

Lecturer responsible for AUE2602:

Topic 1: Corporate Governance

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college of
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CORPORATE GOVERNANCE

What does CORPORATE GOVERNANCE mean:

It is the system or process whereby companies are directed or controlled.

It follows then that:

Healthy, honest, open, competent and responsibly controlled companies will improve the quality of modern society.



CORPORATE GOVERNANCE

Key aspects of King III:

Effective leadership

- * Ethical values of responsibility
- * Accountability
- * Fairness
- * Transparency



Sustainability

- * Inclusivity of stakeholders
- * Innovation, fairness and collaboration
- * Social transformation

Corporate citizenship

- * Consider not only financial performance
- * Consider impact of operations on society and environment
- * Protect, Enhance and Invest in well-being of society, environment and economy



APPLY OR EXPLAIN

WHY?

- Cost/benefit ratio
- One size does not fit all
- Attention to performance

- Therefore: Apply King III Principles and if not, Explain why not.

BOARD OF DIRECTORS

- **Chairman**

Independent non-executive director (*principle 2.16*).

CEO of the company not chairman of the board (*principle 2.16*).

Must be a formalised appointment

Performance to be assessed annually

- **Membership**

The board should comprise a balance of power with a majority of non- executive directors.

Majority of non-executive directors should be independent (*principle 2.18*).

- **Members**

Minimum of two executive directors - CEO and CFO (*principle 2.18*).

$\frac{1}{3}$ to be rotated annually

- **Meetings**

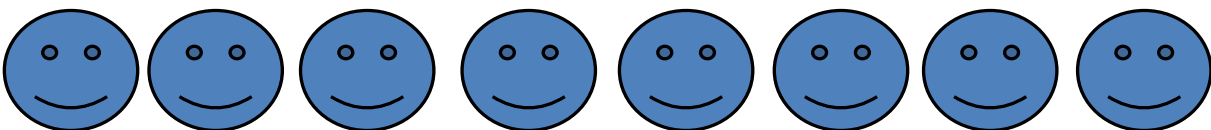
Meet at least four times a year (*principle 2.1.2*).

EXAMPLE - BOARD COMPOSITION

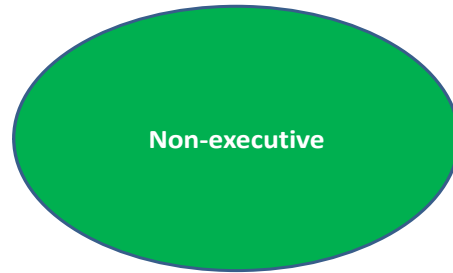
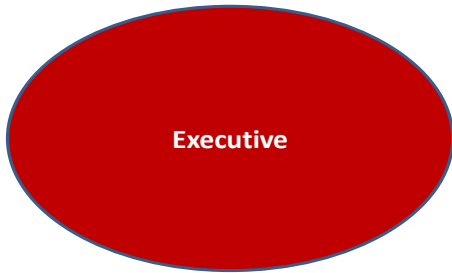
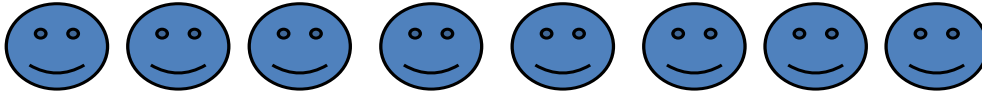
- **XYZ Ltd's board of directors consists of 8 directors**

➤ How should the board be structured in order to comply with the requirements of King III?

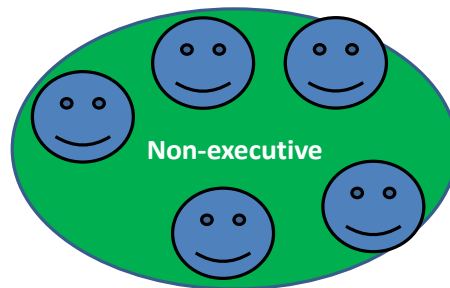
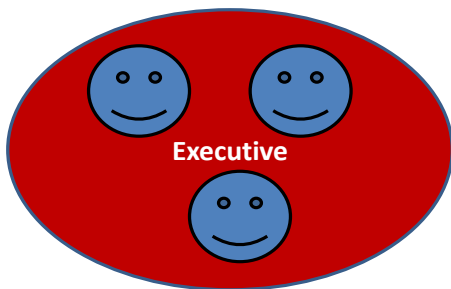
BOARD OF DIRECTORS



