company with the board of a subsidiary company before the holding company exercises its rights to elect directors to the board of the subsidiary.
  - e. Arrangements to address the risk of breaching legal duty in relation to the use of information obtained while acting as director of one company in the group for the purposes of another company in the group.



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17. The board of the holding company should ensure that the agreed group governance framework is implemented across the group.
18. The holding company should disclose an overview of the group governance framework that is implemented across the group.
19. The subsidiary company should disclose what responsibilities it has delegated to board committees of the holding company and the extent to which it has adopted the policies and procedures of the holding company.

## Responsibilities of institutional investors

Principle 17: The governing body of an institutional investor organisation should ensure that responsible investment is practiced by the organisation to promote the good governance and the creation of value by the companies in which it invests.

### RECOMMENDED PRACTICES

20. The governing body of an institutional investor should assume responsibility for governing responsible investing by setting the direction for how it should be approached and conducted by the organisation.
21. The governing body should approve policy that articulates its direction on responsible investment. This policy should provide for the adoption of a recognised responsible investment code, principles and practices.
22. The governing body should delegate to management, if in place, or alternatively, to the outsourced service provider if investment decisions and investment activities are outsourced, the responsibility to implement and execute its policy on responsible investment.
23. Where the institutional investor outsources investment decisions or investment activities to custodians, nominees, consultants or other service providers, the governing body should oversee that the outsourcing is regulated by formal mandate which reflects and gives effect to its responsible investment policy.
24. The governing body should ensure that service providers are held accountable for complying with the formal mandate.
25. The responsible investment code adopted by the institutional investor and the application of its principles and practices should be disclosed.

# PART 6



## SECTOR SUPPLEMENTS

**Part 6.1:** Introduction to sector supplements

**Part 6.2:** Supplement for municipalities

**Part 6.3:** Supplement for non-profit organisations

**Part 6.4:** Supplement for retirement funds

**Part 6.5:** Supplement for small and medium enterprises

**Part 6.6:** Supplement for state-owned entities



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# » SECTOR SUPPLEMENTS

## PART 6.1: INTRODUCTION TO SECTOR SUPPLEMENTS

### How to use the supplements

The supplements should be read together with the balance of the King IV Report, particularly Part 1: *Glossary of Terms*, Part 2: *Fundamental Concepts*, Part 3: *King IV Application and Disclosure* and Part 5: *King IV Code on Corporate Governance*. Exactly how this should be done is explained below, but the following is a quick guide:

All **governance outcomes** as per the Code apply.

All **principles** as per the Code apply, with the necessary adaptation of terminology as explained in each supplement.

The **recommended practices** in the Code should be considered together with the specific recommendations contained in each supplement and industry or sector codes and guidance issued by professional and industry bodies and regulators. Implementation of practices is subject to applicable legislation and scaling for proportional application as is appropriate for the organisation.

Reference should be made to the King IV Implementation Roadmap outlined below.

In keeping with the balance of the King IV Report, the supplements are primarily aimed at the governing body, it being the focal point of corporate governance within the organisation.

In these supplements, “corporate” refers to organisations that are incorporated to form legal entities separate from their founders. It therefore does not apply only to companies or for-profit enterprises, but all forms of incorporation whether as company, voluntary association, retirement fund, trust, legislated entity or others. The term “corporate governance” is used to differentiate it from other forms of governance, for example national or political governance.

### Purpose of the supplements

The purpose of the supplements is to provide high-level guidance and direction on how the King IV Code should be interpreted and applied by a variety of sectors and organisational types.

### SUPPLEMENTS FOR SPECIFIC SECTORS AND CATEGORIES OF ORGANISATION

The King IV Report does not include supplements for all sectors and categories of organisations. It was decided to issue supplements that were representative of a wide range of sectors and categories of organisations. Those sectors and categories of organisations for which specific supplements are not provided should consider the particular supplement which is most closely aligned to their organisational structure.

### *High-level guidance on interpretation and application of King IV*

The supplements illustrate how the King IV Code should be interpreted and applied in various contexts, situations and legislative regimes. Due to the wide variety of such, and the numerous governance challenges that may present themselves as a result, it is not possible to cover all in the supplements. Furthermore, an attempt to do so would be contrary to the normative rather than prescriptive approach of King IV.

# SECTOR SUPPLEMENTS CONTINUED

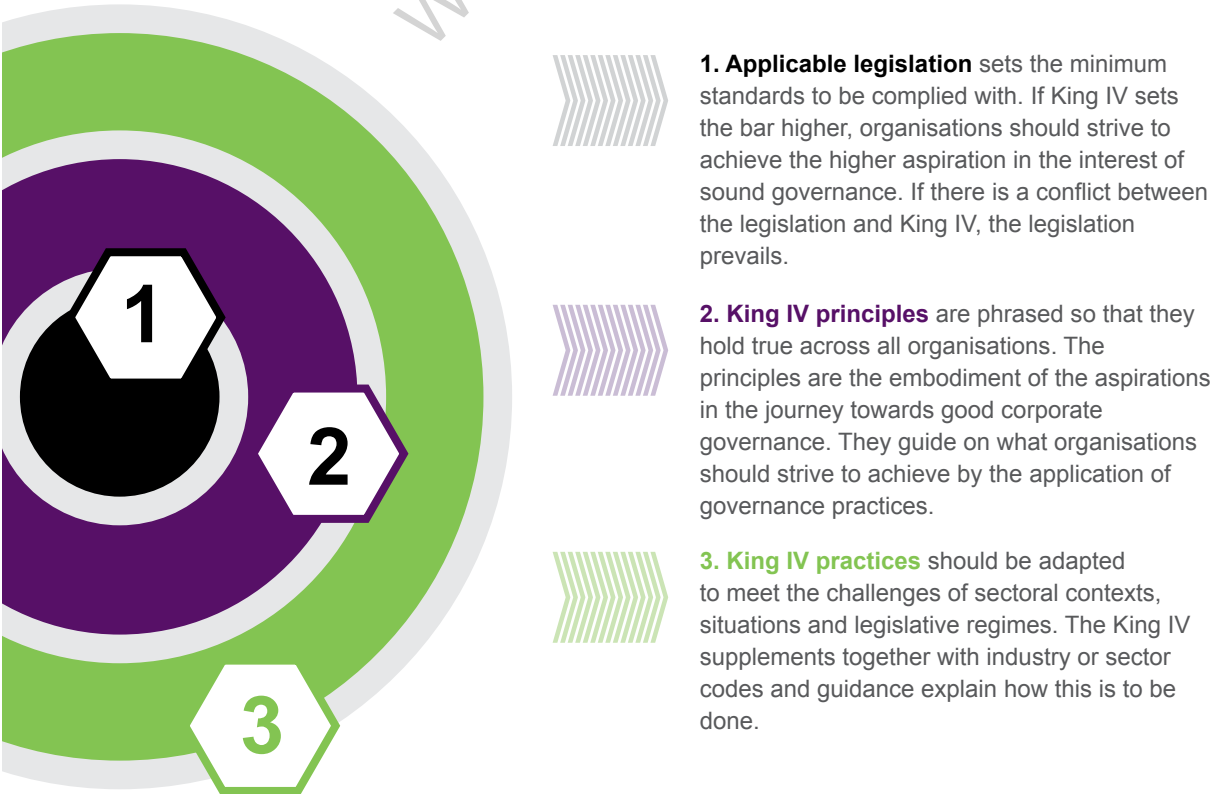
Instead of addressing all the potential variables, the supplements are intended to demonstrate how the Code should be interpreted and applied in a number of representative contexts, situations and legislative regimes. It is hoped that these demonstrations will enable those charged with governance duties to adapt the practices to their particular governance challenges – including those challenges not addressed in the supplements – while still giving effect to the aspirations expressed in the principles. The examples in the supplements are designed to demonstrate the manner in which governing bodies should apply their minds to King IV and do not replace the exercise of judgement by providing detailed solutions for all situations.

Certain aspects of King IV are emphasised in particular supplements for their relevance to a specific sector. It would be inaccurate to conclude that those aspects in the King IV Code that are not dealt with or not referred to specifically in the supplements, need not be considered.

## Reconciling King IV to legislation

Applicable legislation sets the minimum governance standards to be complied with. If King IV sets the bar higher, organisations should strive to achieve the higher aspiration in the interest of sound governance. If there is a conflict between the legislation and King IV, the legislation prevails. However, the mere fact that King IV advocates a higher standard of governance than the legislation demands, does not, in itself, necessarily constitute a conflict. A conflict only arises when King IV and legislated provisions cannot be reconciled, not when they are merely different. Therefore, implementing a higher standard than that required by law will still be compliant with the minimum requirements of the law.

The diagram below depicts the framework for governance of organisations:







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In certain instances, references to particular acts, sections of acts and regulations are included in the supplements to demonstrate the linkage and alignment between the principles and recommendations of King IV and legislation, albeit that different terminology or wording is used. King IV seeks to promote and give substance and effect to legislation, and it should be interpreted in this light.

## Proportional application

Even within the same sector, organisations vary largely in size, resources, and extent and complexity of activities. Appreciating this is important when interpreting King IV in order to apply it.

The following examples illustrate how recommended practices could be scaled in accordance with proportionality considerations:

Where it is recommended in the Code that certain functions should be established – for example finance, risk, technology and information, compliance or internal audit functions – such functions could consist of a senior employee instead of a team of people. If proportionality considerations warrant it, further scaling could be achieved by allocating part-time responsibility for the function to such an employee. Outsourcing of functions is another alternative and so is sharing functions and resources with affiliated organisations.

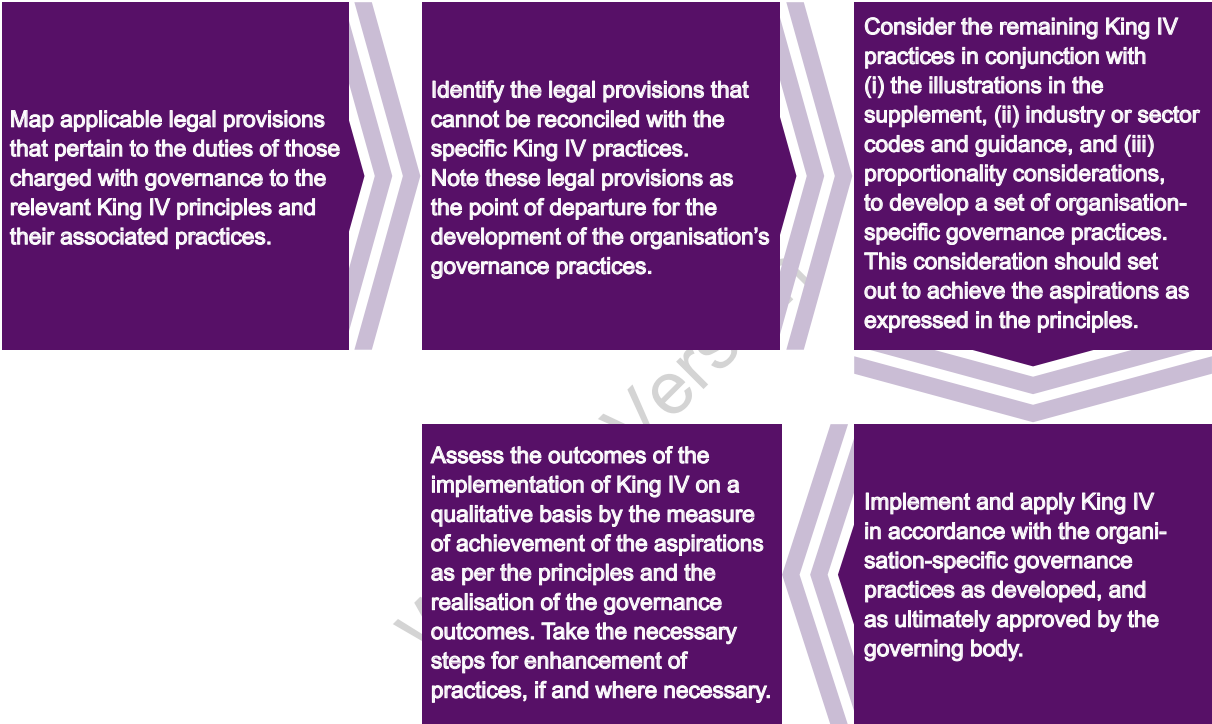
A recommendation that a committee of the governing body should be formed could, if justified by proportionality considerations, be replaced by having the governing body carrying out the functions normally fulfilled by such committee. Alternatively, the governing body could formally delegate, without abdicating accountability, to one of its members to investigate, consider and prepare submissions for recommendation and consideration by the full governing body.

