

AUE2602

Corporate Governance in Accountancy

Topic 1

Corporate Governance and Statutory Matters



Define tomorrow .

UNISA



Who are your lecturers?



Ms Nicolene Coetzee CA(SA)

Tel: 012 429 6480

E-mail: aue2602@unisa.ac.za



Ms Esté-Marie Pieterse CA(SA)

Tel: 012 429 2164

E-mail: aue2602@unisa.ac.za

Dates to remember

- Assignment 1: Due **13 April 2018** (5%)
- Assignment 2: Due **13 April 2018** (15%)
- Remember the submission of either assignment allows you entry into the exam and will be used in calculating your year mark

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- It contains ALL your study material and learning activities. This includes your study guide and tutorial letters
- This is how we communicate with you – please read all announcements carefully!
- You can submit all your assignments online

This is faster and safer than by post!

Topic 1: Corporate governance and statutory matters

- Background to corporate governance
- Section 76 to 78 and 94 of the Companies Act
- King IV Report (Significant matters)

The aim of this topic is to **explain** and **apply** corporate governance in a practical situation, by referring to the Companies Act and the King IV Report

1. Background to Corporate Governance

- What is meant by Corporate Governance (CG)?

- ✓ It is a system whereby **organisations** are **directed and controlled**.

- Why is there a need for Corporate Governance?

- ✓ As we are all **linked** to **organisations** in various ways, a balance between economic, environmental and social goals for the stakeholders of the company is needed, as this will improve the quality of modern society for all.

- Definition of Corporate Governance

- ✓ The exercise of **ethical and effective leadership** by the governing body towards the achievement of governance outcomes: ethical culture, good performance, effective control and legitimacy.

1. Background to Corporate Governance

What is the Basis of the King IV Report?

- The report adopts an **“apply and explain”** basis.
- King IV assumes that all entities already incorporate its principles, as this is in the best interest of any business. Entities are required to explain in a narrative how the practices was implemented to address the principles.

1. Background to Corporate Governance

How has CG developed in South Africa?

1. The King I Report issued in 1994
2. The King II Report issued in 2002
3. The King III Report effective in March of 2010
4. The King IV Report issued 1 November 2016, effective 1 April 2017

Note: King IV includes many of the ideas, principles and characteristics developed in King I, II and King III.

1. Background to Corporate Governance

Objectives of King IV

1. CG is integral to running an organisation and delivering governance outcomes e.g. ethical culture
2. Broaden acceptance of King IV – more accessible across variety of sectors and organisational types.
3. CG is holistic and interrelated arrangements to be understood and implemented in integrated manner.
4. Encourage transparent and meaningful reporting to stakeholders.
5. CG is concerned with structure, process, ethical consciousness and conduct.

1. Background to Corporate Governance

- Are both King IV and the Companies Act legislated into South African Law?
- ✓ The **King IV Report** is **not** legislated in South Africa. It provides **principles** and **recommendations** to all organisations in South Africa to ensure that they adhere to good corporate governance. However non-compliance to the principles of King IV is not contrary to the law.
- ✓ One of the listing requirements of the JSE is compliance to the King IV Report.
- ✓ The **Companies Act is legislated** into South African law, and thus if companies do not comply with the rules and laws in the Companies Act, they are acting contrary to the law.

1. Background to Corporate Governance

Study:

- The King IV Report (2016: 3-7, 20-38)
- Jackson & Stent (2016: 4/3 - 4/18)

Activities:

- Do all the activities related to this learning unit

2. Statutory Matters

- Always a **link** between good corporate governance and compliance with the law
- As **directors** play an important role in corporate governance, you need knowledge of the Companies Act sections which deal with directors
- These sections include: 76, 77, 78 and 94

2. Statutory Matters

Section 76: Standards of Directors Conduct

This section describes certain duties of directors such as:

1. Not to use the position of director to

- Gain an advantage for director or any other person
- Knowingly cause harm to the company

2. Communicate to the board any information that comes to his attention

3. Exercise the powers and functions of a director

- In good faith and for a proper purpose
- In the best interests of the company
- With a degree of care, skill reasonably expected of a director

Study: Companies Act S76 and Jackson & Stent (2016: 3/45 – 3/46)

2. Statutory Matters

Section 77: Liability of Directors and Prescribed Officers

This section deals with instances where a director and prescribed officer may be held **liable for losses** suffered by the company

- Breach of fiduciary duties
- Delict
- Acting for the company without authority
- Carrying on a business recklessly
- Etc.

