

GOVERNANCE OVERSIGHT ROLE OVER STATE OWNED ENTITIES (SOE's)

1 PURPOSE

The purpose of this document is to provide an overview of Government's governance oversight over SOE's.

2 SUMMARY

Corporate governance embodies processes and systems by which SOE's are directed, controlled and held to account. In addition to legislative requirements based on a SOE's enabling legislation, and the Companies Act, corporate governance with regard to SOE's is applied through the precepts of the Public Finance Management Act (PFMA) and run in tandem with the Protocol on Corporate Governance, which encapsulates the principles contained in the King II Report on Corporate Governance.

Governance oversight over SOE's vests in Parliament, the Executive and the Boards of SOE's.

Parliament exercises its role through evaluating the performance of SOE's by interrogating their annual financial statements.

- The Standing Committee on Public Accounts (SCOPA) reviews the annual financial statements and the audit reports of the Auditor-General; and
- The Portfolio Committee exercises oversight over the service delivery performance of SOE's and, as such, reviews the non-financial information contained in the annual reports of SOE's and is concerned with service delivery and enhancing economic growth.

The Executive Authority as owner/shareholder is concerned with appropriate returns on investments and ensuring financial viability of SOE's. The relevant Executive Authority acts as shareholder, while the Minister of Finance and the National Treasury is responsible for financial oversight.

In addition, Government is also the policymaker, concerned with policy implementation of service delivery and acts as regulator. These responsibilities vest in Cabinet as policymaker, the responsible Minister (Executive Authority) and his Department and in some cases the Policy Department (i.e. Shareholder Management of Eskom vests with the Department of Public Enterprises while policy vests with the Department of Minerals and Energy).

Oversight by the Executive Authority rests by and large on the precepts of the PFMA. The PFMA governs/gives authority to the Executive Authority for oversight powers with particular reference to the corporate plans, shareholder's compacts and quarterly reports. The Executive Authority also has the power to appoint and dismiss the Board of an SOE. It must also ensure that the appropriate mix of executive and non-executive directors are appointed and that directors have the necessary skills to guide the SOE.

Shareholder oversight is spread between various shareholder departments while policy departments which, in some instances are not the shareholder department, direct policy.

The Board of Directors of SOE's is the governing body of the SOE. The Board has absolute responsibility for the performance of the SOE and is fully accountable for the performance of the SOE. Governance principles regarding the role and responsibility of SOE Boards are contained in the PFMA and the Protocol on Corporate Governance.

A diagrammatic overview of the current oversight management over SOE's is attached as **(Annexure A)**.

3 PARLIAMENT

3.1 ***Introduction***

The Constitution of South Africa empowers the National Assembly and Provincial Legislatures with an oversight role over their respective Executives.

Section 55(2) of the Constitution deals with the powers of the National Assembly, and states that the National Assembly must provide for a mechanism to:

- Ensure that all executive organs of state in the national sphere of government are accountable to it; and
- To maintain oversight of the national executive authority, including the implementation of legislation, and any organ of the state.

Section 42(3) of the Constitution empowers the National Assembly with the power to scrutinise and oversee the executive action. In addition, Section 92(3)(b) of the Constitution requires that Members of the Cabinet must provide Parliament with full and regular reports concerning matters under their control. The challenge facing members of Parliament is to improve the capacity of the policy/parliamentary Committees to hold Departments and SOE's to account for their performance, using their strategic plans, budget documents and annual reports as the basis.

The PFMA gives effect to financial management that places a greater implementation responsibility with managers and makes them more accountable for their performance. It is left to the Minister/MEC or the Executive (Cabinet) to resolve management failures. The National Assembly and the provincial legislatures are vested with the power to oversee the SOE and the Executive.

3.2 ***Annual Reports***

Annual reports allow Parliament to evaluate the performance of a Department after the end of the financial year. With regard to Departments prior to the year 2000, there was no oversight over non-financial service delivery performance, and Departments only tabled their financial statements and Audit Reports, rather than an annual report. However, reforms since the enactment of the PFMA and Public Service Act requires the Minister of each Department, who might also be the Executive Authority of a SOE, to table an annual report in the legislature within 6 months of the end of each financial year. Section 65 of the PFMA requires the Executive Authority to table the annual reports for SOE's for which they are responsible by 30 September, which is six months after financial year-end of the SOE. This implies that annual reports should be tabled by Parliament a month after the accounting officer has received it from the SOE.

Because it would be impossible for the National Assembly to exercise proper oversight over their Executives by reviewing all performance aspects of the 35 National Departments and \pm 250 National Public Entities, Parliamentary Committees were established to facilitate the oversight role. This division of labour enables the committee members to become experts in different fields, and spend more time doing the actual oversight work.

3.3 ***Roles of different Parliamentary Committees***

3.3.1 *Public Accounts Committee*

The Standing Committee on Public Accounts (SCOPA) fulfils the responsibility of reviewing the audit reports of the Auditor General. This Committee plays an important and specialised role of being the protector of public monies. In fulfilling this role the Committee focuses on the following:

- Issues raised in the General Report of the Auditor-General on Audit outcomes;
- Issues of financial probity as highlighted in the audit report or disclosed in the management report or notes to the financial statements;
- Compliance with the PFMA, Treasury Regulations, the Audit Committee and the management report of the accounting officer;

- Interrogation and evaluation of instances of over-expenditure and instances of unauthorised expenditure;
- Interrogation of instances relating to irregular, fruitless and wasteful expenditure;
- The functioning of risk management systems; and
- Corporate governance of departments, public entities, and constitutional institutions.

