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LEADERSHIP IS RESPONSIBLE FOR ACHIEVING GOOD CORPORATE GOVERNANCE OUTCOMES

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With the media spotlight on the dismal state of governance in some of South Africa's public and private organisations, as well as many of its state-owned enterprises, there cannot be enough said about the enormous role and duties expected of the directors of an organisation. These select few people hold ultimate responsibility for the organisation which they serve, and they are accountable for a very broad spectrum of matters. These include the proper functioning of the organisation, the value it creates, its financial and non-financial performance, and its impact on those people and natural resources which are affected by the organisation.

As the well-known saying goes, *"With great power comes great responsibility"*, and as such directors should be constantly reminded of the liabilities which they face if they do not exercise their fiduciary and other duties in the best interests of the organisation on behalf of its key stakeholders.

These duties of directors are not imposed with the objective of complicating the management and operation of companies, nor are they intended to frustrate the pursuit by companies of their business objectives. They arise from the common law which is developed over centuries with the objective of protecting shareholders and other stakeholders from delinquent and non-performing directors and managers in the context of the separation between ownership and control. The duties which the law imposes on directors and senior managers is based on the concept of trust which is at the heart of the fiduciary and other duties which the law requires from directors and senior managers.

"[B]y accepting their appointment to the position, directors tacitly indicate that they will perform their duties to a certain standard, and it is a reasonable assumption of the shareholders that every individual director will apply his or her particular skills, experience and intelligence appropriately and to the best advantage of the company."

Duties of Directors, Deloitte

(April 2013)

The South African Companies Act, 2008 (the 'Act') partially codifies the directors fiduciary duties and the duties of care, skill and diligence. This codification is effectively a precis of the common law position which has developed over centuries and has been retained in the Act. The fiduciary duties include the duty to act in good faith and for a proper purpose in the best interests of the company and most importantly to avoid conflicts of interest. There are also a number of procedural provisions which reinforce the substantive obligations to avoid conflicts of interest. It is also essential that directors, particularly nominee directors, retain their independence and exercise an independent judgement in the best interests of the company. The law also requires directors to exercise their powers with proper care, skill, and diligence and for this purpose the minimum standard is an objective one. In addition to the fiduciary duties and the duty of care, skill, and diligence, there are a number of statutory duties.

At common law senior managers and executives have the same fiduciary duties and duties of care, skill, and diligence as those applicable to directors. This has been recognised in the Act by the designation of the term 'prescribed officers' which essentially comprises those executives who on a regular basis participate to a material degree in the exercise of general executive control over, and management of the whole, or a significant portion, of the business and activities of the company. Prescribed officers have the identical fiduciary duties as those of directors.

To this end, the King IV Code on Corporate Governance for South Africa, 2016™ ('King IV™') assists directors in their endeavours, by clearly guiding their behaviour. This latest iteration of the King Codes focuses on the *outcomes* of good governance, rather than stipulating a checklist of behaviours which must be followed. Each of the identified good governance outcomes in King IV™ is driven by various *leadership responsibilities.*

Leadership responsibilities of directors

In distilling the essence of director duties, King IV™ identifies four specific leadership responsibilities which are elevated above the many other duties and responsibilities placed on the directors of an organisation.

The first of these is the responsibility to set and steer the organisation's *strategic direction*. Ultimately, it is the organisation's strategy which will inform the action required to achieve the outcomes of good governance. Directors must share their expertise and knowledge to assist the organisation's management as it continually assesses and responds to any challenges or negative consequences of the organisation's business activities.

The second fundamental responsibility of directors, as identified in King IV™, is approving the *organisational policies*, which give effect to the organisation's strategy.

"Sound governance is not some abstract ideal or utopian pipedream. Nor does it occur as a result of accidents or sudden outbreaks of altruism . . . It happens only when leaders lead with integrity, when directors actually direct and when major organisations are held to the highest standards of accountability by vigilant stakeholders and informed individuals."

J Richard Finlay

As soon as these policies (in the form of frameworks, standards and plans) are in place, the directors will be responsible for ensuring that management has implemented the necessary processes and recruited the requisite skills in order for the policies to be put into practice. Directors will then be able to fulfil the third of their identified responsibilities insofar as they oversee and monitor the *implementation of policies* on a regular basis.

Ultimately, the fulfilment of the previous three leadership responsibilities will culminate in the directors ensuring the accountability of the organisation through its *reporting to all of its stakeholders* – both internal and external. The report to stakeholders, in the form of the annual Integrated Report, provides the directors with an opportunity to again review the strategic direction of the organisation and to ensure that the necessary adjustments are made to relevant policies and procedures, amongst other key areas of reporting.

Good governance outcomes

In effectively practicing the key identified leadership responsibilities, directors will be able to benchmark their organisations against four good governance outcomes. The concepts of leadership responsibilities and good governance outcomes are directly proportional and are interrelated.

The four good governance outcomes, as espoused in King IV™, relate to whether or not the organisation: demonstrates effective control; performs well; adopts an ethical culture; and is legitimate. The legitimacy of an organisation is the most critical outcome of good governance and is informed by its reputation, as well as by the trust which its stakeholders place in it.

In order to be trusted, and to maintain a good reputation, the ethical tone of an organisation must be set from the top and must filter throughout all of its structures. Without sound, ethical leaders and practices, an organisation will not be sustainable. As King IV™ observes, effective and ethical leadership should complement and reinforce each other. If an organisation is to achieve its strategic objectives and positive outcomes, its leaders must act with competence, integrity, and transparency. As a natural result, the two remaining identified outcomes – *effective control* and *good performance* (the latter of which is measured from the point of view of the organisation's financial viability, as well as on the basis of its overall sustainability) will follow.

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