Study: Companies Act S77 and Jackson & Stent (2016: 3/46 – 3/47)

2. Statutory Matters

Section 78: Indemnification and Directors Insurance

Any provision of an agreement, the MOI or rules or a resolution of a company, is void if it directly or indirectly seeks to relieve a director of any of that director's duties.

The section does allow certain protection of directors through indemnification (protection) and director insurance provided certain conditions are met.

Study: Companies Act S78 and Jackson & Stent (2016: 3/47-3/48)

2. Statutory Matters

Section 94: Audit Committees

States that a public company, state owned company or other company that is required by its MOI to have an audit committee, must elect an audit committee at each annual general meeting

- Study the membership of this committee (Members must or must not be)
- Study the duties of the audit committee

Study: Companies Act S94 and Jackson & Stent (2016: 3/53 – 3/54)

3. King IV Report

- Applies to all entities regardless of manner and form of incorporation, however compliance is **compulsory** for **public companies listed** on the **JSE**
- The size and nature of the company will determine how the recommendations are applied

3. King IV Report

The **significant matters** covered by the **King Report** include:

- Leadership, ethics and corporate citizenship
- Strategy, performance and reporting
- **Governance structures and delegation**
- The governance of risk
- The governance of information technology
- Compliance governance
- The governance of remuneration
- Assurance
- The governance of stakeholder relationships

3. King IV Report

Governing Structures and Delegation

- The governing body is responsible for the corporate governance of an organisation.
- S66(1) of the Companies Act requires that the business and affairs of companies must be **managed** by or under the direction of a **board of directors**

3. King IV Report

Governing body and committees

Governing Body

Chair	Independent non-executive member
	CEO not fulfill the role of chair (CEO will not be an independent non-executive)
	The role of chair should be formalized
	The chair's performance should be assessed every alternate year
Membership	Comprise a balance of power, knowledge, skill, experience, diversity and independence
	Majority of non-executive members Majority of non-executive members should be independent
	Nominations committee to recommend the eligibility of prospective members
Members	Minimum of two executive members: one should be the CEO and the other may be the chief finance officer or other any executive as is appropriate
	Periodic, staggered rotation of members
Functions	Governing body should have a charter setting out its responsibilities, role, membership requirements and procedural conduct.
	Other functions listed under principle 6.1

3. King IV Report

Governing body and committees

Audit Committee

Chair	Independent non-executive member
	Chair of board should not chair audit committee
Membership	All members should be independent non-executive
Members	Minimum of three members
Meetings	Should meet with internal and external auditors at least once a year without management being present
Functions	Provide independent oversight of the effectiveness of the organisation's assurance functions and services
	Provide independent oversight of the integrity of the annual financial statements and other external reports
	May approve the annual financial statements (but the governing body remains ultimately accountable)
	The governing body may delegate the risk governance to the audit committee
	Oversee the management of financial and other risks that affect the integrity of external reports

3. King IV Report

Governing body and committees

Other Committees

	Remuneration Committee	Nomination Committee	Risk Committee	Social and Ethics Committee
Chair	Independent non-executive member	Not specified	Not specified	Not specified
Membership	All should be non-executive of which majority should be independent .	All should be non-executive of which majority should be independent .	Executive and non-executive of which majority should be non-executive	Executive and non-executive of which majority should be non-executive
Members	Minimum of three members	Minimum of three members	Minimum of three members	Minimum of three members

3. King IV Report

Governing body and committees

Other Committees continued...

	Remuneration Committee	Nomination Committee	Risk Committee	Social and Ethics Committee
Functions	Should assist the governing body in setting and administering remuneration policies.	The process for nominating, electing and appointing members of the governing body.	Should consider the risk management policy and plan and monitor the risk management process.	Oversight of, and reporting on organisational ethics, responsible corporate citizenship, sustainable development and stakeholder relationships.
		Succession planning iro governing body members.		
		Evaluation of the performance of the governing body.		