3.3.2 *Portfolio Committees*

Given their involvement in the legislative, budget and in-year monitoring processes, Portfolio Committees exercise oversight of the service delivery performance of SOE's.

Portfolio Committees fulfill the responsibility of reviewing non-financial information contained in the annual reports of SOE's. These Committees should exercise oversight as to whether entities have delivered on the service delivery commitments they made in their corporate plans. They must also consider the SOE's financial performance in order to develop a holistic understanding of the SOE's performance.

To give effect to this role, these Committees focus on the following in considering the annual reports of SOE's:

- The technical quality of the annual reports produced by Departments and SOE's;
- The economic, efficiency and effectiveness of service delivery as measured by performance indicators presented in the annual reports;
- Evaluating management's explanation as to why the entity's service delivery performance did not attain the targets set in the corporate plans;
- Equity of service delivery; and
- Investigating the circumstances that led to financial underperformance and the impact this had on service delivery and the measures taken by management to rectify the situation.

The National Assembly Portfolio Committees are responsible for overseeing the relevant National Department for which they are responsible. SOE's report to an Executive Authority (Shareholder Ministry) and their annual reports are submitted to both the Public Accounts Committee and the relevant Portfolio Committee by the Executive Authority.

3.3.3 *Links between Portfolio Committees and the Public Accounts Committee (SCOPA)*

Ideally the oversight process should provide a complete picture of an SOE's performance, encompassing its finances, its systems, its

human resources and its service delivery performance. In addition, the exercising of the SOE's mandate must also be scrutinised to ensure that policy objectives are being met. While SCOPA focuses on financial matters and the Portfolio Committee focuses on policy and service delivery, the sharing of information between them is important.

3.3.4 *Input by other role-players*

Part of the success of the oversight process depends on the extent to which Portfolio Committees and SCOPA are able to leverage inputs by other role-players.

3.3.4.1 The Auditor-General

The Auditor-General is a state institution accountable to the National Assembly. In terms of Section 188 of the Constitution, the Auditor-General must audit and report on the accounts, financial statements and financial management of all national and provincial departments, all municipalities and any other institution or accounting entity required by national and provincial legislation. In this regard the Auditor-General must submit audit reports to the relevant legislature.

3.4.4.1 Departments

SOE's are institutions/entities through which the Executive delivers on services. Departmental targets should incorporate the service delivery targets of SOE's that report to their Executive Authorities. The annual shareholders' compact documents the agreements between the SOE and the Executive Authority on targets (KPI's).

4 GOVERNMENT'S ROLE AS OWNER, POLICY MAKER AND REGULATOR

4.1 ***Oversight role of the Executive Authority***

4.1.1 *Introduction*

The Executive plays various roles in its relationship with the SOEs. On one hand, Government as an owner and shareholder is concerned with obtaining a suitable return on investments, and ensuring the financial viability of the SOE. On the other hand, Government as policymaker is concerned with the policy implementation of service delivery. Finally, Government as regulator is concerned with the industry practices of SOEs, pricing structures, and the interests of consumers.

The Executive Authority (Responsible Minister) is the governing body that is responsible for the effective and efficient delivery of the service delivery requirements identified and also exercises shareholder

oversight. A list of Schedule 2 and 3B Public Entities and their Executive Authorities is provided (**Annexure B**). The Executive Authority plays a constructive and proactive role in the governance of the SOE and in the achievements of its service delivery objectives. Oversight is concerned with the reviewing, monitoring and overseeing of the affairs, practices, activities, behavior and conduct of the SOE, in order to be satisfied that the SOE's affairs and business are being conducted in the manner expected and in accordance with all normal commercial, legislative and other prescribed or agreed norms.

This includes the review, monitoring and overseeing of the fact that the management of the SOE, its strategic and business planning, its conduct of its business operations and its reporting thereon and accounting thereof, is being effectively managed by the SOE's executive management and staff and that the assets and goodwill are being properly protected and preserved.

The Executive Authority's corporate governance responsibility as shareholder, involves ensuring that, from the Board of directors downwards, and also in respect of accountability of the Board upwards to the shareholder, all the necessary and appropriate corporate governance structures, procedures, practices and controls and safeguards, are established, properly implemented and operate effectively in the SOE concerned.

If the Executive Authority is the shareholder of an SOE whose activities represents a fully commercial viable and profitable enterprise and operation, then the shareholder's concern for return on investment (ROI) entails reviewing, monitoring and overseeing that the SOE's strategic and business plans, as well as its actual operations, delivery and performance are met and are achieving any expected and agreed levels of return on investment and/or return on asset.

Financial performance from the shareholder's perspective is about monitoring whether the SOE has:

- Appropriate and effective planning and budgeting processes in place [Section 52 of the PFMA];
- The financial management and control structures and processes are such that accurate, timeous and reliable recording and reporting of all financial transactions takes place [Section 51 of the PFMA];
- That the appropriate financial management systems and controls are in place to ensure the effective management of the financial affairs of the SOE [Section 51 of the PFMA]; and
- That the financial affairs and performance of the SOE as reported is acceptable in terms of the corporate plans and shareholders compacts [Section 52 and Treasury Regulations 29.1].

The administration concerns of the owner/shareholder focuses on the appropriateness, adequacy and effectiveness of the organisational structure, administrative structures, administrative and management procedures and practices within the SOE, to ensure that the infrastructure and practices are in place to manage and conduct a well run and optimally performing business and organisation.