Where the Code recommends that a formal policy be established, it could be accomplished by formalising in writing a few guiding criteria and processes, and by continually developing the document as learning evolves. The benefits of being intentional and devoting the necessary consideration to putting policies and structures in place should not be underestimated. Doing so clarifies intention and ensures alignment among those affected by the policy on the nature and extent of responsibilities, functions and authority delegated.

Proportional application of the practices should still give effect to the principles. Refer to Part 3: *King IV Application and Disclosure* for more guidance on proportionality.

# SECTOR SUPPLEMENTS CONTINUED

## King IV implementation roadmap





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## PART 6.2: SUPPLEMENT FOR MUNICIPALITIES

The supplements should be read together with the balance of the King IV Report, particularly Part 1: *Glossary of Terms*, Part 2: *Fundamental Concepts*, Part 3: *King IV Application and Disclosure* and Part 5: *King IV Code on Corporate Governance*.

### Municipalities: the macro view and benefits of corporate governance

The structural and institutional arrangements are different for the different types of municipalities – metropolitan, district and local municipalities. The common feature is that they are accountable to the communities they serve. In terms of section 152(1) of the Constitution, the objectives of local government (which consists of municipalities) are:

- to provide democratic and accountable government for local communities;
- to ensure the provision of services to communities in a sustainable manner;
- to promote social and economic development;
- to promote a safe and healthy environment; and
- to encourage the involvement of communities and community organisations in the matters of local government.

Section 153 of the Constitution furthermore refers to the developmental duties of municipalities. Thus, municipalities provide a foundation for our democracy; the efficiency with which they deliver services is the basis for economic and social cohesion in the context of a developmental state.

Good governance is essential to ensure the success of the municipality itself, and to protect and advance the interests of those whom it serves. Good corporate governance assists by enhancing the functioning of leadership structures, and by providing the arrangements which enable the council to govern the municipality in such a way that it is able to meet its objectives.

### Scope

This supplement applies to category A, B and C municipalities as provided for in the Municipal Structures Act.

Even within the same sector, organisations vary largely in size, resources, and extent and complexity of activities. The scope of this supplement was, therefore, limited for the sake of clarity. An attempt to address too wide a range of variables may defeat the intent of the supplement, namely to demonstrate how the practices in the Code should be interpreted and applied in a number of representative contexts, situations and legislative regimes.

Municipalities falling outside the scope of this supplement should still align with the principles and consider the practices while adapting them along the approach as demonstrated in this supplement. Refer to Part 6.1:

*Introduction to Sector Supplements* for the King IV Implementation Roadmap to assist with this.

# SECTOR SUPPLEMENTS CONTINUED

## King IV and municipalities

### TERMINOLOGY

In order to apply the King IV Code to municipalities without having to repeat it in its entirety, it is necessary to explain how the terminology used in the Code could be substituted for terminology applicable to municipalities. Although leadership structures in municipalities are not directly comparable to those of other organisations, the following guidelines can be used when interpreting the terminology in the King IV Code in a municipal context:

Term used in the King IV Code	Relevant term for municipalities
Organisation	Municipality
Governing body	Municipal council
Management	Management of the municipality, including the municipal manager as accounting officer and senior management as defined in the Municipal Finance Management Act (MFMA).
Members of the governing body	Councillors
Chair of the governing body	Speaker
Chief executive officer	Municipal manager or accounting officer
External auditor	Auditor-General of South Africa (Auditor-General)
Shareholder	Municipalities do not have shareholders, but in many respects, community members can be regarded as such.

The office of mayor or executive mayor of a municipality does not have an equivalent in the King IV Code. However, this does not suggest that the mayor or executive mayor of a municipality does not fulfil a governance function in a municipality. In respect of these politically elected positions, the Municipal Structures Act, MFMA and other pertinent legislation must be followed.

### BACKGROUND

Municipalities are autonomous, but operate within a system of cooperative governance in terms of the Constitution. Cooperative governance requires that the various spheres of government (national, provincial and local) cooperate in exercising their powers and performing their functions. The governance of municipalities should be viewed in the context of cooperative governance without detracting from municipal autonomy.

### KING IV PRINCIPLES AND PRACTICES

The essence of the King IV Code, as represented by its governance outcomes and principles, applies to municipalities with the necessary adaptation in terminology. Principles are repeated below for ease of reference.



Ethical culture

Good performance

Effective control

Legitimacy

### Principle 1: The council should lead ethically and effectively.

Ethical and effective leadership is exemplified by integrity, competence, responsibility, accountability, fairness and transparency. Members of the council should individually and collectively cultivate these characteristics and exhibit them in their conduct, as set out in the practices under Principle 1. This is congruent with section 195 of the Constitution, in terms of which public administration must be governed by the democratic values and principles enshrined in the Constitution, including that a high standard of professional ethics must be promoted and maintained. Section 50 of the Municipal Systems Act echoes this and a Code of Conduct for Councillors is included in Schedule 1 of that act. Schedule 5 of the Municipal Structures Act similarly includes a Code of Conduct for Councillors. The practices associated with Principle 1 should be considered to supplement and provide substance to these legal provisions.

### Principle 2: The council should govern the ethics of the municipality in a way that supports the establishment of an ethical culture.

In addition to assuming responsibility for their own character and conduct, in accordance with Principle 2, municipal councils should govern the ethics of the municipality. Schedule 2 of the Municipal Systems Act contains a Code of Conduct for Municipal Staff Members. The recommended practices under Principle 2 provide useful guidance on how to ensure and oversee adherence to this code and the ethics of the municipality, generally.

### Principle 3: The council should ensure that the municipality is and is seen to be a responsible corporate citizen.

Corporate citizenship is an alternative expression of the objectives of the municipality as set out in section 152(1) of the Constitution (see above). Therefore, the recommended practices under Principle 3 apply with the necessary adaptation to municipalities as a means to give effect to these objectives.

### Principle 4: The council should appreciate that the municipality's core purpose, its risks and opportunities, strategy, business model, performance and sustainable development are all inseparable elements of the value creation process.

The practices recommended under Principle 4 address the development and approval of the organisation's strategy, implementation thereof and organisational performance. For municipalities, strategy-development and performance-management processes are largely legislated and the practices in King IV should therefore be modified accordingly.

## SECTOR SUPPLEMENTS CONTINUED

**Principle 5: The council should ensure that reports issued by the municipality enable stakeholders to make informed assessments of the municipality's performance and its short, medium and long-term prospects.**

Reports issued by the municipality are a means of communicating with its community. Reports that are underpinned by integrated thinking and that present information about the resources and relationships on which the municipality relies, its activities, outputs and outcomes in an integrated manner, are an effective way of informing the community and other stakeholders about the municipality's performance. It also demonstrates accountability.

The role of the council with regards to reporting by the municipality is prescribed by legislation. The recommended practices under Principle 5 should be considered by the council, and adapted as is necessary to reconcile with legal provisions, so as to assist with executing its reporting duties.

**Principle 6: The council should serve as the focal point and custodian of corporate governance in the municipality.**

The council should serve as the focal point of corporate governance as provided for in Principle 6. In accordance with the Municipal Systems Act, a municipality is "an organ of state within the local sphere of government exercising legislative and executive authority within an area". In terms of section 151 of the Constitution, both legislative and executive authority vest in the council.

The legislative and executive authority that the council derives from the Constitution and other legislation, gives it dominium over the taxes and levies collected from those who reside within the borders of the municipality for the supply of electricity, water, sanitation, refuse removal and other services. Also, municipal elections are a means by which citizens nominate representatives, giving them the power to make decisions and execute them on their behalf. Therefore, even though the MFMA ascribes fiduciary duties to the municipal manager as accounting officer, the council shares in these fiduciary duties by virtue of its constitutional role.

Under Principle 6, the primary leadership role of any governing body is expressed as encompassing the following:

- a. steering the organisation and setting its strategic direction;
- b. approving policy and planning that give effect to the direction provided;
- c. overseeing and monitoring of implementation and execution by management; and
- d. ensuring accountability for organisational performance by means of, among others, reporting and disclosure.

It should be noted that the terminology used under this principle, namely strategy leading to policymaking, is usually used in the reverse in a government setting with policy directives leading to strategic initiatives and plans. Notwithstanding, and even though the Constitution, MFMA, Municipal Structures Act and Municipal Systems Act all allocate specific responsibilities to the council, the above is a useful framework for the council to attain an overarching understanding of its role. It should be used as a standing reference point by the council when discharging its responsibilities in any area of governance.



Ethical culture

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Effective control

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**Principle 7:** The council should comprise the appropriate balance of knowledge, skills, experience, diversity and independence for it to discharge its governance role and responsibilities objectively and effectively.

### **Knowledge, skills, experience and diversity of councillors**

Principle 7 deals with the criteria for the composition of the governing body. In a municipality, a mixed electoral system is followed for the election of councillors in terms of which, depending on the category of municipality, about half of the councillors are elected through a proportional representation ballot where voters vote for a party. The other half are elected as ward councillors by the residents in each ward. The composition of councils can therefore, not be proactively planned by means of a nomination process on the basis of the knowledge, skills, experience, diversity and independence required, as dealt with in the recommended practices under Principle 7.

Even though the legislated provisions pertaining to election of council members prevail over the King IV recommended practices for nomination, election and appointment, the council should still strive towards the aspiration expressed in this principle, as its composition is a key factor driving the performance of a municipality. Political parties can assist with the achievement of this aspiration by deploying councillors with the necessary knowledge, skills, experience and diversity.

There should also be a strong emphasis on in-depth induction for newly elected councillors at the start of a new political term in the interest of bolstering knowledge on the council. The council should furthermore ensure that a continued and robust professional education programme for councillors is established, which runs for the full term of office to ensure the building of competence.

Employing external expertise as recommended in the practices under Principle 7 will further assist the council with its oversight duties in the event that objective input on specific matters outside the knowledge, skills and experience of councillors is required.

### **Independence of councillors**

Independence of the members of the governing body is dealt with under Principle 7. Municipal councillors are elected to represent local communities on the council, but they may have party political affiliations which result in them not being independent in appearance. However, as a matter of law, all councillors must exercise objective judgement when executing their legal duties in the best interests of the municipality and its community.

This is reinforced in the Code of Conduct for Councillors in Schedule 1 of the Municipal Systems Act. The constitutional integrity of the council as a collective body acting at all times in the best interests of the municipality and the community it serves, enjoys priority over the interests of individual councillors.

### **Speaker**

There is no independent chair of council as provided for in the Code. The role of chair is fulfilled by the speaker. It is recommended that the practices under Principle 7 in relation to the chair be considered for how they could supplement the legislated role of the speaker.

Summary of recommended practices for the council's access to the appropriate balance of knowledge, skills, experience, diversity and independence:

- Political parties should deploy councillors with the necessary skills and competency.
- Council should ensure in-depth induction for councillors.
- Council should ensure the establishment of professional education programmes.
- Council should make use of external expertise on specific matters outside the knowledge, skills and experience of councillors, when required.

## SECTOR SUPPLEMENTS CONTINUED

**Principle 8: The council should ensure that its arrangements for delegation within its own structures promote independent judgement, and assist with balance of power and the effective discharge of its duties.**

The Municipal Systems Act provides in section 59 that the council must “develop a system of delegation that will maximise administrative and operational efficiency and provide for adequate checks and balances”. The Municipal Systems Act prescribes a wide range of powers and functions that may or may not be delegated. Councils may only delegate authority if they are expressly or by implication authorised to do so by law. The recommended practices under Principles 8 and 10 should be considered subject to these legal provisions.

In terms of section 79 of the Municipal Structures Act, the council is entitled to set up committees such as Municipal Public Accounts Committees<sup>1</sup> to assist with general oversight of the municipality’s performance. This aligns with the practices recommended under Principle 8 of the Code, which address delegation by the council within its own structures.

The audit committee’s duties as regards to the appointment and independence of the auditor, as set out in the recommended practices under this principle, apply differently in municipalities as the Auditor-General serves as the external auditor for a municipality. Furthermore, the structure and functions of the municipal audit committee are prescribed by legislation and prevail over the recommended practices in the Code. However, in so far as the legislation allows, the Code’s recommended practices in respect of the execution of the duties of the audit committee should be considered to supplement the minimum standard set by law.