3. King IV Report

Governing body and committees

- Principle 8 states that 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**. This means that the governing body **may delegate** some of its responsibilities to various committees as needed to **ensure the best interest** of the organisations is achieved.
- The governing body **remains the ultimately responsible**.

3. King IV Report

Governing body and committees

Study: King IV Report (2016: 49 – 60) and Jackson & Stent (2016: 4/26 – 4/40)

When doing the activities, tutorial 102 questions, assignments and past examination papers, take note of how the information is given in the scenario, as well as how the solution is presented. You will notice that marks are available for **applying** the information in the scenario to the requirements of the King IV Report.

3. King IV Report

Non-executive member

- A non-executive member is a member who is **not involved in the management** of the company.
- The role of the non-executive member is to **provide independent judgment, advice and opinions** on issues facing the company – “an outsiders’ view”
- Required to **attend governing body and committee meetings** to which they have been appointed.

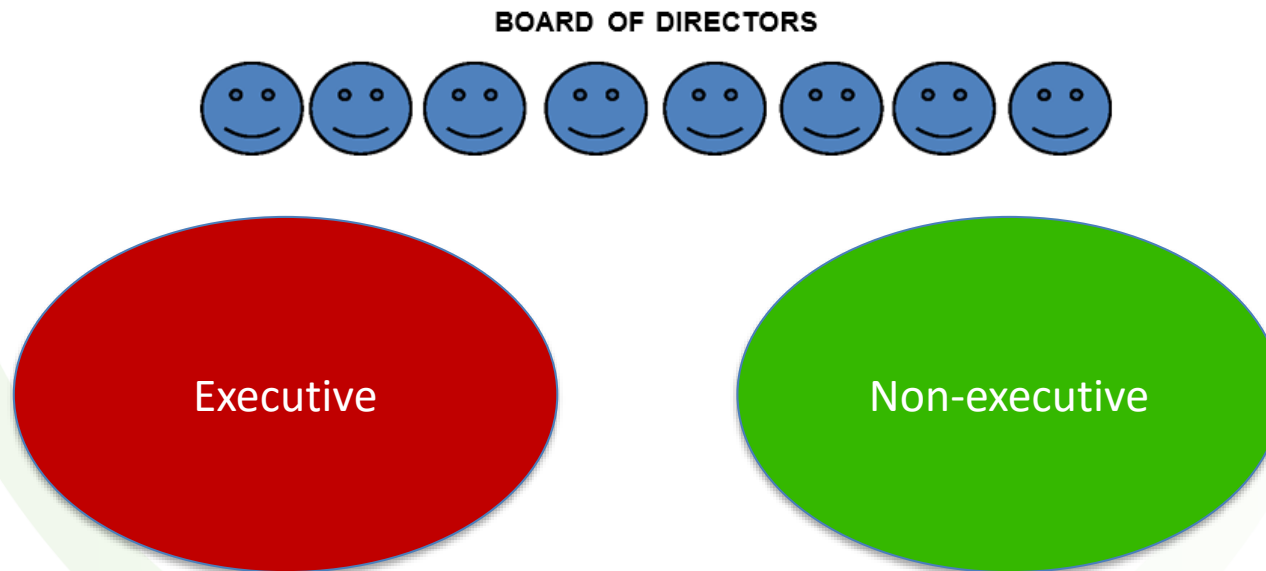
3. King IV Report

Independent non-executive member

- 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.