4.2 **Government's policy role**

4.2.1 *Introduction*

The ultimate authority to direct policy vests in Cabinet. Cabinet decides on the appropriate and desired policy to meet the mission and mandate of the country. This policy, through the appropriate Minister and Department is then issued as a policy directive by the Minister through the applicable policy department, to the relevant SOE charged with implementing and delivering against that policy.

Having issued the policy directive, the Minister and the Policy Department should ensure that the necessary structures, processes, practices, and business activities have been put in place within the SOE, to facilitate the implementation of the policy and the delivery of the required service or product. Thereafter, the Policy Department's role would entail the monitoring, reviewing and overseeing of service delivery from the SOE to ensure that service delivery is consistent with the expected outputs and represents delivery of the policy. Treasury Regulation 30.2 provides that the accounting authority of a public entity must make quarterly reports to the Executive Authority in order to facilitate effective performance monitoring, evaluation and corrective action. However, the dilemma with regard to effective oversight is that in many instances the policy Minister and department is not the Executive Authority (i.e. Eskom, Transnet, Denel, etc), while these reports are submitted to the Executive Authority.

In addition, policy directives may impact on the viability of the SOE, which affects the financial performance and shareholder monitoring by the Executive Authority.

4.2.2 *Corporate Plan and Shareholder's Compact*

The oversight role of the Executive Authority and their Department is done in accordance with Section 52 of the PFMA, which deals with annual budgets and corporate plans. Section 52 provides that the board of the SOE must annually submit:

- “(a) a projection of revenue, expenditure and borrowings for that financial year in the prescribed format; and
- (b) a corporate plan in the prescribed format covering the affairs of that public entity or business enterprise for the following three

financial years, and, if it has subsidiaries, also the affairs of the subsidiaries.”

In addition, Treasury Regulation 29.1 deals with corporate plans that must be submitted by SOE's (Schedule 2 and 3B). This regulation provides that the accounting authority for a public entity listed in Schedule 2 and 3B must annually submit a corporate plan to their Executive Authority and the relevant Treasury. The corporate plan must cover a period of 3 years and include:

- Strategic objectives and outcomes identified and agreed on by the executive authority in the shareholder's compact;
- Strategic and business initiatives as embodied in business function strategies;
- Key performance measures and indicators for assessing the entity's performance in delivering the desired outcomes and objectives;
- A risk management plan;
- A fraud prevention plan;
- A materiality/significant framework, referred to in Treasury Regulation 28.3.1;
- A financial plan addressing -
 - Projections of revenue, expenditure and borrowings;
 - Asset and Liability Management;
 - Cash flow projections;
 - Capital expenditure programmes; and
 - Dividend policies.

In addition to the Corporate Plan, the Executive Authority of a SOE must annually conclude a shareholders' compact with the SOE falling under its control. Treasury Regulation 29.2.2 directs that:

“The shareholder's compact must document the mandated key procedures for quarterly reporting to the Executive Authority in order to facilitate effective performance monitoring, evaluation and corrective action.”

The shareholder's compact represents an agreement between the relevant Executive Authority at national or provincial government level, as the majority shareholder and the Accounting Authority of the public entity, with respect to performance expectations and parameters. It does not replace the strategic, corporate and business plans but is rather complimentary to these. It describes the relationship between the signatories and identifies the behaviour that would be required on both sides to support effective management and performance of the entity.

The shareholder's compact finds its origin, on the one side, in the protocol of corporate governance in the public sector, which is time *independent*. On the other, it is anchored in the strategic, corporate

and business plans of the public entity, which are time *dependent*. The shareholder's compact results from the need to have a clear understanding of the relationship between Government and the public entities as an extension of delivering public service through business entities. It is a product of research and development into corporate governance and performance agreements between majority/sole shareholders and boards, and subsequent discussions and debate with the parties concerned.

This document forms a framework within which entities can reach agreement with the Executive Authority on objectives to be pursued in reaching the vision of the organisation. It also includes guidelines for a restructuring plan upon which the shareholder and the accounting authority can reach agreement prior to the implementation of the annual budget.

It is crucial to note that the shareholder's compact can derive information required from the corporate plan that has already been prepared by the public entity.

4.2.3 *Executive Authorities' power to dismiss and appoint the Board*

The Executive Authority has the power to constitute the Board and to dismiss directors in the event of a SOE not performing satisfactorily.

4.2.4 *National Treasury's role*

The role of the National Treasury as the protector of the National Revenue Fund and the sovereign credit rating of the country is to exercise financial oversight through:

- Setting reporting guidelines to promote and enforce transparency in respect of revenue, expenditure, assets and liabilities of SOE's;
- Oversight over the funding/borrowing programmes of SOE's;
- Controlling the utilisation of contingent liabilities; and
- Effective treasury management models.

The above functions of the National Treasury is provided by the PFMA as follows:

- Promotion and enforce transparency and effective management in respect of revenue, expenditure, assets and liabilities of departments, Public Entities and constitutional institutions [Section 6(1)(g)];
- The approval/evaluation of the creation of any new entity that a Public Entity intends to establish [Section 51(1)(g)];
- Receipt of corporate plans [Section 52];

- The National Treasury may prescribe information, returns, documents, explanations and motivations as required [Section 54(1)];
- Must be informed of the transactions undertaking in terms of Section 54(2);
- Receipt of draft and final Annual Financial Statements within the timeframes set out in Section 55;
- Authority to borrow, issue a guarantee, indemnity or security for a Schedule 3(b) Public Entity vests with the Minister of Finance who acts on advice of the National Treasury's Government Guarantee Certification Committee [Section 66(3)(b)]; and
- A Public Entity authorised to borrow money must provide a borrowing programme for the year and may not borrow in foreign currency above a prescribed limit [Section 66(7)]

5 GOVERNMENT'S ROLE AS REGULATOR

Government's role as regulator is more focused on the industry within which the SOE operates or which the SOE serves. The Regulator would concern itself with issues like pricing, consumer interest and industry issues and interest. Although the regulator is a government agency and is carrying out a government role, the relationship of a regulator with the SOE can be and should be an independent, objective, arms length relationship with the SOE, unlike the more direct relationship that Government as shareholder and policy-maker, would have.