**Principle 9: The council should ensure that the evaluation of its own performance and that of its committees, its speaker and its individual councillors, support continued improvement in its performance and effectiveness.**

The evaluation of the performance of the governing body, its members and committees as addressed by Principle 9 and its associated practices, applies to municipalities. In respect of council members who are deployed by political parties, it is recommended that the council and political parties collaborate on the manner and form in which the performance of the council and councillors should be assessed. The results of the performance evaluations should be responded to by the council so as to achieve continued improvement in its performance and effectiveness as per the principle.

<sup>1</sup> Municipal Public Accounts Committee, “Enhancing Oversight in the Municipality Practical Guide”, SALGA and National Treasury, March 2012. Also refer to section 129(4) of the MFMA.





Ethical culture

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**Principle 10: The council should ensure that the appointment of, and delegation to, management contribute to role clarity and the effective exercise of authority and responsibilities.**

In accordance with Principle 10 and also section 82 of the Municipal Structures Act, the council should appoint the municipal manager. The regulations for performance management and minimum competency levels of municipal managers should be taken into account in this regard. It is in the interest of the council to ensure that it appoints competent municipal management, so that it is able to place reasonable reliance for its decision-making on any information, opinions, recommendations, reports or statements presented by management.

Under Principle 10, it is furthermore recommended that the council should ensure that it has access to professional and independent guidance on corporate governance and its legal duties, and also that it has support to coordinate the functioning of the council and its committees. For companies, this role is fulfilled by the company secretary. As a matter of leading practice, it is recommended that municipal councils appoint a suitably experienced professional to provide these services.

**Principle 11: The council should govern risk in a way that supports the municipality in setting and achieving its strategic objectives.**

**Principle 12: The council should govern technology and information in a way that supports the municipality setting and achieving its strategic objectives.**

**Principle 13: The council should govern compliance with applicable laws and adopted, non-binding rules, codes and standards in a way that supports the municipality being ethical and a good corporate citizen.**

**Principle 14: The council should ensure that the municipality remunerates fairly, responsibly and transparently so as to promote the achievement of strategic objectives and positive outcomes in the short, medium and long term.**

## SECTOR SUPPLEMENTS CONTINUED

**Principle 15:** The council should ensure that assurance services and functions enable an effective control environment, and that these support the integrity of information for internal decision-making and of the municipality's external reports.

The recommended practices under Principles 11 to 15, which deal with specific governance functional areas, should be interpreted and applied in conjunction with industry or sector codes and guidance, applicable legislation and proportionality considerations.

**Principle 16:** In the execution of its governance role and responsibilities, the council should adopt a stakeholder-inclusive approach that balances the needs, interests and expectations of material stakeholders in the best interests of the municipality over time.

### **Stakeholders**

The primary stakeholder of a municipality is its community. In terms of section 2 of the Municipal Systems Act, a municipality consists of a community, a council and an administration. Therefore, communities must be involved, and community engagement should go beyond one-way communication from the municipality to its community. Other stakeholders include community organisations, political parties active in the municipality, national and provincial departments and industry and sector bodies. The practice recommendations under Principle 16 are applicable to give effect to the duties of the council in relation to governing stakeholder relationships.

In alignment with government initiatives already under way, it is recommended that municipal councils proactively set up reviews of municipal service delivery by the citizenry, as a way of monitoring and evaluating municipal performance.

### **Municipal entities as stakeholders of municipalities**

In keeping with Principle 16, the council is legally obliged to oversee the performance of administration and executive organs of the municipality, including the municipal entities (MEs). MEs should be managed as a material stakeholder grouping. The council should ensure that the business plan of the ME, developed in terms of section 87 of the MFMA, the municipal mandate and the Integrated Development Plan are all aligned. Integrating the strategy plan and execution thereof between the municipality and the MEs, ensures that the MEs operate within the mandate, powers and functions assigned and agreed with the municipality. A governance framework, broadly based on the recommended practices for group companies under Principle 16, is useful and should be considered by municipal councils to govern their relationship with the MEs.

(Note that Principle 17 does not apply to municipalities.)



Ethical culture

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## PART 6.3: SUPPLEMENT FOR NON-PROFIT ORGANISATIONS

The supplements should be read together with the balance of the King IV Report, particularly Part 1: *Glossary of Terms*, Part 2: *Fundamental Concepts*, Part 3: *King IV Application and Disclosure* and Part 5: *King IV Code on Corporate Governance*.

### NPOs: the macro view and benefits of corporate governance

Taking into account the critical role non-profit organisations (NPOs) fulfil, it is in the interest of the whole of society that this sector should thrive. This role is articulated as follows by the World Bank:

- *providing goods and services – especially meeting needs which have not hitherto been met by either the state or by the private sector;*
- *assisting the government to achieve its development objectives – in particular through contributing skills for which NPOs have comparative advantage, such as public information, education and communications campaigns, or providing information about the situations and needs of particularly vulnerable groups;*
- *helping citizens to voice their aspirations, concerns and alternatives for consideration by policy makers, thereby giving substance to governments' policies regarding freedoms of association and speech;*
- *helping to enhance the accountability and transparency of government and local government programmes and of officials.<sup>1</sup>*

Good corporate governance contributes to the success of an NPO as it enhances the functioning of its leadership structures and provides the arrangements by which the governing body should govern the NPO so that it is able to meet its strategic objectives. The particular benefits that could be derived from the good governance of an NPO include the following:

- Added credibility and enhanced reputation.
- Increased impact of activities and advocacy through stronger stakeholder relationships and more effective operational processes.
- Access to funding, grants and loans on better terms.
- The ability to leverage a wider pool of expertise for employment and volunteer work.
- Better fraud prevention due to improved controls.
- Business continuity arrangements that permit the NPO to operate under conditions of volatility, and to withstand and recover from acute shocks.
- Leadership continuity through succession planning.

<sup>1</sup> World Bank, "The Role of Non-profit organizations in Development: The experience of the World Bank", *The World Bank*, available at <http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/EXTSOCIALDEVELOPMENT/EXTPCENG/0,,contentMDK:20507529~menuPK:1278313~pagePK:148956~piPK:216618~theSitePK:410306,00.html>

# SECTOR SUPPLEMENTS CONTINUED

## Scope

An NPO can be incorporated in various forms, including as a non-profit company, charitable trust, voluntary association, club or fund. NPOs may also be referred to as non-governmental organisations (NGOs) or as Public Benefit Organisations (PBOs) – the latter refers to the tax exempt status of certain activities of organisations granted by the South African Revenue Service and not their form of incorporation, although for-profit organisations do not qualify for this status. The term “social enterprises” describes organisations that fulfil social or environmental needs. They could be set up as for-profit entities that operate as private companies, sole proprietorships, business trusts or partnerships.<sup>2</sup>

This supplement addresses non-profit legal forms, but is not limited to organisations that have been granted NPO status in terms of the Non-Profit Organisations Act. It thus applies to NGOs, PBOs and other NPOs, but would exclude social enterprises that follow a for-profit business model.

## King IV and NPOs

### TERMINOLOGY

In order to apply the King IV Code to NPOs without having to repeat it in its entirety, it is necessary to explain how the terminology used in the Code could be interchanged for terminology applicable to NPOs.

Term used in the King IV Code	Relevant term for NPOs
Organisation	A board, commission, company, corporation, fund, trust, voluntary association, or other term that would be applicable.
Governing body	Board or other term that would be applicable.
Shareholder	Member of an NPO incorporated as a non-profit company with members, or member of a voluntary association and also a donor as the provider of financial capital to the NPO. If donor funding is provided once-off, <i>ad hoc</i> or anonymously and no continuing relationship exists, references to shareholders do not apply to this category of funders.

In this supplement, the collective nouns “NPO” or “organisation” are used interchangeably. The supplement also refers generically to “governing body” and “member of the governing body”.

### KING IV PRINCIPLES AND PRACTICES

The essence of King IV, as represented by its governance outcomes and principles, applies to NPOs with the necessary adaptation in terminology. Principles are repeated below for ease of reference.

<sup>2</sup> Bertha Institute of Social Innovation and Entrepreneurship, *A Guide to Legal Forms for Social Enterprises in South Africa* (2015), p 5, available at <http://www.gsb.uct.ac.za/files/BerthaCentreGuideLegalFormsSocialEnterprisesSouthAfrica.pdf>



Ethical culture

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Legitimacy

### Principle 1: The governing body should lead ethically and effectively.

Ethical and effective leadership is exemplified by integrity, competence, responsibility, accountability, fairness and transparency. Members of the governing body should individually and collectively cultivate these characteristics and exhibit them in their conduct as set out in the practices under Principle 1.

Included in the ethical duties of the governing body are its legal duties. The fiduciary duties of the members of the governing body of an NPO are, as a matter of law, owed to the organisation itself and not the party or constituency by which the member is appointed. These legal duties stand regardless of whether members of the governing body of an NPO act *pro bono* or for a minimum fee.

A governing body whose members are appointed as representatives of constituents, donors or other stakeholders of the NPO should be especially proactive in managing potential and actual conflicts. These conflicts usually manifest in the entanglement of the private and professional interests of an individual. Examples of typical conflicts in an NPO environment include community members, being the beneficiaries of the outputs of the organisation's efforts, also serving on the NPO's executive or governance structures; and the appointment of relatives and friends as employees or paid consultants or suppliers. The following practice under Principle 1 should be implemented in this regard: "Members of the governing body should avoid conflicts of interest. In cases where a conflict cannot be avoided it, should be disclosed to the governing body in full at the earliest opportunity, and then proactively managed as determined by the governing body and subject to legal provisions."

### Principle 2: The governing body should govern the ethics of the organisation in a way that supports the establishment of an ethical culture.

In addition to assuming responsibility for its own character and conduct, in accordance with Principle 2, the governing body should govern the ethics of the NPO. The practices associated with this principle guide on how the governing body should discharge this responsibility.

### Principle 3: The governing body should ensure that the organisation is and is seen to be a responsible corporate citizen.

By virtue of advocating for and fulfilling social and environmental needs, acting as a collective voice and holding others responsible, NPOs are an integral part of the societal dynamic. NPOs are thus corporate citizens and should apply the recommended practices pertaining to responsible corporate citizenship under Principle 3.

## SECTOR SUPPLEMENTS CONTINUED

**Principle 4: The governing body should appreciate that the organisation's core purpose, its risks and opportunities, strategy, business model, performance and sustainable development are all inseparable elements of the value creation process.**

The practices recommended under Principle 4 address the development and approval of the organisation's strategy, implementation thereof and organisational performance.

The governing body of an NPO should balance its priorities so as to both remain financially viable and deliver on environmental or social objectives as per its constitution. This accords with King IV's assertion that performance encompasses the triple context of the economy, society and the environment in which the organisation operates. To accomplish this, it is important that an NPO clearly understands its strategy and business model as part of the value creation process. The Codes of Good Practice for South African Non-Profit Organisations issued by the Department of Social Development (Codes of Good Practice for South African NPOs) specifically highlight three major responsibilities of the leaders of an emerging NPO to ensure survival and growth:

- Ensuring that its service programme is meeting community needs or problems effectively and efficiently.
- Ensuring it establishes a reliable and sustainable support base in order to fulfil its work.
- Putting procedures in place to ensure the careful and accountable handling of all the organisation's resources and programmes.<sup>3</sup>

This guidance together with the recommended practices under Principle 4 will assist the governing bodies of NPOs with the processes for strategy development and oversight of implementation and execution.

**Principle 5: The governing body should ensure that reports issued by the organisation enable stakeholders to make informed assessments of the organisation's performance and its short, medium and long-term prospects.**

Reports are a powerful means for an NPO to communicate meaningfully with its stakeholders, among others, beneficiaries, donors and regulators. Reports that are underpinned by integrated thinking and that present information about the resources and relationships on which the NPO relies, its activities, outputs and outcomes in an integrated manner, are an effective way of informing stakeholders about the NPO's performance. It also demonstrates accountability.