Example - Board Composition (Continued)



Example - Board Composition (Continued)

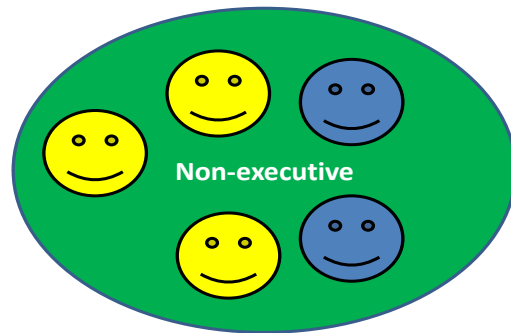
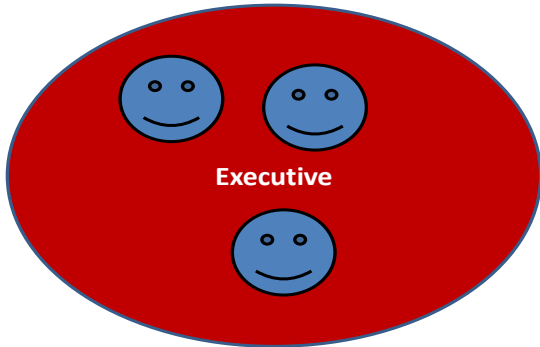


Minimum: CEO and Finance

Example - Board Composition (Continued)

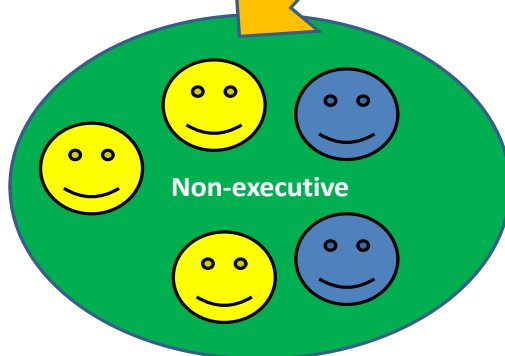
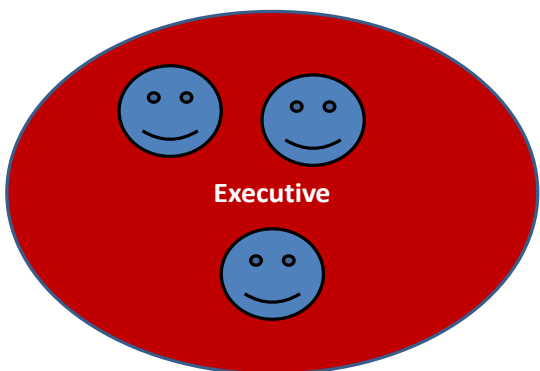


I am independent!!!!



Example - Board Composition (Continued)

Chairman



INDEPENDENT NON-EXECUTIVE DIRECTOR

- Is **not a representative of a shareholder** who has the ability to control or significantly influence management.
- Does not have a **direct or indirect interest** in the company which is material to the director or the company. (A holding of **5%** or more is considered material)
- Has not been **employed** by the company in any **executive capacity** for the preceding three financial years.
- Is not a member of the **immediate family** of an individual who is, or has been during the **previous three financial years**, employed by the company in an executive capacity.
- Is **not a professional advisor** to the company
- Is **free from any business** or other relationship which could be seen to interfere materially with the individual's capacity to act independently.
- Does **not receive remuneration contingent upon the performance** of the company.

King III Quiz 1

- Would the following individuals qualify as independent non-executive directors in terms of the King III Report? Justify your answer.
 - a partner in the law firm that acts as legal advisors to the company;
 - the company's auditor;
 - the company's recently retired chief executive; and
 - a shareholder who holds 3% of the company's shares.