6 THE OVERSIGHT ROLE OF THE BOARD OF DIRECTORS OF SOE's

6.1 **Introduction**

The Board of Directors is the governing body of a SOE. All SOE's should be headed by and controlled by an effective and efficient Board, comprising of the appropriate mix of executive and non-executive directors representing the necessary skills to strategically guide the SOE. The Board has an absolute responsibility for the performance of the SOE and is fully accountable to the SOE for such performance. The Board should also give strategic direction to the SOE.

6.2 **Mission of the Board**

The mission of the Board is to fulfil the mandate of the SOE in accordance with the strategic objectives of the Government, whilst achieving its commercial objectives.

The Board is ultimately accountable and responsible to the Shareholder for the performance and affairs of the SOE. The Board

must therefore retain full and effective control over the SOE and must give strategic direction to the SOE's management. The Board is also responsible for ensuring that the SOE complies with all relevant laws, regulations and codes of business practice.

In addition, the Board has a responsibility to the broader stakeholders, which include the present and potential beneficiaries of its products and services, clients, lenders and employees.

6.3 ***Fiduciary responsibility***

The individual directors and the Board as a whole of the SOE, both executive and non-executive, carry full fiduciary responsibility in terms of the Companies' Act and the Public Finance Management Act.

6.4 ***Powers and duties of the Board of Directors***

6.4.1 *Public Finance Management Act*

Extracts from the PFMA and the Treasury Regulations pertaining to the Powers and Duties of the Board of Directors of a SOE are attached as **(Annexure C)**. The Board shall produce an Annual Budget and Corporate Plan (Section 52 of the PFMA and Treasury Regulation 29.1) which shall be submitted to the accounting officer for the line department, as designated by the responsible Minister and to the National Treasury, at least one month or another period as agreed with National Treasury, before the start of its financial year, consisting of the following:

- A projection of revenue, expenditure and borrowings for that financial year in the prescribed format; and
- A corporate plan in the prescribed format covering the affairs of the SOE for the following three financial years, and, if it has subsidiaries, also the affairs of the subsidiaries.

Without derogating from any duty imposed by law, the Board shall:

- Ensure that the executive management implements the SOE's strategy as established from time to time;
- Ensure that the SOE has effective, efficient and transparent systems of operational, risk management and financial internal controls [Section 51(1)(a)(i)];
- Monitor the activities of the executive management;
- Provide information on the activities of the SOE to those entitled to it;
- Ensure the succession, and approve the appointment, of senior executives;
- Ensure that the SOE operates ethically;

- Address the adequacy of retirement and health care benefits and the funding thereof;
- Ensure that the SOE has and maintains a system of internal audit under the control and direction of an audit committee complying with and operating in accordance with regulations and instructions prescribed in terms of sections 76 and 77 of the PMFA;
- Ensure that the SOE has and maintains an appropriate procurement and provisioning system which is fair, equitable, transparent, competitive and cost-effective [Section 51(1)(a)(iii)];
- Ensure that all applicable black economic empowerment legislative frameworks and requirements are complied with; and
- Ensure that the SOE has and maintains a system for properly evaluating all major capital projects prior to a final decision on the project.

The Board must take effective and appropriate steps to [Section 51(1)(b)]:

- Collect all revenue due to the SOE;
- Prevent irregular expenditure, fruitless and wasteful expenditure, losses resulting from criminal conduct, and expenditure not complying with the operational policies of the SOE; and
- Manage available working capital efficiently and economically.

The Board is responsible for the management, including the safeguarding, of the assets and for the management of the revenue, expenditure and liabilities of the SOE [Section 51(1)(c)].

The Board must comply with any tax, levy, duty, pension and audit commitments as required by the Statutes [Section 51(1)(d)].

The Board must take effective and appropriate disciplinary steps against any employee of the SOE who [Section 51(1)(e)]:

- Contravenes or fails to comply with a provision of the PMFA;
- Commits an act which undermines the financial management and internal control system of the SOE; or
- Makes or permits an irregular expenditure or a fruitless and wasteful expenditure.

The Board is responsible for the submission by the SOE of all reports, returns, notices and other information to Parliament, the Member, and to the Treasury, as may be required by the Statutes [Section 51(1)(f)].

The Board must promptly inform the Treasury on any new entity which the SOE intends to establish or in the establishment of which it takes the initiative, and allow the Treasury a reasonable time to

submit its decision prior to formal establishment, and seek approval of the establishment of the new entity from their Executive Authority [Section 51(1)(g)].

The Board must ensure that the SOE has an Affirmative Action Plan in place to advance members of the groups historically discriminated against, including on the grounds of race, colour, origin, gender and disability.

The directors shall, in the exercise of their powers, use their best endeavours to achieve the objectives of the SOE as set out in the memorandum of association of the SOE and as conveyed to them by the Executive Authority.

If the Board is unable to comply with any of the responsibilities determined for it in the PMFA, it must promptly report the inability, together with reasons, to the Minister and the National Treasury [Section 51(2)].