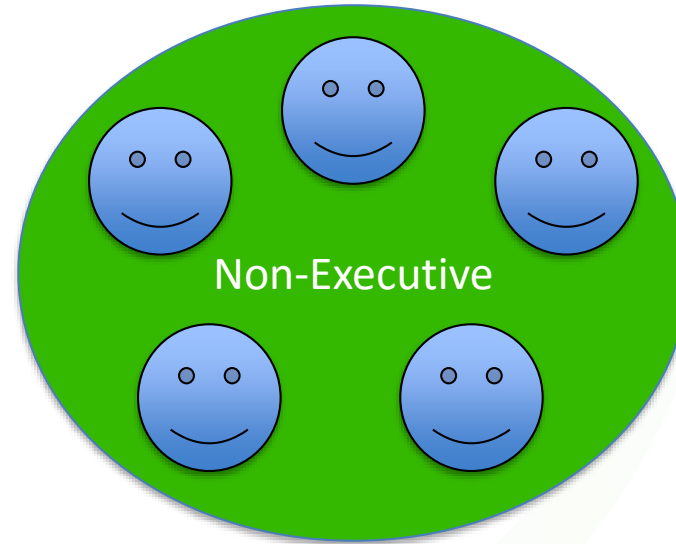
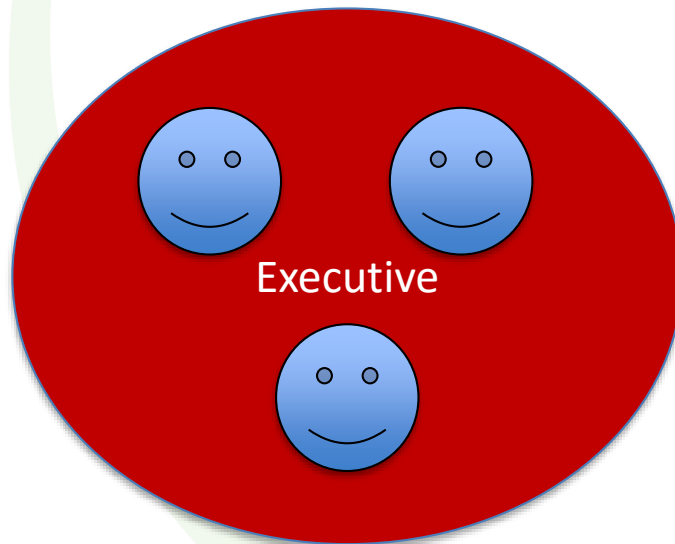
Example – Governing body composition

How should the governing body be structured in order to comply with the requirements of King IV?



Example – Governing body composition

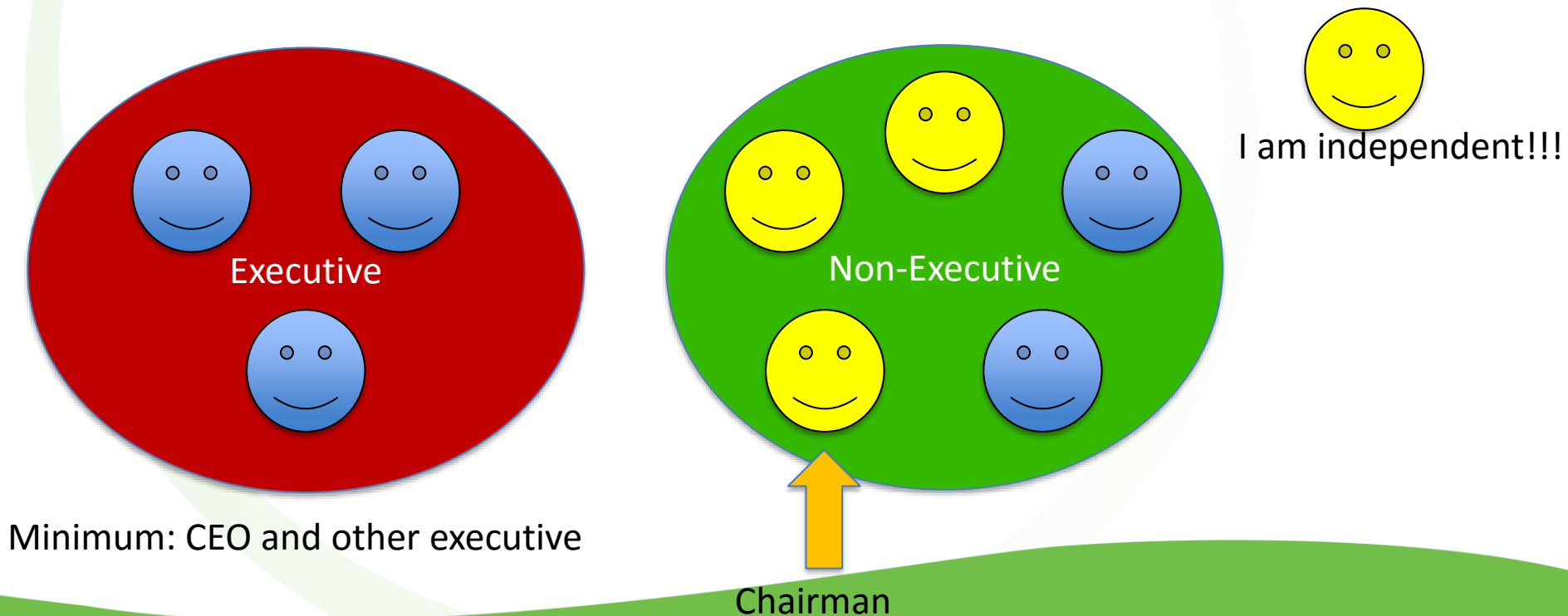
How should the governing body be structured in order to comply with the requirements of King IV?