<sup>3</sup> Adapted from: Department of Social Development, *Codes of Good Practice for South African Non-profit Organisations* (2001), p 7; available at [http://www.dsd.gov.za/npo/index.php?option=com\\_docman&task=cat\\_view&gid=20&Itemid=116](http://www.dsd.gov.za/npo/index.php?option=com_docman&task=cat_view&gid=20&Itemid=116)



Ethical culture

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The G4 Global Reporting Initiative's Sector Disclosures for NGOs highlights why reporting is important to NPOs:

- It enables NPOs to report on the extent to which they act as sustainable organisations in society.
- It provides NPOs with the opportunity to demonstrably meet the same standards of transparency and disclosure of positive and negative aspects of performance that are asked of other sectors.
- It provides opportunities for the organisation itself and its stakeholders to assess its policies and programmes and effectiveness, and the economic, social and environmental impacts of its activities.
- Through the process of reporting, an NPO can critically examine its own activities, benchmark itself with other organisations, learn from experience and make improvements over time to better serve the causes it pursues.<sup>4</sup>

The practices under Principle 5 should be considered by the governing body to assist with its reporting responsibilities.

### Principle 6: The governing body should serve as the focal point and custodian of corporate governance in the organisation.

The governing body's status as the focal point and custodian of corporate governance, as set out in Principle 6, is a natural consequence of its fiduciary duties towards the organisation. This common law duty originates from the fact that the governing body is entrusted with assets and interests, other than its own.

Under Principle 6, the primary leadership role of any governing body is expressed as encompassing the following:

- a. steering the organisation and setting its strategic direction;
- b. approving policy and planning that give effect to the direction provided;
- c. overseeing and monitoring of implementation and execution by management; and
- d. ensuring accountability for organisational performance by means of, among others, reporting and disclosure.

The above is a useful framework for the governing body of an NPO to attain an overarching understanding of its role. It should be used as a standing reference point by the governing body when discharging its responsibilities in any area of governance.

As stated in the Codes of Good Practice for South African NPOs<sup>5</sup>, the role of an NPO's governing body tends to emerge from the circumstances that gave birth to the organisation. As the organisation evolves and grows, so the governing body finds itself faced with evolving challenges. At any stage of the organisational life cycle, it is important for a governing body to be clear on how best to lead and provide direction.

<sup>4</sup> Adapted from: Global Reporting Initiatives, *G4 Sustainability Reporting Guidelines – Sector Disclosures for NGOs*, (2013); p 8

<sup>5</sup> Department of Social Development, *Codes of Good Practice for South African Non-profit Organisations* (2001), p 13, available at [http://www.dsd.gov.za/npo/index.php?option=com\\_docman&task=cat\\_view&gid=20&Itemid=116](http://www.dsd.gov.za/npo/index.php?option=com_docman&task=cat_view&gid=20&Itemid=116)

## SECTOR SUPPLEMENTS CONTINUED

**Principle 7: The governing body should comprise the appropriate balance of knowledge, skills, experience, diversity and independence for it to discharge its governance role and responsibilities objectively and effectively.**

Principle 7 provides for the governing body to be composed so it is able to discharge its governance role and responsibilities objectively and effectively. Where members of the governing body of an NPO are appointed as representatives of constituents, donors or other stakeholders, it is challenging to achieve the balance of knowledge, skills, experience, diversity and independence needed.

A formal process for the nomination, election and ultimately appointment of members of the governing body will help to ensure that the knowledge, skills, experience, diversity and independence requirements of the governing body are identified, that the requirements are communicated to those who are responsible for nomination and election, and that candidates are properly vetted. The practices recommended in support of Principle 7 should be considered to accomplish this.

In order to overcome resource constraints and an inability to pay market-related fees for the services of professional members of its governing body, an NPO should collaborate with professional bodies in its search for governing body members. Many experienced professionals are prepared to serve their communities through serving on the governing bodies of NPOs for no or minimal fees.

There is no optimum size and composition for the governing body of an NPO. There may be statutory requirements and other considerations to be taken into account, such as where the NPO is in its growth cycle.

The governing body of an NPO and its chair should guard against members of the governing body sending representatives to the governing body meetings, instead of attending themselves. Legally, this practice puts both the member of the governing body and his or her representative at risk.

**Principle 8: The governing body should ensure that its arrangements for delegation within its own structures promote independent judgement, and assist with balance of power and the effective discharge of its duties.**

The establishment and delegation to committees of the governing body as addressed in the practices under Principle 8 should be considered in conjunction with industry or sector codes and guidance, applicable legislation and proportionality considerations.





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**Principle 9:** The governing body should ensure that the evaluation of its own performance and that of its committees, its chair and its individual members, support continued improvement in its performance and effectiveness.

The evaluation of the performance of the governing body, its members and committees as addressed by Principle 9 and its associated practices, applies to NPOs. The results of the performance evaluations should be responded to by the governing body so as to achieve continued improvement in its performance and effectiveness as per the principle.

**Principle 10:** The governing body should ensure that the appointment of, and delegation to, management contribute to role clarity and the effective exercise of authority and responsibilities.

An NPO may be said to be maturing when members of the governing body are not involved in the day-to-day running of the operations, management of staff, or other functions of the chief executive officer.<sup>6</sup> The practices under Principle 10 are pertinent in this regard. Due to resource constraints, delegation to members of the governing body may be necessary under certain circumstances, but should only be considered and implemented with the necessary governance processes and controls in place, particularly as they relate to conflicts of interest.

Under Principle 10, King IV furthermore recommends that the governing body should ensure that it has access to professional and independent guidance on corporate governance and the legal duties of the governing body, and also that it has support to coordinate the functioning of the governing body and its committees. For companies, this role is fulfilled by the company secretary. As a matter of leading practice, it is recommended that the governing bodies of NPOs appoint a suitably experienced professional to provide these services. Consult the guidance on proportional application provided in Part 6.1: *Introduction to Sector Supplements* for how this could be implemented by NPOs.

**Principle 11:** The governing body should govern risk in a way that supports the organisation in setting and achieving its strategic objectives.

<sup>6</sup> Department of Social Development; Codes of Good Practice for South African Non-profit Organisations (2001); p 13; available at [http://www.dsd.gov.za/npo/index.php?option=com\\_docman&task=cat\\_view&gid=20&Itemid=116](http://www.dsd.gov.za/npo/index.php?option=com_docman&task=cat_view&gid=20&Itemid=116)

## SECTOR SUPPLEMENTS CONTINUED

Principle 12: The governing body should govern technology and information in a way that supports the organisation setting and achieving its strategic objectives.

Principle 13: The governing body should govern compliance with applicable laws and adopted, non-binding rules, codes and standards in a way that supports the organisation being ethical and a good corporate citizen.

Principle 14: The governing body should ensure that the organisation remunerates fairly, responsibly and transparently so as to promote the achievement of strategic objectives and positive outcomes in the short, medium and long term.

Principle 15: The governing body should ensure that assurance services and functions enable an effective control environment, and that these support the integrity of information for internal decision-making and of the organisation's external reports.

The recommended practices under Principles 11 to 15, which deal with specific governance functional areas, should be interpreted and applied in conjunction with industry or sector codes and guidance, applicable legislation and proportionality considerations.

Principle 16: In the execution of its governance role and responsibilities, the governing body should adopt a stakeholder-inclusive approach that balances the needs, interests and expectations of material stakeholders in the best interests of the organisation over time.

Principle 16 addresses stakeholder relationships. Some NPOs have shareholders or members, and others have donors or funders who are the primary providers of financial capital to the NPO. Other stakeholders include employees, regulators, media, partners, beneficiaries, communities, suppliers and creditors. The recommended practices under this principle assist with establishing stakeholder relationships that result in legitimacy, something that is critical to the long-term viability and sustainability of the NPO.

Additional guidance is to be found in Section 4 of the G4 Global Reporting Initiative's Sector Disclosures for NGOs<sup>7</sup>, which is instructive on executing accountability to stakeholders.

(Note that Principle 17 does not apply to NPOs.)

<sup>7</sup> Global Reporting Initiatives, *G4 Sustainability Reporting Guidelines – Sector Disclosures for NGOs*, (2013), p 31, available at <https://www.globalreporting.org/standards/sector-guidance/sectorguidanceG4/Pages/default.aspx>



Ethical culture

Good performance

Effective control

Legitimacy

## PART 6.4: SUPPLEMENT FOR RETIREMENT FUNDS

The supplements should be read together with the balance of the King IV Report, particularly Part 1: *Glossary of Terms*, Part 2: *Fundamental Concepts*, Part 3: *King IV Application and Disclosure* and Part 5: *King IV Code on Corporate Governance*.

### Retirement funds: the macro view and benefits of corporate governance

Retirement funds are an important part of the institutional investor industry, which consists of retirement funds, insurance companies as well as custodians, nominees and service providers who act under mandate in respect of any investment decisions and activities.

Retirement funds play an important role in the overall system of governance. They make investment decisions and have rights as shareholders, and the way in which these decisions are made and rights are exercised either reinforce or weaken the corporate governance of the companies that they invest in. Also, these funds owe fiduciary duties to their members. They therefore need to be well-governed and apply the principles of responsible investing in the quest for long-term, sustainable returns.

Retirement funds that follow and mandate responsible investing wield significant power for the enhancement of the checks and balances that are essential for an overall effective ecosystem of corporate governance and the creation of value. In King IV following responsible investing principles and practices is put forward as part and parcel of the good governance of retirement funds.

### Scope

This supplement applies to all retirement funds, including the following types of funds in accordance with their definitions in the Income Tax Act, No 58 of 1962, as amended:

- Pension funds
- Provident funds
- Preservation funds
- Retirement annuity funds.

Even within the same sector, organisations vary largely in size, resources, and extent and complexity of activities. The scope of the supplement was, therefore, limited for the sake of clarity. An attempt to address too wide a range of variables may defeat the intent of the supplement, namely to demonstrate how the practices in the Code should be interpreted and applied in a number of representative contexts, situations and legislative regimes. Retirement funds falling outside the scope of this supplement should still align with the principles and consider the practices while adapting them along the approach as demonstrated in the supplement. Refer to Part 6.1: *Introduction to Sector Supplements* for the King IV Implementation Roadmap to assist with this.

# SECTOR SUPPLEMENTS CONTINUED

## King IV and retirement funds

### BACKGROUND

In addition to legislation and King IV, the Code for Responsible Investing in South Africa<sup>1</sup> (CRISA) is a voluntary code applicable to institutional investors, the definition of which includes retirement funds. CRISA and King IV are complementary codes that reinforce and complement each other. Other industry or sector codes and guidance, such as Financial Services Board Circular PF 130<sup>2</sup> (FSB Circular PF 130) should be considered in conjunction with this supplement. (Refer to the governance framework included in Part 6.1: *Introduction to Sector Supplements*.)

### TERMINOLOGY

In order to apply the King IV Code to retirement funds without having to repeat it in its entirety, it is necessary to explain how the terminology used in the Code could be interchanged for terminology applicable to retirement funds.

Term used in the King IV Code	Relevant term for retirement funds
Organisation	Retirement fund, including pension fund, provident fund, preservation fund or retirement annuity fund.
Governing body	Board of the fund as defined in the Pension Funds Act.
Chief executive officer	Similar but not identical to Principal Officer.
Shareholder	Member of the retirement fund and, depending on the context, could include the sponsoring employee.

In this supplement, the collective nouns “retirement fund” or “fund” are used interchangeably, as are “board” and “governing body”.

### KING IV PRINCIPLES AND PRACTICES

The essence of King IV as represented by its governance outcomes and principles apply to retirement funds with the necessary adaptation in terminology. Principles are repeated below for ease of reference.

**Principle 1: The board should lead ethically and effectively.**

Ethical and effective leadership is exemplified by integrity, competence, responsibility, accountability, fairness and transparency. Members of the board of the fund should individually and collectively cultivate these characteristics and exhibit them in their conduct as set out in the practices under Principle 1.

**Principle 2: The board should govern the ethics of the fund in a way that supports the establishment of an ethical culture.**

In addition to setting an example through its own character and behaviour, the board should also ensure that the ethics of the fund is governed effectively. Principle 2 and its supporting practices apply to both a retirement fund with its own staff complement to carry out the administration, and to a fund that outsources those services. When outsourced, the board should satisfy itself that the fund’s service providers manage their ethics effectively through codes of conduct, ethics policies and supporting processes.