The Board of an SOE in terms of Section 55 of the PFMA:

- Must keep full and proper records of the financial affairs of the SOE;
- Prepare financial statements for each year in accordance with GAAP;
- Must submit the draft financial statements within two months after year-end to the treasury and auditors for auditing; and
- Must submit the audited statements within 5 months after the financial year-end to the Executive Authority, National Treasury and the Auditor-General.

The Board must annually (Treasury Regulation 29.2) in consultation with its Executive Authority conclude a shareholder's compact. The shareholder's compact must document the mandated key performance measures and indicators to be attained by the SOE as agreed between the parties. The Board of an SOE must also (Treasury Regulation 29.3) establish procedures for quarterly reporting to the Executive Authority to facilitate effective performance monitoring, calculation and corrective action.

6.4.2 *Protocol on Corporate Governance*

The Protocol on Corporate Governance was accepted by Cabinet in 2003 and all Public Entities have been informed that they must comply with the principles contained therein. The Protocol is a code of conduct similar to the King Report on Corporate Governance and has not been legislated. It encapsulates the King II Report and aligns corporate governance principles to the PFMA, while striving to maintain the independence of SOE's.

The Government, as the major shareholder in SOE's, is exposed to a wide range of risks associated with the operations of SOE's, including financial, reputation, political and operational risks. It is the responsibility of each Executive Authority to ensure that these risks are identified, reduced and managed. SOE's must report and account their financial and non-financial performance to the Executive Authority, while maintaining independence in the conduct of their duties free from day-to-day involvement by the Executive Authority. The purpose of the Protocol is to guide this relationship.

With regard to governance issues the Protocol states that:

The Government's relationship to its SOE's is similar to the relationship between a holding company and its subsidiaries, features of which include:

- A strong interest in the financial performance of the SOE;
- Reporting and accountability arrangements that facilitate an appropriate oversight by the shareholder; and
- Remedial action by the shareholder where the SOE's strategic direction deviates from that preferred by the shareholder.

The relevant Executive Authority, as contemplated in the PFMA, and the Minister of Finance represent the Government's ownership interest in the SOE's. The Executive Authority acts as shareholder while the Minister of Finance and the National Treasury is responsible for financial oversight.

The guiding principles of the Protocol are:

- The Executive Authority should exercise policy control over the SOE's consistent with their accountability to Parliament and the public;
- The Executive Authority should set clear objectives for SOE's.
- Any Social Service Obligations that a SOE is to undertake should generally be specified through a Shareholder's Compact; and
- The directors of a SOE should ensure the development of business strategies, policies and procedures and monitor management in the implementation thereof.

The directors of a SOE should ensure that:

- The SOE's activities are conducted so as to minimise any divergence of interests between the SOE and the shareholder;
- SOE's are managed in the best interests of the SOE's, shareholder and other stakeholders;
- SOE's and their officers maintain the highest standards of integrity, accountability and responsibility; and

- As recommended by the King Code, the Board has a charter setting out its responsibilities, which should be disclosed in its annual report. At a minimum, the charter should confirm the board's responsibility for the adoption of strategic plans, monitoring of operational performance and management, determination of policy processes to ensure the integrity of the SOE's risk management and internal controls, communication policy, and director selection, orientation and evaluation.

The Boards of SOE's constitute a fundamental base for the application of corporate governance principles in SOE's. Each SOE should be handled and controlled by an effective and efficient Board, the majority of which should be non-executive to ensure independent and objectivity in decision-making.

The role of the Board is as follows:

- It holds absolute responsibility for the performance of the SOE;
- It retains full and effective control over the SOE;
- It has to ensure that the SOE complies with applicable laws, regulations and government policy;
- It has unrestricted access to information of the SOE;
- It formulates, monitors, reviews corporate strategy, major plans of action, risk policy, annual budgets and business plans;
- It ensures that the shareholders' performance objectives are achieved;
- It manages potential conflicts of interest;
- It develops a clear definition of levels of materiality;
- The Board must attend annual meetings;
- It ensures financial statements are prepared;
- The Board must appraise the performance of the Chairperson;
- It must ensure effective Board induction; and
- Must maintain integrity, responsibility and accountability.

Since a Board cannot attend to all the matters effectively the Protocol recommends the establishment of the following committees:

- Audit Committee;
- Remuneration Committee;
- Nomination Committee; and
- Risk Management Committee

In line with the precepts of the PFMA the Protocol states that the relationship between the Executive Authority and SOE Boards should be governed by a shareholder's compact. The Executive Authority should closely monitor the extent to which the Board as a whole achieve the objectives and specific performance targets set, and where necessary, effect remedial action.

With regard to the role of the Chief Executive Officer the Protocol states:

“Unless otherwise agreed in the shareholders agreement or shareholder’s compact (as the case may be) the Executive Authority should appoint the chief executive officer whose role should, preferably, be separate from that of the chairperson. The Executive Authority should consult with the Board about its preferred candidate for the position of Chief Executive Officer and provide sufficient time for the Board to consider the candidate and respond prior to an appointment being made. The chief executive officer’s role should focus mainly on the operations of the SOE, ensuring that the SOE is run efficiently and effectively and in accordance with the strategic decisions of the Board. The chief executive officer is accountable to the board.”

Regarding financial governance the Protocol relies on the PFMA as the principle Act stipulating the rules and regulations related to financial management of SOE’s.

6.4.3 *Independent Auditors*

The Auditors of SOE’s need to confirm in the Auditors Report that the SOE has complied with the PFMA and the Protocol on Corporate Governance.