Minimum: CEO and other executive

Example – Governing body composition

How should the governing body be structured in order to comply with the requirements of King IV?



Quick Quiz 1

Would the following individual qualify as an independent non-executive member in terms of the King IV Report? Justify your answer:

- A partner in the law firm that acts as legal advisors to the company;
- The company's external auditor;
- The company's recently retired CEO;
- A shareholder who holds 3% of the company's shares

Quick Quiz 2

State whether the following are true or false in terms of the King IV Report:

- The chair of the audit committee should be the chair of the board;
- The CEO must chair the remuneration committee;
- The nominations committee should consist of only non-executive directors

3. King IV Report

Compliance Governance – Company Secretary

- Governing body should ensure it has access to professional and independent guidance on corporate governance and its legal duties.
- For some companies, the appointment of a company secretary is a statutory requirement.
- King IV recommends appointing a company secretary or other professional as appropriate for the organisation, to provide professional CG services.

3. King IV Report

Compliance Governance – Company Secretary

The Company Secretary should:

- Be suitably qualified, competent and experienced
- Have an “arms’-length” relationship
- Not be a director
- Prepare and circulate governing body papers
- Elicit responses, input, feedback for governing body and its committee meetings
- Ensure preparation and circulation of minutes of governing body and committee meetings

3. King IV Report Compliance Governance

Study: King IV Report (2016: 63 – 64) and
Jackson & Stent (2016: 4/46 – 4/47)

3. King IV Report Assurance

Principle 15 states:

“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.”

3. King IV Report **Assurance**

Combined assurance model:

- Incorporates and optimizes all assurance services and functions to enable an effective control environment, support the integrity of info used for internal decision-making, and support the integrity of external reports.

3. King IV Report

Assurance

Internal Audit

- Board ensure an effective **risk based** internal audit
- Should follow an approved **risk based internal audit plan**
- Should provide an **overall statement annually** to the effectiveness of the organisation's governance, risk management and control processes.
- The audit committee should be **responsible** for overseeing internal audit
- Should be **strategically** positioned to achieve its objectives
- External, independent quality **review of internal audit function** should be conducted at least once every five years.

Quick Quiz 3

- Why should the internal audit function be independent and not partake in the day-to-day management or operations of the company?
- Who oversees the internal audit function?
- To whom does the Chief Audit Executive report to?
- Who appoints the Chief Audit Executive?
- Should the CAE be a member of the governing body?

3. King IV Report **Assurance**

Study: King IV Report (2016: 68 – 70) and
Jackson & Stent (2016: 4/51 – 4/55)

Corporate Governance

Activities:

- Do all the activities related to this Topic

Tutorial letter 102:

- Do all questions under topic 1 from the prescribed textbook, *Graded Questions on Auditing* (2017)

Assignments and past examination papers:

- Do the assignments (tut 101) and past examination questions (on myUnisa) to see how this topic could be examined
- Remember to read the scenario and the questions carefully, and answer what was asked!
- Remember that Corporate Governance only account for approximately 25% of the exam – do not spend more than 25% of your time on this Topic.
- This is easy marks!

EXAM TECHNIQUE

- When doing the activities, tutorial 102 questions, assignments and past examination papers, take note of how the information is given in the scenario, as well as how the solution is presented. You will notice that marks are available for **applying** the information in the scenario to the requirements of the King IV Report.



Thank **you**

Define tomorrow.

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