<sup>1</sup> Committee for Responsible Investment in South Africa, *Code for Responsible Investment in South Africa* (Institute of Directors in Southern Africa, 2011), available at: [www.iodsa.co.za](http://www.iodsa.co.za)

<sup>2</sup> Financial Services Board, *Good Governance for Retirement Funds – Circular 130, 2007* available at <https://www.fsb.co.za/>



Ethical culture

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Legitimacy

**Principle 3: The board should ensure that the fund is and is seen to be a responsible corporate citizen.**

Compliance with Regulation 28 of the Pension Funds Act and, in particular, the preamble stating that prudent investing “should give appropriate consideration to any factor which may materially affect the sustainable long-term performance of the fund’s assets, including factors of an environmental, social and governance character”, should be seen as an integral part of the fiduciary duties of the board of a fund.

Principle 3 conveys the same intent, albeit using different terminology. A retirement fund gives substance to its duty to be a responsible corporate citizen by ensuring that its investment analyses and practices, whether executed by the fund itself or an asset or fund manager or other service provider, take account of sustainability including environmental, social and governance (ESG) considerations, as provided for in Principle 1 of CRISA. Principle 3 of King IV includes that the fund should accept ownership responsibility for its investment arrangements and investment activities as provided for in Principle 2 of CRISA.

**Principle 4: The board should appreciate that the fund’s core purpose, its risks and opportunities, strategy, business model, performance and sustainable development are all inseparable elements of the value creation process.**

The practices recommended under Principle 4 address the development and approval of the organisation’s strategy, implementation thereof and organisational performance. These practices should be considered and adapted by the board of the fund, being mindful of the fact that, unlike a commercial enterprise, the purpose of a retirement fund is more narrowly defined to provide the benefits to its members, their beneficiaries and dependants as set out by its rules. The performance of a retirement fund consists of delivering targeted investment returns in terms of its investment strategy without irresponsible risk-taking, and managing expenses to maximise value for money.<sup>3</sup> For a retirement fund, it is especially critical that a long-term view is taken of the fund’s performance in the interests of its members.

**Principle 5: The board should ensure that reports issued by the fund enable stakeholders to make informed assessments of the fund’s performance and its short, medium and long-term prospects.**

Reports are a powerful means for a retirement fund to communicate meaningfully with its stakeholders, among others, members and regulators. Reports that are underpinned by integrated thinking and that present information about the resources and relationships on which the fund relies, its activities, outputs and outcomes in an integrated manner, are an effective way of informing stakeholders about the retirement fund’s performance. It also demonstrates accountability. The practices under Principle 5 should be considered by the board to assist with its reporting responsibilities.

In addition, it is recommended that retirement funds apply the disclosure practices as recommended under Principle 5 of CRISA as these pertain specifically to demonstrating accountability on investment decisions and activities.

<sup>3</sup> Stewart, F. and J. Yermo, “Pension Fund Governance: Challenges and Potential Solutions”, *OECD Working Papers on Insurance and Private Pensions, No. 18*, OECD publishing, © OECD. doi:10.1787/241402256531, 2008

## SECTOR SUPPLEMENTS CONTINUED

**Principle 6: The board should serve as the focal point and custodian of corporate governance in the fund.**

The board's status as the focal point and custodian of corporate governance, as set out in Principle 6, is a natural consequence of its fiduciary duties towards the members of the fund. This common law duty originates from the fact that the board is entrusted with assets and interests, other than its own.

Under Principle 6, the primary leadership role of any governing body is expressed as encompassing the following:

- a. steering the organisation and setting its strategic direction;
- b. approving policy and planning that give effect to the direction provided;
- c. overseeing and monitoring of implementation and execution by management; and
- d. ensuring accountability for organisational performance by means of, among others, reporting and disclosure.

The above is a useful framework for the board of a retirement fund to attain an overarching understanding of its role. It should be used as a standing reference point by the board when discharging its responsibilities in any area of governance.

Principle 6 and its associated recommended practices should be read together with section 7C of the Pension Funds Act.

**Principle 7: The board should comprise the appropriate balance of knowledge, skills, experience, diversity and independence for it to discharge its governance role and responsibilities objectively and effectively.**

### ***Election and appointment of board members***

Even though the election and appointment mechanisms of members of retirement fund boards are prescribed in legislation, the boards of retirement funds should still strive towards the aspiration expressed in Principle 7. One of the ways in which this can be achieved is by using external expertise as recommended in the practices under Principle 7, to assist the board with its oversight duties in the event that objective input on specific matters outside its knowledge, skills and experience is required.

Another manner in which balanced board composition can be accomplished is for employers or sponsors to use their powers of appointment to ensure that the board has members with the necessary expertise and experience. Those board members appointed by the employer should not be involved in the employer's decisions as regards the fund, and employers should not use their power of appointment of board members to ensure some sort of control over funds.<sup>4</sup> Also, a process of engagement with the employees who elect retirement fund board members should be initiated to convey the nature of board members' duties and the competencies required, so that informed elections take place.

As is the case with all organisations, professional development and learning are of critical importance in ensuring that those charged with the governance of retirement funds are able to execute their duties effectively. Ongoing development programmes should include responsible investment and ESG matters.

<sup>4</sup> Rosemary Hunter, "The Governance Of Pension Funds", April 2002  
(Paper presented by Rosemary Hunter to the annual convention of the Financial Planning Institute Durban)



Ethical culture

Good performance

Effective control

Legitimacy

### ***Independence of board members and conflicts of interest***

Members of the board should act with independence of mind, regardless of who elected or appointed them. Members of the board should not act as representatives of their constituencies, and meetings of the board should not be understood as forums for collective bargaining. Doing so results in board members facing conflicts between the interests of those who appointed or elected them and the interests of the fund itself.<sup>5</sup>

Funds benefit from board members who are independent in appearance as this supports balanced, objective decision-making in the best interests of the fund and its members. It is recommended that at least half of the members of the board are independent and appointed from a pool of professional board members. Such independent board members should be free from any relationships that could, in the opinion of a reasonable and informed outside party, affect their objectivity. Smaller funds should consider appointing at least one independent, professional board member.

Independent board members could add objective judgement in dealing with the conflicts of interest that those board members who are also members of the fund may have. Conflicts may arise in both expense and investment allocations and in the context of valuations. Valuations can be especially complex when dealing with portfolio companies and assets that are difficult to assess. The board should ensure that a policy exists which provides for how these conflicts of interest should be managed.

All members of the board are bound to treat as confidential any information that comes to their attention during the course of performing their duties as such. Such information cannot be disclosed to outside parties, including to those who elected the members of the board and to fund members, without the express permission of the board on behalf of the fund.

Summary of recommended practices for the board's access to the appropriate balance of knowledge, skills, experience, diversity and independence:

- The board should make use of external expertise on specific matters outside the knowledge, skills and experience of the board when required.
- Employers or sponsors should use their powers of appointment to ensure that the board has members with the necessary expertise and experience.
- The board should ensure engagement with those who elect board members.
- The board should ensure ongoing development programmes for its members.

**Principle 8: The board should ensure that its arrangements for delegation within its own structures promote independent judgement, and assist with balance of power and the effective discharge of its duties.**

Principle 8 deals with the establishment of board committees. The boards of all funds that undergo a statutory audit should consider having an audit committee to ensure proper oversight of the quality of the audit and the independence of the auditor. Retirement funds should also consider investment committees to set investment strategy and monitor the performance of asset and fund managers against the strategy. Death and disability committees may be appropriate for larger funds.

Regardless of the actual board committees that are established, the practices that address board committees under this principle are generally applicable to retirement funds and should be considered in conjunction with industry or sector codes and guidance, applicable legislation and proportionality considerations.

<sup>5</sup> Rosemary Hunter, "The Governance Of Pension Funds", April 2002  
(Paper presented by Rosemary Hunter to the annual convention of the Financial Planning Institute Durban)



## SECTOR SUPPLEMENTS CONTINUED

**Principle 9:** The board should ensure that the evaluation of its own performance and that of its committees, its chair and its individual members, support continued improvement in its performance and effectiveness.

The evaluation of the performance of the governing body, its members and committees as addressed by Principle 9 and its associated practices, applies to retirement funds. The results of the performance evaluations should be responded to by the board so as to achieve continued improvement in its performance and effectiveness as per the principle.

**Principle 10:** The board should ensure that the appointment of, and delegation to, management contribute to role clarity and the effective exercise of authority and responsibilities.

### ***Outsourcing***

Many retirement funds outsource all or part of the fund's administrative functions and investment activities. Delegation of responsibilities to a third party does not absolve the board from accountability. Oversight of service providers to whom the administration of the fund or investment decisions or investment activities are outsourced, is an integral part of the board's governance role, as the board can be held liable for their actions. The practices as recommended in the Code under Principle 10 are helpful guidance on oversight of management and should be applied by the board with the necessary adaptation in relation to fund administrators and other service providers.

When administrative and investment functions are outsourced, mechanisms and processes should be introduced for adequate and effective oversight in the same way as the board would have done if all these functions were conducted by the management of the fund. The board should ensure that a clear mandate is in place between the retirement fund and the fund administrator and other service providers. The mandate should provide for performance measures and targets and the application of responsible investing principles and practices. Execution of such mandates by outsourced service providers should be supervised by the board.

The board must be especially proactive in overseeing how service providers manage conflicts of interest. This challenge is particularly acute when various funds' investments are pooled and managed by the same investment manager, and the board should ensure that the interests of the retirement fund are treated fairly in relation to the potential competing interests of the co-investment vehicles and parallel funds.

### ***Appointment of principal officer***

Another matter that falls under Principle 10 is the appointment of the principal officer. In terms of the Pension Funds Act, the board appoints the principal officer. Hence, the principal officer is accountable to the board and the board, in turn, is accountable to the members of the fund. (The board also has a secondary line of accountability to the sponsoring employer of the fund, as the retirement fund is fulfilling an obligation on behalf of the employer.)

The principal officer may also be a board member but may, in terms of FSB Circular PF 130, not act as the chair of the board.





Ethical culture

Good performance

Effective control

Legitimacy

***Professional corporate governance services to the governing body***

Under Principle 10, it is furthermore recommended that the board should ensure that it has access to professional and independent guidance on corporate governance and its legal duties, and also that it has support to coordinate the functioning of the board and its committees. For companies, this role is fulfilled by the company secretary. As a matter of leading practice, it is recommended that boards of retirement funds appoint a suitably experienced professional to provide these services.

Principle 11: The board should govern risk in a way that supports the fund in setting and achieving its strategic objectives.

Principle 12: The board should govern technology and information in a way that supports the fund setting and achieving its strategic objectives.

Principle 13: The board should govern compliance with applicable laws and adopted, non-binding rules, codes and standards in a way that supports the fund being ethical and a good corporate citizen.

Principle 14: The board should ensure that the fund remunerates fairly, responsibly and transparently so as to promote the achievement of strategic objectives and positive outcomes in the short, medium and long term.

Principle 15: The board should ensure that assurance services and functions enable an effective control environment, and that these support the integrity of information for internal decision-making and of the fund's external reports.

The recommended practices under Principles 11 to 15, which deal with specific governance functional areas, should be interpreted and applied in conjunction with industry or sector codes and guidance, applicable legislation and proportionality considerations.

## SECTOR SUPPLEMENTS CONTINUED

**Principle 16:** In the execution of its governance role and responsibilities, the board should adopt a stakeholder-inclusive approach that balances the needs, interests and expectations of material stakeholders in the best interests of the fund over time.

Principle 16 addresses stakeholder relationships. The stakeholders of a retirement fund include, among others, the members of the fund, their dependents and nominees, the participating employer, the sponsor (if different from the participating employer), the Registrar of Pension Funds and the respective service providers. The recommended practices under this principle assist in establishing stakeholder relationships that contribute to the sustainability of the fund.

**Principle 17:** The board should ensure that responsible investment is practiced by the fund to promote the good governance and the creation of value by the companies in which it invests.

Principle 17 invokes the application of the principles and practices of responsible investing as advocated in CRISA, and which should be applied by all retirement funds as a matter of good governance.



Ethical culture

Good performance

Effective control

Legitimacy

## PART 6.5: SUPPLEMENT FOR SMALL AND MEDIUM ENTERPRISES

The supplements should be read together with the balance of the King IV Report, particularly Part 1: *Glossary of Terms*, Part 2: *Fundamental Concepts*, Part 3: *King IV Application and Disclosure* and Part 5: *King IV Code on Corporate Governance*.