Compiled by:

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Date: 2005/11/25**

ANNEXURE B**MAJOR PUBLIC ENTITIES**

NO	SCHEDULE 2	DEPARTMENT
1	Air Traffic and Navigation Service Company	Transport
2	Airport Company of South Africa	Transport
3	Alexkor	Public Enterprises
4	Armcor	Defence
5	Central Energy Fund	Minerals and Energy
6	Denel	Public Enterprises
7	Development Bank of Southern Africa	National Treasury
8	Eskom Holding (Pty) Ltd	Public Enterprises
9	Industrial Development Trust	Public Works
10	Industrial Development Corporation of SA	Trade and Industry
11	Land and Agricultural Bank of South Africa	Agriculture
12	South African Broadcasting Corporation	Communications
13	South African Forestry Company	Public Enterprises
14	South African Nuclear Energy Corporation	Minerals and Energy
15	South African Post Office Limited	Communications
16	Telkom SA Limited	Communications
17	Trans-Caledon Tunnel Authority	Water Affairs and Forestry
18	Transnet Limited	Public Enterprises

NO	SCHEDULE 3B	DEPARTMENT
1	Albany Coast Water Board	Water Affairs and Forestry
2	Amatola Water Board	Water Affairs and Forestry
3	Aventura	Public Enterprises
4	Bala Farms (Pty) Ltd LIQUIDATED AND DEREGISTERED	Land Affairs
5	Bloem Water	Water Affairs and Forestry
6	Botshelo Water Board	Water Affairs and Forestry
7	Bushbuckridge Water Board	Water Affairs and Forestry
8	Council for Minerals Technology (MINTEK)	Minerals and Energy
9	Council for Scientific and Industrial Research (CSIR)	Trade and Industry
10	Export Credit Insurance Corporation of SA Limited (ECIC)	Trade and Industry
11	Ikangala Water	Water Affairs and Forestry
12	Inala Farms (Pty) Ltd UNDER LIQUIDATION	Land Affairs
13	Khula Enterprises	Trade and Industry
14	Lepelle Northern Water	Water Affairs and Forestry
15	Magalies Water	Water Affairs and Forestry
16	Mhlathuze Water	Water Affairs and Forestry
17	Namakwa Water	Water Affairs and Forestry
18	Ncera Farms (Pty) Ltd	Agriculture
19	Ntsika Enterprises Now SEDA	Trade and Industry
20	Onderstepoort Biological Products	Agriculture
21	Overberg Water	Water Affairs and Forestry
22	Pelladrift Water Board	Water Affairs and Forestry
23	Rand Water	Water Affairs and Forestry
24	SA Bureau of Standards – SABS	Trade and Industry
25	SA Rail Commuter Corporation Limited	Transport
26	SASRIA	National Treasury
27	Sedibeng Water	Water Affairs and Forestry
28	Sentech	Communications
29	Umgeni Water	Water Affairs and Forestry
30	Umsobomvu Youth Fund	Labour

ROLE OF THE BOARD**AS PRESCRIBED BY KING CODE II ON CORPORATE GOVERNANCE:**

- The Board is appointed by and accountable to the Shareholder for its stewardship of the company and the company's assets and resources.
- The company's articles of association will reserve the powers to the board to enable it to fulfil its responsibilities.
- All companies should be headed by an effective Board, which can both lead and control the company.
- The Board has a collective responsibility to provide effective corporate governance that involves a relationship between the management of the company, its board, its shareowners and other stakeholders to determine the company's purpose and values.
- The Board should strive to focus on performance in directing the commercial and economic fortunes of the company.
- The Board should comprise a balance of executive and non-executive directors, preferably with a majority of non-executive directors of who should be independent of management for minority interest to be protected.
- The Board should be composed of individuals of integrity who bring a blend of skill, knowledge, objectivity, experience and commitment to the board, under the firm and objective leadership of a chairperson.
- The Board should be able to exercise objective judgement on the corporate affairs of the business enterprise, independent from management but with sufficient management information to enable a proper and objective assessment to be made by directors collectively.
- The Board should guide and set the pace of the company's current operations and future developments.
- Strategies, policies, mutually agreed management performances criteria and business plans of the company must be clearly defined and reliably measured.
- The Board should ensure that internal control procedures provide reliable and valid information for monitoring and evaluation. Internal controls include not only financial matters but also operational and compliance controls and management of the business risk associated with the company.

PUBLIC FINANCE MANAGEMENT ACT (PFMA) PRECEPTS:

- **Section 50** entails the Fiduciary duties of Accounting Authorities.
- **Section 50 (1)** provides that the accounting authority for a public Entity must:
 - a) exercise the duty of utmost care to ensure reasonable protection of the assets and records of the public entity;
 - b) act with fidelity, honesty, integrity and in the best interest of the in managing the financial affairs of the public entity;
 - c) on request, disclose to the executive authority responsible for that public entity all material facts; and
 - d) seek to prevent any prejudice to the financial interests of the state.
- **Section 50 (2)** provides that a member of an accounting authority may not-
 - a) act in a way that is inconsistent with the responsibilities assigned to the accounting authority in terms of this Act; or
 - b) use the position or privileges of, or confidential information obtained as a member of accounting authority for personal gain or to improperly benefit another person.

A member of an accounting authority must-

- a) disclose to the accounting authority any direct or indirect personal or private business that they may have in any matter before the accounting authority; and
- b) withdraw from the proceedings of the accounting authority when that matter is considered.