BOARD – ROLES AND FUNCTIONS

- Focal point for custodianship of **corporate governance**
- Effective **leadership based on ethical foundation**
- Ensure company is and seen to **be responsible corporate citizen**
- Company's **ethics are managed effectively**
- Company has effective and independent **audit committee**
- Governance of **risk**
- Governance of **information technology**
- Act in the **best interest** of the company



BOARD COMMITTEES

	Audit committee	Remuneration committee	Nomination committee	Risk committee
Chairman	Independent non-executive director (principle 3.3). Chairman of the board should not be the chairman or member of the audit committee (principle 3.2).	Independent non- executive director (principle 2.23, par 131 of the King Report).	Independent non-executive director (principle 2.23, par 131 of the King Report).	Independent non- executive director (principle 2.23, par 131 of the King Report).
Membership	All members should be independent non-executive directors (principle 3.2).	Majority should be non- executive directors of which majority should be independent (principle 2.23).	Majority should be non- executive directors of which majority should be independent (principle 2.23.7). The Chairman of the board should be a member and may also be chairman (principle 2.16 par 45.3 of the King Report).	Executive and non- executive directors (principle 4.3).

Board Committees (Continued)

	Audit committee	Remuneration committee	Nomination committee	Risk committee
Members	Minimum of three members (principle 3.2).	Not specified in King III.	Not specified in King III.	Minimum of three members (principle 4.3)
Meetings	Meet at least twice a year (principle 3.1). Should meet with internal and external auditors at least once a year without management being present (principle 3.1).	Not specified in King III.	Not specified in King III.	Meet at least twice a year (principle 4.3).

King III Quiz 2

- State whether the following are true or false in terms of the King III Code:
 - The chairperson of the audit committee should be the chairperson of the board.
 - The CEO must chair the remuneration committee.
 - The nominations committee should consist of only non-executive directors.

COMPANY SECRETARY

Refer principle 2.21

- Should be suitably qualified, competent and experienced
- Should have an “arms-length” relationship
- Should not be a director of the company
- Prepare and circulate board papers
- Elicit responses, input, feedback for board and board committee meetings.
- Ensure preparation and circulation of minutes of board and committee meetings
- Etc

RISK

GOVERNANCE OF RISK AND IT

WHAT	WHO
Governance of risk.	The board (principle 4.1).
Design, implementing and monitoring the risk management plan.	The board should delegate to management (principle 4.4).
Monitor risk management process.	The board, risk committee, audit committee (principle 4.3).
Perform an objective assessment of the effectiveness of risk management.	Internal audit (principle 7.1).

RIKS MANAGEMENT

- Board is responsible – Charter + Risk Management Policy
- Risk (and sustainability) committee (together with Audit Committee)
- Delegate to management → Chief Risk Officer

Example: Company wants to double its turnover in the next 5 years. Strategy is to import from cheaper source, rather than to buy locally. Allow more generous credit terms.

INTERNAL AUDIT

KING III- Internal audit

Internal audit should perform the following functions

Systematically analyse and evaluate business processes and associated controls (principle 7.1).

Perform an objective assessment of the effectiveness of risk management and the internal control framework (principle 7.1).

Evaluate the company's governance processes (principle 7.1.2.1).

Provide a source of information as appropriate, regarding instances of fraud, corruption, unethical behaviour and irregularities (principle 7.1).

IA should be independent – cannot partake in day-to-day management / operations of the company. WHY?

NB NB! Chief Audit Executive should report functionally to the chairman of the Audit Committee (principle 7.4)

GOVERNING STAKEHOLDER RELATIONSHIPS

Stakeholders are any group affected by and affecting the company's operations

Main categories:

- Suppliers
- Creditors
- Employees
- Government (e.g. SARS)
- External Auditors
- Consumers/Customers
- Industry
- Local communities
- Media
- Regulators
- Potential investors

EXAM TECHNIQUE

- Study theory...
- REQUIRED REQUIRED REQUIRED...
- Do not make assumptions...
- QUESTIONS QUESTIONS QUESTIONS!!!!
- Corporate Governance will only count approx **25%** of exam

❖ When you get a compliance question:

THEORY – What does King III say

APPLICATION – What happened in the scenario

CONCLUSION – Did they comply / not?