### SMEs: the macro view and benefits of corporate governance

Small and medium enterprises (SMEs) are the drivers of a growing and inclusive economy, and of societal transformation. In order to survive, SMEs need to be innovative and entrepreneurial, and open to technological change and productivity growth. They are therefore an integral part of the renewal process that defines a market economy. SMEs play a particularly important role as job creators, thus providing a way for people to enter the formal economy and join the mainstream of society.<sup>1</sup>

Good corporate governance contributes to the success of an SME, as it enhances the functioning of its leadership structures and helps the governing body to govern in such a way that the SME meets its strategic objectives. Some of the further benefits SMEs can derive from good corporate governance include the following:

- Added credibility and enhanced reputation.
- Access to capital and loans on better terms.
- The ability to attract talent for employment.
- Improved access to customers and market participants.
- Better positioning to capture business opportunities.
- Better fraud prevention due to improved controls.
- Business continuity arrangements that permit the SME to operate under conditions of volatility, and to withstand and recover from acute shocks.
- Leadership continuity through succession planning.
- Better management of the risk of conflict in family businesses.

### Scope

For the purposes of this supplement an SME is defined as a private, for-profit company which has a public interest score of at least 350 calculated in terms of regulation 26(2) of the Companies Act.

Even within the same sector, organisations vary largely in size, resources, and extent and complexity of activities. The scope of this supplement was, therefore, limited for the sake of clarity. An attempt to address too wide a range of variables may defeat the intent of the supplement, namely to demonstrate how the practices in the Code should be interpreted and applied in a number of representative contexts, situations and legislative regimes. SMEs falling outside the scope of this supplement should still align with the principles and consider the practices while adapting them along the approach as demonstrated in the supplement. Refer to Part 6.1: *Introduction to Sector Supplements* for the King IV Implementation Roadmap to assist with this.

<sup>1</sup> Adapted from: François Groepe, "The role of the small business in the economy", October 2015 (address given by him while he was the Deputy Governor of the South African Reserve Bank at the AHI conference, George, 9 October 2015).

# SECTOR SUPPLEMENTS CONTINUED

## King IV and SMEs

### TERMINOLOGY

In order to apply the King IV Code to SMEs without having to repeat it in its entirety, it is necessary to explain how the terminology used in the Code could be interchanged for terminology applicable to SMEs.

Term used in the King IV Code	Relevant term for SMEs (within the scope of this supplement)
Organisation	Company or SME
Governing body	Board
Members of the governing body	Directors

### BACKGROUND

SMEs typically grow from the investment of energy, passion and resources by founding members over time, sometimes over decades and generations. Such SMEs eventually become a family partnership, consortium, syndicate or even company owned by a number of outside shareholders. The risk is for the governance structures and processes not to evolve and mature as the company does. Corporate governance facilitates stable and sustainable development and the ability to leverage opportunities. It is therefore important for SMEs to ensure that a foundation of good governance is established from the beginning, so that it is entrenched in the way the business is conducted.

A key consideration in developing corporate governance in tandem with the growth of the company is the transition of ownership and management. Business growth ultimately requires an evolution from an entrepreneurial to a professionally managed organisational system<sup>2</sup>.

### KING IV PRINCIPLES AND PRACTICES

The essence of King IV, as represented by its governance outcomes and principles, applies to SMEs with the necessary adaptation in terminology. Principles are repeated below for ease of reference.

**Principle 1: The board should lead ethically and effectively.**

Ethical and effective leadership is exemplified by integrity, competence, responsibility, accountability, fairness and transparency. Directors should individually and collectively cultivate these characteristics and exhibit them in their conduct as set out in the practices under Principle 1.

**Principle 2: The board should govern the ethics of the company in a way that supports the establishment of an ethical culture.**

In addition to setting an example through its own character and behaviour, the board should also ensure that the SME's ethics is governed effectively in accordance with Principle 2. The practices associated with this principle guide on how the board should discharge this responsibility.

<sup>2</sup> Tony Balshaw, *Thrive! Making Family Business Work* (Human & Rousseau (Pty) Ltd, 2003), p116



Ethical culture

Good performance

Effective control

Legitimacy

**Principle 3: The board should ensure that the company is and is seen to be a responsible corporate citizen.**

Due to the critical role of SMEs in an inclusive, growing economy and societal transformation, they are integral to society. SMEs also form part of the supply chain of other organisations, and are held accountable by their customers for responsible corporate citizenship and ethical practices. In short, SMEs are corporate citizens and should apply the recommended practices pertaining to responsible corporate citizenship under Principle 3 as is appropriate to their particular circumstances.

**Principle 4: The board should appreciate that the company's core purpose, its risks and opportunities, strategy, business model, performance and sustainable development are all inseparable elements of the value creation process.**

The practices recommended under Principle 4 address the development and approval of the organisation's strategy, implementation thereof and organisational performance.

King IV asserts that organisations contribute to the creation of value and perform well by enhancing the triple context of the economy, society and the environment and the capitals that they use or affect. By understanding the connection between sustainability and the business, an SME can measure its business performance, identify areas for improvement and manage change effectively. This will drive performance and innovation within the SME.<sup>3</sup> The practices recommended under Principle 4 are helpful guidance for accomplishing this.

**Principle 5: The board should ensure that reports issued by the company enable stakeholders to make informed assessments of the company's performance and its short, medium and long term prospects.**

Reports are a powerful means for SMEs to communicate meaningfully with stakeholders, among others, shareholders, customers and potential providers of financial capital. Reports that are underpinned by integrated thinking and that present information about the resources and relationships on which the SME relies, its activities, outputs and outcomes in an integrated manner, are an effective way of informing stakeholders about the SME's performance. It also demonstrates accountability. The practices under Principle 5 should be considered by the board to assist with its reporting responsibilities.

<sup>3</sup> Adapted from: Global Reporting Initiative, *GRI Ready to Report? Introducing sustainability reporting for SMEs booklet* (2014) available at <https://www.globalreporting.org/resourcelibrary/Ready-to-Report-SME-booklet-online.pdf>

## SECTOR SUPPLEMENTS CONTINUED

**Principle 6: The board should serve as the focal point and custodian of corporate governance in the company.**

The board's status as the focal point and custodian of corporate governance, as set out in Principle 6, is a natural consequence of its fiduciary duties towards the company. This common law duty originates from the fact that the board is entrusted with assets and interests, other than its own.

Even though SMEs are often more informal in conducting their business activities, there is a need to put their corporate governance on a formal footing. A key element of this is recognition of the board's overarching leadership and governance role as provided for in Principle 6, and its supporting practices. Under this principle, the primary leadership role of any governing body is expressed as encompassing the following:

- a. steering the organisation and setting its strategic direction;
- b. approving policy and planning that give effect to the direction provided;
- c. overseeing and monitoring of implementation and execution by management; and
- d. ensuring accountability for organisational performance by means of, among others, reporting and disclosure.

The above is a useful framework for the board of an SME to attain an overarching understanding of its role. It should be used as a standing reference point by the board when discharging its responsibilities in any area of governance.

In an SME, a director is often also a shareholder and manager. In the interest of role clarity, it is recommended that formal processes be put in place to differentiate between a single individual's roles as director, manager and shareholder. For example, board meetings should be scheduled separately from management meetings even though the same persons may be involved in both. As the founder's role changes from shareholder-director-manager to shareholder-director and finally to just shareholder, the degree of involvement and governance structures will also need to change. Transition will be easier if roles have been defined and kept separate from the start.

Formalising a description of each of these roles in writing will further assist individuals to identify in which capacity they should be acting, especially when specific authorities are exercised. It is recommended that an SME's shareholders sign an agreement with the board (even if they are related or consisting of the same individuals), and incorporate in this agreement a board charter, a management charter and a delegation of authority.



Ethical culture

Good performance

Effective control

Legitimacy

**Principle 7: The board should comprise the appropriate balance of knowledge, skills, experience, diversity and independence for it to discharge its governance role and responsibilities objectively and effectively.**

Principle 7 and its related practices are applicable to SMEs, but the following points should specifically be considered:

**Enhancing board independence**

All directors should, as a matter of law, exercise independent judgement in the best interests of the company. Having directors who are also independent in appearance in that there is no interest, position, association or relationship which is likely to affect, or may appear to unduly influence or cause bias, could pose a challenge to SMEs due to capacity and resource constraints.

Nevertheless, input free from perceived and actual bias adds value to board deliberations, and serves as an added control. Therefore, SMEs should strongly consider inviting an experienced and competent person to serve as a non-executive and, ideally, independent director. If this is not possible, such a person may be consulted on an *ad hoc*-basis, and invited to attend board meetings, as and when necessary, to obtain objective input until such time as the SME is in a position to appoint a full-time, independent, non-executive director. As the company grows in capacity, resources and consequently impact, steps should be taken to include a number of non-executive directors and at least one independent non-executive director who serves as chair.

Having a mix of executive and non-executive and one or more independent directors on the board also mitigates the risk that emotive issues drive decision-making, especially in family-owned companies or where the authority of the founding member is entrenched.

**Encouraging professional development**

Directors of SMEs who are not experienced non-executive directors should undergo corporate governance training so that they are adequately equipped to fulfil their fiduciary duties.

**Nomination, election and appointment of non-executive directors**

Many SMEs do not have a separate nominations committee to deal with the selection and nomination of new directors. It is thus recommended that the board charter clearly outlines the nomination, election and appointment process, the knowledge, skills and experience required from directors, and any other specific eligibility criteria. Once a number of non-executive directors are serving on the board, the formation of a nominations committee should be considered.

Non-executive directors should be formally appointed and fees and obligations agreed upfront. Creating a professional relationship with board members will help to establish a sound governance structure that is progressively less affected by emotive issues that may be connected to family dynamics or a more informal working environment.

## SECTOR SUPPLEMENTS CONTINUED

### ***Rotation and succession of directors***

In order to ensure that there is a balance of power as envisaged in Principle 7, the board needs to ensure that non-executive directors are rotated on a regular basis so as to maintain objectivity, which is one of the non-executive director's primary contributions. At the same time, care must be taken to protect the required institutional knowledge. For an SME, too-regular rotation may not be practical or feasible (especially if the SME only has one or two non-executive directors) and thus non-executive directors of SMEs may serve for longer periods than in larger companies.

Because a single individual often fulfils the roles of director, manager and shareholder, SMEs face the risk of increased dependence on key individuals. Succession planning for directors and managers should be put in place to ensure that key positions can be filled temporarily on an emergency basis and over the longer term. This is often a challenge in SMEs, and can affect business growth and continuity from one generation to the next if not dealt with appropriately.

An effective succession plan requires deliberate and well-thought-out processes that are tested and considered over time. The succession plan should describe how the successor will be chosen, what kind of knowledge, skills and experience will be required, what training and grooming will be necessary and how all of this should be accomplished.<sup>4</sup>

**Principle 8: The board should ensure that its arrangements for delegation within its own structures promote independent judgement, and assist with balance of power and the effective discharge of its duties.**

Principle 8 deals with delegation by the board to board committees. Due to capacity and resource constraints, it may not be possible for an SME to have all the board committees as recommended in the Code. With this being the case, the board is responsible for ensuring that it addresses those matters which a board committee would otherwise have addressed. Agendas should be appropriately structured or, if necessary, separate meetings should be set up to ensure sufficient focus on one particular topic or area (such as audit, risk and ethics).

**Principle 9: The board should ensure that the evaluation of its own performance and that of its committees, its chair and its individual members, support continued improvement in its performance and effectiveness.**

The evaluation of the performance of the governing body, its members and committees as addressed by Principle 9 and its associated practices, applies to SMEs. The results of the performance evaluations should be responded to by the board of the SME so as to achieve continued improvement in its performance and effectiveness as per the principle.

<sup>4</sup> Tony Balshaw, *Thrive! Making Family Business Work*, (Human & Rousseau (Pty) Ltd, 2003), p114





Ethical culture

Good performance

Effective control

Legitimacy

Principle 10: The board should ensure that the appointment of, and delegation to, management contribute to role clarity and the effective exercise of authority and responsibilities.

The practices under Principle 10 are pertinent in helping SMEs to attain clarity on the respective roles of the board and management. The boards of SMEs should apply these practices to achieve this aim.

Under Principle 10, it is furthermore recommended that the board should ensure that it has access to professional and independent guidance on corporate governance and its legal duties, and also that it has support to coordinate the functioning of the board and its committees. For companies, this role is fulfilled by the company secretary. As a matter of leading practice, it is recommended that boards of SMEs appoint a company secretary to provide these services. Consult the guidance on proportional application provided in Part 6.1: *Introduction to Sector Supplements* for how this could be implemented by SMEs.