GENERAL RESPONSIBILITIES OF ACCOUNTING AUTHORITIES:

- **Section 51 (1)** An accounting authority for a public entity-
 - a) must ensure that that public entity has and maintains-
 - i) effective, efficient and transparent systems of financial and risk management and internal control;
 - ii) a system of internal audit control.
 - iii) Appropriate procurement and provisioning system which is fair, equitable, transparent, competitive and cost effective;
 - iv) A system of properly evaluating all major capital projects prior to a final decision on the project;
 - b) must take effective and appropriate steps-
 - i) to collect all revenue to the public entity concerned;
 - ii) and to prevent irregular expenditure, fruitless and wasteful expenditure, losses resulting from criminal conduct; and

- iii) manage available working capital efficiently and economically;
 - c) is responsible for the management of assets and for the management of revenue, expenditure and liabilities of that public entity;
 - d) must comply with any tax, levy, duty, pension and audit commitments as required by legislation;
 - e) must take effective and appropriate disciplinary steps against any employee of the public entity who-
 - i) contravenes or fails to comply with the provisions of this Act;
 - ii) commits an act which undermines the financial management and internal control system of the public entity;
 - iii) makes or permits an irregular expenditure or a fruitless and wasteful expenditure;
 - f) is responsible for the submission by the public entity of all reports, returns, notices and other information to Parliament or the relevant provincial legislature and to the relevant executive authority or treasury, as may be required by this Act;
 - g) must promptly inform the National Treasury on any new entity which that public entity intends to establish or in the establishment of which it takes the initiative, and allow the National Treasury a reasonable time to submit its decision prior to formal establishment; and
 - h) must comply, and ensure compliance by the public entity, with the provisions of this Act and any other legislation applicable to the public entity.
- **Section 51 (2)** provides that if an accounting authority is unable to comply with any of the responsibilities determined for an accounting authority in this part, the accounting authority must promptly report the inability, together with reasons, to the relevant executive authority and treasury.
- **Section 52 - Annual budget and corporate plan by Schedule 2 public entities and government business enterprises**
 The accounting authority for a public entity listed in Schedule 2 or a government business enterprise listed in Schedule 3 must submit to the executive authority and to the relevant treasury at least one month before the start of its financial year-
 - a) a projection of revenue , expenditure and borrowings for that financial year in the prescribed format; and
 - b) a corporate plan in the prescribed format covering the affairs of that public entity or business enterprise for the following three financial years, and if it has subsidiaries, also the affairs of the subsidiaries.

- **Section 54** – Information to be submitted by accounting authorities.
- **Section 54 (1)** the accounting authority must submit to the relevant treasury such information, returns, documents, explanations and motivations as may be prescribed.
- **Section 55** - Annual report and financial statements
- **Section 55 (1)** the accounting authority for a public entity-
 - a) must keep full and proper records of the financial affairs of the public entity;
 - b) prepare financial statements for each year in accordance with GAAP;
 - c) must submit those financial statements within two months after year-end of the financial year to relevant treasury and auditors for that public entity for auditing; and
 - d) must submit within five months of year end of a financial year end to the treasury , to the executive authority responsible for that public entity and to the Auditor –General
- **Section 56** - Assignment of powers and duties by accounting authorities
- **Section 56 (1)** the accounting authority for a public entity may-
 - a) in writing delegate any of the powers entrusted to an official in that public entity; or
 - b) instruct an official in that public entity to perform any of the duties assigned to the accounting authority in terms of the PFMA.
- **Section 56 (2)** a delegation or instruction to an official in terms of subsection (1):
 - a) is subject to any limitations and conditions the accounting authority may impose;
 - b) may either be to specific individual or the holder of a specific post; and
 - c) does not divest the accounting authority of the responsibility concerning the exercise of the delegated power or performance of the assigned duty.
- **Section 56 (3)** the accounting authority may confirm, vary or revoke any decision taken by an official as a result of a delegation.
- **Section 66 (3)** - Public entities listed in Schedule 2 may borrow money, issue a guarantee, indemnity or a security or enter into any transaction that bind or may bind that public entity to any future financial commitment only through the Accounting for that public entity.

- **Section 86 - the accounting authority is guilty of an offence and liable on conviction to a fine or to imprisonment for a period not exceeding five years, if that accounting authority wilfully or in a gross negligent way fails to comply with a provision of Section 50,51 or 55.**

TREASURY REGULATIONS:

ANNUAL FINANCIAL STATEMENTS AND ANNUAL REPORTS

28.1 Financial statements [Section 55 of the PFMA]

28.1.1 The annual financial statements must include a report by the accounting authority which must include the disclosure of remuneration in respect of all:

- members of the accounting authority;
- the chief executive officer or the person in charge of the public entity;
- the chief financial officer;
- persons serving on the public entity's senior management; and
- members or persons in (a) to (d) above serving in other entities under the ownership control of the public entity.

28.1.2 Remuneration paid or receivable by the members or persons in paragraph 28.1.1 (a) to (e) shall be disclosed in aggregate and per member or person for the last financial period.

28.1.3 Disclosures in terms of paragraphs 28.1.1 and 28.1.2 is required whether such payment is receivable in the capacity as indicated in paragraph 28.1.1 (a) to (d) or in any other capacity.

28.1.4 The disclosure requirements in paragraphs 28.1.1 to 28.1.3 shall include:

- fees for services as a member or person in paragraph 28.1.1 (a) to (d);
- basic salary;
- bonuses and performance related payments;
- sums paid by way of expense, salary or other allowances;
- contributions made to any pension fund, medical aid, insurance scheme, etc;
- any commission, gain or profit sharing arrangements;
- any share options, including their strike price and period; and
- any other material benefits received.

28.1.5 Public entities listed in Schedule 3A or 3C of the Act may, after consultation with the designated accounting officer, submit

their annual financial statements and any other information required in terms of the Act to the designated accounting officer for inclusion in the relevant department's annual report.

- 28.1.6 In terms of section 55(1)(b) of the Act, public entities shall prepare financial statements in accordance with generally accepted accounting practice. Should the statements materially depart from Statements of GAAP, the financial statements must provide disclosure of the departure, the particulars thereof, the reasons therefore and the effect of such departure on the financial statements.

28.2 Annual reports [Section 55(1)(d)(i) of the PFMA]

- 28.2.1 Any material losses through criminal conduct and any irregular and fruitless and wasteful expenditure must be disclosed as a note to the annual financial statements of the public entity.

- 28.2.2 Particulars of the public entity's strategic objectives and outcomes as identified and agreed on by the executive authority, the key performance measures and indicators for assessing the entity's performance in delivering the desired outcomes and objectives and the entity's actual performance against the strategic objectives and outcomes, must be disclosed in the annual report of the public entity.

28.3 Materiality and Significance [Sections 55(2) and 54(2) of the PFMA]

- 28.3.1 For purposes of material [section 55(2) of the Act] and significant [section 54(2) of the Act], the accounting authority must develop and agree a framework of acceptable levels of materiality and significance with the relevant executive authority.

CORPORATE PLANNING, SHAREHOLDER'S COMPACTS AND ANNUAL BUDGETS

29.1 Corporate plans [Section 52 of the PFMA]

- 29.1.1 The corporate plan must cover a period of three years and must include -
- (a) strategic objectives and outcomes identified and agreed on by the executive authority in the shareholder's compact;
 - (b) strategic and business initiatives as embodied in business function strategies;
 - (c) key performance measures and indicators for assessing the entity's performance in delivering the desired outcomes and objectives;

- (d) a risk management plan;
- (e) a fraud prevention plan;
- (f) a materiality/significant framework, referred to in Treasury Regulation 28.3.1;
- (g) a financial plan addressing -
 - (i) projections of revenue, expenditure and borrowings;
 - (ii) asset and liability management;
 - (iii) cash flow projections;
 - (iv) capital expenditure programmes; and
 - (v) dividend policies.

29.1.2 The executive authority of a public entity may request additional information to be included in the corporate plan.

29.1.3 Public entities listed in Schedule 2 or 3B must:

- (a) submit a three-year borrowing programme (beginning with the first financial year of the corporate plan) with their corporate plan to the National Treasury; and
- (b) submit quarterly reports on the borrowing programme to the National Treasury, reflecting actual borrowing for that quarter and any update of the borrowing programme.

29.1.4 Provincial government business enterprises listed in Schedule 3D and authorised to borrow by the Minister of Finance must -

- (a) submit to the relevant treasury, with their corporate plans, a three-year borrowing programme beginning with the first financial year of the corporate plan. The programme must be in terms of approvals and limits determined by the Minister, and in terms of the Borrowing Powers of Provincial Governments Act; and
- (b) submit to the relevant treasury, quarterly reports on the approved borrowing programme, reflecting actual borrowing for that quarter and any update of the borrowing programme.

29.1.5 The relevant treasury must forward to the National Treasury –

- (a) a copy of the corporate plan and approved borrowing plan;
- (b) quarterly updates reflecting actual borrowing for that quarter; and
- (c) any update in the borrowing programme of Schedule 3D provincial government business enterprises that are authorised to borrow.

29.1.6 The borrowing programme referred to in paragraphs 29.1.3 and 29.1.4 must include -

- (a) the terms and conditions on which the money is borrowed;
- (b) information on proposed domestic borrowing;
- (c) for national public entities, information on proposed foreign borrowing within the prescribed limit, where applicable;
- (d) short and long-term borrowing;
- (e) borrowing in relation to a pre-approved corporate plan;
- (f) the maturity profile of the debt;
- (g) the confirmation of compliance with existing and proposed loan covenants;
- (h) debts guaranteed by the government;
- (i) motivations for government guarantees, if required; and
- (j) the executive authority's approval of the borrowing programme, if required by the legislation in terms of which the public entity was established.

29.2 Shareholder's compact

- 29.2.1 The accounting authority for a public entity listed in Schedule 2, 3B or 3D must, in consultation with its executive authority, annually conclude a shareholder's compact.
- 29.2.2 The shareholder's compact must document the mandated key performance measures and indicators to be attained by the public entity as agreed between the accounting authority and the executive authority.

29.3 Evaluation of performance

- 29.3.1 The accounting authority of a public entity must establish procedures for quarterly reporting to the executive authority in order to facilitate effective performance monitoring, evaluation and corrective action.

29.4 Annual budgets [Section 52(a) of the PFMA]

- 29.4.1 For purposes of section 52(a) of the Act, the projection of revenue, expenditure and borrowings must be in the same format as submitted for the accounting authority's approval.

STRATEGIC PLANNING

30.1 Strategic plan

- 30.1.1 The accounting authority for a public entity listed in Schedule 3A or 3C must annually submit a proposed strategic plan for approval by the relevant executive authority. Such a plan must be submitted at least six months before the start of the financial year of the designated department or another time

period as agreed to between the executive authority and the public entity

30.1.2 The strategic plan must be finalised and submitted to the relevant executive authority no later than 1 April of each year.

30.1.3 The strategic plan must –

- (a) cover a period of three years;
- (b) include objectives and outcomes as identified by the executive authority;
- (c) include multi-year projections of revenue and expenditure;
- (d) include key performance measures and indicators for assessing the public entity's performance in delivering the desired outcomes and objectives;
- (e) include the materiality/significant framework, referred to in Treasury Regulation