Principle 11: The board should govern risk in a way that supports the company in setting and achieving its strategic objectives.

Principle 12: The board should govern technology and information in a way that supports the company setting and achieving its strategic objectives.

Principle 13: The board should govern compliance with applicable laws and adopted, non-binding rules, codes and standards in a way that supports the company being ethical and a good corporate citizen.

Principle 14: The board should ensure that the company remunerates fairly, responsibly and transparently so as to promote the achievement of strategic objectives and positive outcomes in the short, medium and long term.

## SECTOR SUPPLEMENTS CONTINUED

**Principle 15:** The board should ensure that assurance services and functions enable an effective control environment, and that these support the integrity of information for internal decision-making and of the company's external reports.

The recommended practices under Principles 11 to 15, which deal with specific governance functional areas, should be interpreted and applied in conjunction with industry or sector codes and guidance, applicable legislation and proportionality considerations.

**Principle 16:** In the execution of its governance role and responsibilities, the board should adopt a stakeholder-inclusive approach that balances the needs, interests and expectations of material stakeholders in the best interests of the company over time.

Principle 16 addresses stakeholder relationships. Due to the sometimes informal nature of relationships at an SME, shareholders may be more involved than is the case with bigger companies. With family businesses, shareholders also have personal ties with managers and directors which necessitate communication structures that create a bridge between family and business matters. Consideration should be given to establishing a formal forum in which shareholders of an SME may raise broad questions. Issues typically addressed in such a forum could include, among others, succession planning, growth and return on investment, dividend policy, acquisitions and/or disposals, going public, shareholder sacrifices and management performance.<sup>5</sup>

The company and its shareholders should also agree on policies for future equity ownership. Such policies should deal, for example, with the transfer, acquisition and disposal of shares in the SME, including the method of valuing shares equitably.<sup>6</sup>

The recommended practices under Principle 16 should be applied by the SME in respect of all its stakeholders.

(Note that Principle 17 does not apply to SMEs.)

<sup>5</sup> See Tony Balshaw, *Thrive! Making Family Business Work*, (Human & Rousseau (Pty) Ltd, 2003), p96-97 for more information on the role of the family shareholders' committee.

<sup>6</sup> Tony Balshaw, *Thrive! Making Family Business Work*, (Human & Rousseau (Pty) Ltd, 2003), p123



Ethical culture

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## PART 6.6: SUPPLEMENT FOR STATE-OWNED ENTITIES

The supplements should be read together with the balance of the King IV Report, particularly Part 1: *Glossary of Terms*, Part 2: *Fundamental Concepts*, Part 3: *King IV Application and Disclosure* and Part 5: *King IV Code on Corporate Governance*.

### SOEs: the macro view and benefits of corporate governance

As the Presidential Review Committee on State-owned Enterprises<sup>1</sup> makes clear, state-owned enterprises (which include state-owned entities (SOEs)), create the foundation that underpins economic growth and transformation, and thus have an important part in addressing the economic and social challenges facing the country. “South Africa aspires to be a Developmental State ... [and] SOEs need to be aligned to this agenda. If the country is to attain improved quality of life underpinned by a robust democracy and a just society, along with other initiatives, the State must preside over viable, efficient, effective and competitive SOEs”.

Good corporate governance is paramount to the success of the SOE itself, and to protect and advance the interests of the country and its citizenry. Governance helps enhance the functioning of leadership structures of an SOE, and provides the arrangements by which the SOE should be governed so that it is able to meet its strategic objectives.

### Scope

This supplement applies to all public entities listed in Schedules 2 and 3 of the Public Finance Management Act (PFMA).

Even within the same sector, organisations vary largely in size, resources, and extent and complexity of activities. The scope of this supplement was, therefore, limited for the sake of clarity. An attempt to address too wide a range of variables may defeat the intent of the supplement, namely to demonstrate how the practices in the Code should be interpreted and applied in a number of representative contexts, situations and legislative regimes. SOEs falling outside the scope of this supplement should still align with the principles and consider the practices while adapting them along the approach as demonstrated in the supplement. Refer to Part 6.1: *Introduction to Sector Supplements* for a King IV Implementation Roadmap to assist with this.

<sup>1</sup> Presidential Review Committee on State-owned Enterprises, *Executive summary of the final report, Volume 1*, p 7, available at [www.thepresidency.gov.za/electronicreport/...1/volume\\_1.pdf](http://www.thepresidency.gov.za/electronicreport/...1/volume_1.pdf)

# SECTOR SUPPLEMENTS CONTINUED

## King IV and SOEs

### TERMINOLOGY

In order to apply the King IV Code to SOEs without having to repeat it in its entirety, it is necessary to explain how the terminology used in the Code could be interchanged for terminology applicable to SOEs. Although structures in SOEs are not necessarily directly comparable to those of other organisations, the following can be used as a guideline when interpreting the terminology in the King IV Code in an SOE context:

Term used in the King IV Code	Relevant term for SOEs
Organisation	Business enterprise, board, commission, company, corporation, or other type of entity as provided for in the enabling legislation.
Governing body	“Accounting authority” as defined in the PFMA or board or other terminology as provided for in the enabling legislation.
Members of the governing body	Members of the accounting authority or board
External auditor	Auditor General of South Africa
Shareholder	“Executive authority” as defined in the PFMA.

In this supplement, “SOE” and “entity” are used interchangeably, as are, “governing body” and “accounting authority”, and “shareholder” and “executive authority”.

### KING IV PRINCIPLES AND PRACTICES

The essence of King IV, as represented by its governance outcomes and principles, applies to SOEs with the necessary adaptation in terminology. Principles are repeated below for ease of reference.

**Principle 1: The accounting authority should lead ethically and effectively.**

Ethical and effective leadership is exemplified by integrity, competence, responsibility, accountability, fairness and transparency. Members of the accounting authority should individually and collectively cultivate these characteristics and exhibit them in their conduct as set out in the practices under Principle 1. This is congruent with section 195 of the Constitution in terms of which public administration must be governed by the democratic values and principles enshrined in the Constitution, including that a high standard of professional ethics must be promoted and maintained.

**Principle 2: The accounting authority should govern the ethics of the SOE in a way that supports the establishment of an ethical culture.**

In addition to setting the example through its own character and conduct, the accounting authority should also ensure that the ethics of the SOE is governed effectively in accordance with Principle 2. The practices associated with this principle guide on how the accounting authority should discharge this responsibility.



Ethical  
culture

Good  
performance

Effective  
control

Legitimacy

**Principle 3: The accounting authority should ensure that the SOE is and is seen to be a responsible corporate citizen.**

By virtue of their public-interest mandates, corporate citizenship is core to the purpose of an SOE. Also, taxpayers contribute to the funding of SOEs. SOEs are thus accountable to these citizens, and the state organs that are representative of these citizens, for discharging their responsibilities in accordance with their mandates. Therefore, Principle 3 and the practices recommended under it should be applied by SOEs as a means by which to give expression to their public-interest mandates.

**Principle 4: The accounting authority should appreciate that the SOE's core purpose, its risks and opportunities, strategy, business model, performance and sustainable development are all inseparable elements of the value creation process.**

The practices recommended under Principle 4 address the development and approval of the organisation's strategy, implementation thereof and organisational performance. These practices should be considered by SOEs and modified, keeping the following in mind:

The strategic priorities of government, as decided by Cabinet, are devolved to the appropriate ministers and departments. Where in respect of an SOE, its executive authority is different from the minister responsible for policy, the policy ministry sets industry or sector policy on a country-wide basis and the role of the executive authority is then to set policy parameters for a specific SOE within this framework. The accounting authority of an SOE should actively seek common understanding between the entity and the executive authority on how to reconcile competing objectives so that a strategic plan for the SOE can be developed within these confines.

As far as performance is concerned, SOEs have to balance their priorities so as to both, fulfil their mandate and remain financially sustainable. This is congruent with King IV's assertion that performance encompasses both an organisation's achievements relative to its strategic objectives, and positive outcomes in terms of its effects on the capitals and the triple context in which it operates.

In order to obtain clarity and alignment on strategic objectives, key performance measures and targets and potential trade-offs to be made, it is recommended that these be agreed in writing between the entity, as represented by its accounting authority, and the shareholder, even where such an agreement is not required in terms of legislation.

## SECTOR SUPPLEMENTS CONTINUED

**Principle 5: The accounting authority should ensure that reports issued by the SOE enable stakeholders to make informed assessments of the SOE's performance and its short, medium and long-term prospects.**

Reports are a powerful means for an SOE to communicate meaningfully with its stakeholders, among others, the executive authority and taxpayers. Reports that are underpinned by integrated thinking and that present information about the resources and relationships that the entity relies on, its activities, outputs and outcomes in an integrated manner, are an effective way of informing stakeholders about the SOE's performance. It also demonstrates accountability. The practices under Principle 5 should be considered by the accounting authority to assist with its reporting responsibilities.

**Principle 6: The accounting authority should serve as the focal point and custodian of corporate governance in the SOE.**

The accounting authority is the governing body of an SOE, and thus bears fiduciary responsibilities in terms of section 50 of the PFMA and, where the SOE is a company, also section 75 of the Companies Act. The governing body's status as the focal point and custodian of corporate governance, as set out in Principle 6, is a natural consequence of its fiduciary duties which originate from the fact that the accounting authority is entrusted with assets and interests, other than its own.

Under Principle 6, the primary leadership role of any governing body is expressed as encompassing the following:

- a. steering the organisation and setting its strategic direction;
- b. approving policy and planning that give effect to the direction provided;
- c. overseeing and monitoring of implementation and execution by management; and
- d. ensuring accountability for organisational performance by means of, among others, reporting and disclosure.

It should be noted that the terminology used under this principle, namely strategy leading to policymaking, is usually used in the reverse in a government setting with policy directives leading to strategic initiatives and plans. Notwithstanding, the supporting practices are helpful in giving effect to the duties of the accounting authority as set out in the PFMA and other legislation. The above is also a useful framework for the accounting authority to attain an overarching understanding of its role. It should be used as a standing reference point by the accounting authority when discharging its responsibilities in any area of governance.



Ethical culture

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**Principle 7: The accounting authority should comprise the appropriate balance of knowledge, skills, experience, diversity and independence for it to discharge its governance role and responsibilities objectively and effectively.**

The composition of its accounting authority is a key factor driving the performance of an SOE. Like the governing bodies of all organisations, an SOE's accounting authority must have the right balance of knowledge, skills, experience, diversity and independence for it to discharge its governance role and responsibilities objectively and effectively. The practices recommended under Principle 7, with regards to the appointment of members of the governing body, and the role of a nominations committee in this process, are relevant to SOEs. Even when accounting authorities do not have the power to nominate or elect members, they should actively seek to collaborate with the shareholder on this critical issue.

The SOE and the executive authority should be transparent regarding the processes followed for the nomination, election and appointment of governing body members. The accounting authority and executive authority should also, subject to legal provisions, agree to put in place arrangements for the staggered rotation of members of the accounting authority. This should be done in order to introduce members with new expertise and perspectives whilst retaining valuable knowledge, skills and experience and maintaining continuity.

**Principle 8: The accounting authority should ensure that its arrangements for delegation within its own structures promote independent judgement, and assist with balance of power and the effective discharge of its duties.**

The practices recommended in support of Principle 8, which deal with the delegation of responsibilities by the governing body to its committees, are applicable to SOEs, subject to legal provisions. In particular, it should be noted that the duties of the audit committee in relation to the appointment and independence of the external auditor apply differently as the Auditor-General (who can agree to the appointment of a third party to fulfil this role) generally serves as the external auditor of SOEs. Furthermore, the composition of an SOE's audit committee is prescribed by legislation, which prevails over the recommended practices in the Code. However, the practices with regards to objective oversight by the audit committee over all assurance service providers and functions and the quality of their output still apply as provided for under Principle 8.

**Principle 9: The accounting authority should ensure that the evaluation of its own performance and that of its committees, its chair and its individual members, support continued improvement in its performance and effectiveness.**

The evaluation of the performance of the governing body, its members and committees as addressed by Principle 9 and its associated practices, applies to SOEs. The results of the performance evaluations should be responded to by the accounting authority so as to achieve continued improvement in its performance and effectiveness as per the principle.

## SECTOR SUPPLEMENTS CONTINUED

**Principle 10: The accounting authority should ensure that the appointment of, and delegation to, management contribute to role clarity and the effective exercise of authority and responsibilities.**

Principle 10 provides for the appointment of, and delegation of responsibilities to, competent executive management. In SOEs, the executive authority (as opposed to the accounting authority) often has the power, in terms of enabling legislation or the SOE's founding documents, to appoint the chief executive officer (CEO). As a matter of good practice, the appointment of the CEO of an SOE should be a robust and transparent process that involves the accounting authority to the greatest extent possible, even if the shareholder has the right to make the final appointment.

It should furthermore be agreed between the accounting authority and the shareholder that the CEO reports to the governing body. The governing body and shareholder should ensure that the CEO's letter of appointment and the delegation of authority to the CEO clearly set out that:

- The CEO is accountable to the accounting authority,
- The accounting authority agrees performance measures and targets with the CEO and assesses the performance of the CEO accordingly, and
- The accounting authority has primary responsibility for the removal of the CEO.

Under Principle 10, it is also recommended that the accounting authority should ensure that it has access to professional and independent guidance on corporate governance and its legal duties, and also that it has support to coordinate the functioning of the accounting authority and its committees. For companies, this role is fulfilled by the company secretary. As a matter of leading practice, it is recommended that the accounting authority of an SOE appoint a company secretary or suitably experienced professional to provide these services.

**Principle 11: The accounting authority should govern risk in a way that supports the SOE in setting and achieving its strategic objectives.**

**Principle 12: The accounting authority should govern technology and information in a way that supports the SOE setting and achieving its strategic objectives.**

**Principle 13: The accounting authority should govern compliance with applicable laws and adopted, non-binding rules, codes and standards in a way that supports the SOE being ethical and a good corporate citizen.**

**Principle 14: The accounting authority should ensure that the SOE remunerates fairly, responsibly and transparently so as to promote the achievement of strategic objectives and positive outcomes in the short, medium and long term.**





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**Principle 15:** The accounting authority should ensure that assurance services and functions enable an effective control environment, and that these support the integrity of information for internal decision-making and of the SOE's external reports.

The recommended practices under Principles 11 to 15, which deal with specific governance functional areas, should be interpreted and applied in conjunction with industry or sector codes and guidance, applicable legislation and proportionality considerations.

**Principle 16:** In the execution of its governance role and responsibilities, the accounting authority should adopt a stakeholder-inclusive approach that balances the needs, interests and expectations of material stakeholders in the best interests of the SOE over time.

Government is a primary stakeholder of SOEs in various capacities: Firstly, it is the shareholder concerned with financial viability, the consequences of the SOE's activities and outputs on the triple context and the capitals, and the SOE's delivery against its mandate. Secondly, government is the industry policymaker overseeing implementation of service delivery. Thirdly, it is the regulator concerned with the industry practices of SOEs, their pricing structures and the interests of consumers.<sup>2</sup> These various roles may overlap, and may even conflict with each other.

In addition, the SOE, together with Cabinet and the executive authority, is accountable to the National Assembly, and particularly the Standing Committee on Public Accounts, on the basis of the annual financial statements and the audit reports of the Auditor-General, and to the Portfolio Committees for service-delivery performance by the SOE.<sup>3</sup>

The accounting authority of an SOE should, therefore, ensure that it proactively engages with government, in all its various stakeholder capacities, to foster a working relationship and develop a mutual understanding of how these various expectations and accountabilities are to be reconciled.

As far as its relationship with government as shareholder is concerned, the accounting authority of an SOE should ensure that the shareholder compact or similar agreement defines the role of the accounting authority and the executive authority respectively. Generally, the executive authority should provide direction on policy to the SOE, and the accounting authority should oversee its effective implementation by the entity in accordance with strategic, corporate and business plans. The shareholder compact or such other agreement should provide for an alternative dispute resolution procedure if there is a dispute about the interpretation of the compact or agreement.

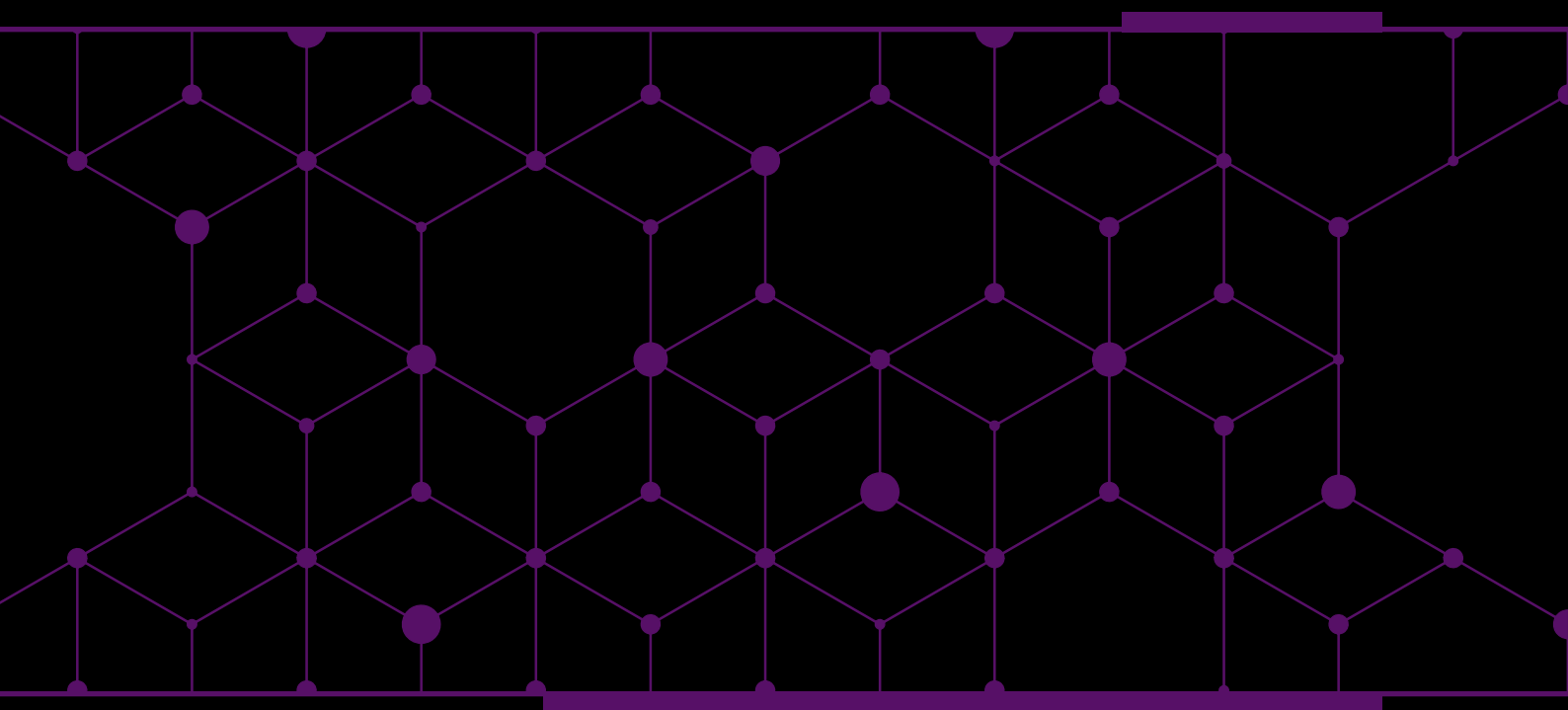
The recommended practices under Principle 16 should be applied by the SOE in respect of all its stakeholders.

(Note that Principle 17 does not apply to SOEs.)

<sup>2</sup> Higgo du Toit, "Governance Oversight Role Over State Owned Entities", *National Treasury*, 25 November 2005, p 5, available at <http://www.treasury.gov.za/publications/other/soe/governance%20oversight%20Role.pdf>

<sup>3</sup> Higgo du Toit, "Governance Oversight Role Over State Owned Entities", *National Treasury* 25 November 2005, p 2, available at <http://www.treasury.gov.za/publications/other/soe/governance%20oversight%20Role.pdf>

# PART 7



## CONTENT DEVELOPMENT AND KING COMMITTEE



# » CONTENT DEVELOPMENT AND KING COMMITTEE

## CONTENT DEVELOPMENT PROCESS

The process for developing King IV was designed to build on the strengths of King III. The King Committee also strived to involve as many as possible of those who would be affected by King IV in its development. To this end, the King IV process was widely consultative, with a participative and inclusive approach to the development of its content.

The drafting of King IV was led by the King IV Project Lead, who was assisted by a task team (see below) appointed by the King Committee from its membership to oversee the drafting process. The King Committee itself provided final approval.

The philosophy, principles and practices in King III were the starting point for content development. The input gained from extensive face-to-face consultative meetings with individual stakeholders, and the matters that had to be addressed as a result of local and international corporate governance developments, were also considered. Together, these formed the basis for the development of the King IV content.

There were no standing working groups or sub-committees established for drafting of content. A combination of technical corporate governance experts and representatives from interest groups or sectors volunteered to participate in a series of facilitated working sessions. Particular governance topics and the governance of organisations in the non-profit, SME, retirement fund and public sectors were explored through these sessions. An appreciative inquiry methodology was used by professional facilitators as the model for the working sessions which brought about a focus on what currently works and what the possibilities are, rather than the deficiencies of the *status quo*. These facilitated working sessions were then supplemented by a number of *ad hoc*-focus group sessions, convened to address specific governance topics and the various sectors in more depth.

The draft King IV Report was subjected to a formal public comment process which resulted in further engagement and consultation before finalisation.

King IV is a culmination of all of the efforts and processes as set out above. It is the sincere hope of the King Committee that it will be embraced by corporate South Africa, in its wider sense, and that it will contribute to a healthy economy, society and environment.

## MEMBERS OF KING COMMITTEE

### KING IV TASK TEAM MEMBERS:

Ms Ansie Ramalho (King IV Project Lead)
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Mr Mohamed Adam
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Ms Linda de Beer
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Ms Lindie Engelbrecht
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Mr Richard Foster
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Mr Michael Judin
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Dr Suresh Kana
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Dr Len Konar
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Ms Parmi Natesan
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Ms Annamarie van der Merwe
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# CONTENT DEVELOPMENT AND KING COMMITTEE CONTINUED

## KING COMMITTEE MEMBERS

(Unless otherwise indicated the members below served from August 2014, when the content development process started, until the launch of King IV on 1 November 2016.)

Prof Mervyn King	Independent
Mr Mohamed Adam	Independent
Mr Bernard Agulhas	Independent Regulatory Board for Auditors
Mr Roy Andersen	Independent
Mr Suleman Badat	Auditor General of South Africa
Ms Linda de Beer	Independent
Mr John Burke	Johannesburg Stock Exchange
Mr Chose Choeru	The South African Chamber of Commerce and Industry
Dr Gert Cruywagen	The Institute of Risk Management South Africa
Ms Friede Dowie	Business Leadership South Africa
Mr Shahied Daniels	South African Institute of Professional Accountants (until July 2015)
Ms Lindie Engelbrecht	South African Institute of Chartered Accountants
Mr Richard Foster	Independent
Mr Jaco de Jager	Association of Certified Fraud Examiners: SA Chapter
Mr Michael Judin	Independent
Dr Suresh Kana	Independent
Dr Reuel Khoza	Independent
Dr Len Konar	Independent
Ms Khanyisile Kweyama	Business Unity South Africa (from February 2016)
Mr Mabulenyana Marweshe	Financial Services Board (until April 2016)
Ms Justine Mazzocco	The Institute of Internal Auditors South Africa (from February 2015)
Ms Julie Methven	Compliance Institute Southern Africa
Mr Ewald Müller	Independent
Mr Jayce Nair	National Treasury
Ms Parmi Natesan	Institute of Directors in Southern Africa
Mr Madimetja Lucky Phakeng	Takeover Regulation Panel
Ms Ansie Ramalho	Institute of Directors in Southern Africa
Prof Deon Rossouw	The Ethics Institute (from February 2015)
Ms Matsietsi Mokholo	Department of Public Enterprises (from September 2016)
Mr Stephen Sadie	Chartered Secretaries Southern Africa
Mr Marius van den Berg	Independent
Ms Annamarie van der Merwe	Independent
Mr Anton van Wyk	Independent
Mr Andre Visser	Johannesburg Stock Exchange
Adv Rory Voller	Companies and Intellectual Property Commission
Vacant	Association for the Advancement of Black Accountants of Southern Africa
Vacant	Law Society of South Africa







