THE ROLE OF KING III REPORT ON CORPORATE GOVERNANCE IN IMPROVING POOR SERVICE DELIVERY IN THE SOUTH AFRICAN GOVERNMENT

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ABSTRACT

When the new government came in to power in 1994 it inherited dysfunctional municipalities. In fact it inherited a country with high levels of poverty, growing levels of inequality and also social dysfunctionality. As such in an attempt to redress apartheid legacies, the new government reformed previous legislation and policies to address issues pertaining to segregation, inequity, inequality, discrimination, poverty and to establish new transitional local authorities. Therefore new institutions have been created with new principles, philosophies and support mechanisms to make the transformation of local government a success. This is irrespective of the government coming up with good policies and laws the South African local government sphere is still rocked by poor service delivery in the majority of the municipalities including the big metropolitan municipalities. Since 2008, South Africa has witnessed many service delivery protests by communities demanding better services. This article critically analyses the role of the King III report on corporate governance in improving poor service delivery in South African local government and to assess if indeed these policies and legislations can improve service delivery. The findings in this article indicates that corporate governance principles are an effective instrument in improving municipalities in South Africa and if adhered to by the municipal councils and management of all municipalities then the challenges that are faced at the local government will be minimised. This article further finds that the only way to restore public confidence in South Africa is by first fixing the local government as it is a test of the country as to whether it is able to manage its affairs and providing services to the members of the communities (public).

Keywords: Corporate governance, Dysfunctionality, Local authorities, Support mechanisms.

1. INTRODUCTION

The South African government inherited dysfunctional system of government from the apartheid government and after the official end of apartheid in 1994 the introduction of democracy left many people with lot of expectations for a better well-being. Most people who were in serious poverty, particularly in black homelands, expected the government to deliver them out of poverty aggravated by unequal allocation of resources by the apartheid government. According to Green (1957) Jan van Riebeck landed in South Africa in 1652. Local government began thirty.... years later, and its subsequent history was confined almost wholly to the Cape of Good Hope until the middle of the nineteenth century.

There was little settled population elsewhere before the urban centres of Pietermarizburg, Durban, Winburg, Bloemfontein, Potchefstroom and Pretoria began to grow between 1840 and 1860; and it was not until the passing of the Natal Municipal Ordinance, 1854, that the initiative in the development of local government first tended to pass from the Cape (Green 1957). Since the beginnings of the present system of local government are thus to be found in a colony administered from both the Netherlands and the United Kingdom, local government in South Africa has two historic sources which are; firstly the Dutch and secondly the other British. The Dutch source was pre Napoleonic and exerted its influence through the *landdrost* and *heemraden* system of rural government, and the urban Cape *raad der gemeente*. The British source mainly influenced the development of urban municipal government but it also had the effect of divorcing judicial from civil administration in rural government and led to the introduction of elected representatives there long before the English County councils Act of 1888 (Green 1957).

Van der Walt, Venter, Van der Walt, Phutiagae, Khalo, Van Niekerk, Nealer (2007) posits that the present post-apartheid democratically elected South African government inherited problematic administrative, economic and political structures emanating from the legacy of decades of apartheid rule. The legal and administrative structures it inherited were not developed to serve the broad population of the country, but rather a small section of it, the white people. After the abolishment of apartheid in South Africa the new Constitution of the Republic of South Africa, 1996 was developed which plays a pivotal role in the development and function of the municipality.

Atkinson (2002) attests that since 1994, South Africa has experienced a steep learning curve with regard to institutional design in general, and local government in particular. When the transition to democracy took place, South Africa inherited a dysfunctional local government system, based

on inappropriate jurisdictions, structures and programmes (Sebei 2013). During the past years, great progress has been made in designing municipal systems and governmental principles intended to promote sustainable development. Non-Compliance and lack of proper implementation of government policies and legislation has always contributed to a large-scale of failure of governance. This therefore resulted in poor service delivery from the South African government to its citizens. It was observed that the failures of the majority of municipalities with regard to service delivery are a result of lack of competent and qualified people in the municipality. It further seems that the government failures from the nation, provincial and local government emanates from lack of proper implementations of Cooperate Governance Principles as provided for by the king III Report.

2. METHODOLOGY

This research is library based and reliance is on library materials such as textbooks, reports, legislations, regulations and articles, government manuals, legislative policies as well as internet sources. Consequently, a combination of legal comparative and legal historical methods, based on jurisprudential analysis was employed. A legal comparative method was applied to find solutions, especially to resolve the South African challenges from the local government level

3. THE APPLICATION OF THE CORPORATE GOVERNANCE

The King III Report and the Code apply to all entities incorporated in and resident in South Africa and the national institutions (departments), regardless of the manner and form of incorporation or establishment and whether that establishment is in the public, private or non-profit sectors. In contrast, the King II Report only applied to certain categories of business enterprises, namely listed companies, financial institutions and sector enterprises, while companies falling out of these categories were merely required to consider the application of the King II Report insofar as it was applicable.

The USA codified its corporate governance provisions in the Sarbanes-Oxley Act of 2002 and legal sanctions are applied for non-compliance with this Act (Cassim, Jooste, Shev & Yeast 2012). In South Africa, compliance with the King III Report and the code is mandatory for the companies listed on the JSE, financial institutions and sector enterprises, but for all other entities there is no statutory obligation to comply with the King III Report and the Code. While corporate governance practices in South Africa may be voluntary, note that they are highly recommended and have considerable persuasive force. Commonwealth countries and the European Union states have also not legislated their corporate governance practices and have adopted a similar approach to that adopted in

South Africa.

4. THE PRINCIPLES OF CORPORATE GOVERNANCE

The King III Report is divided into nine chapters of which each one of the principles contained in this Report is set out in the Code together with the recommended practices relating to each principle. Therefore some of the main principles and practices of the King III Report will be discussed below. The King III Report provides guidance on the following aspects related to corporate governance: Ethical leadership and corporate citizenship, Boards and directors, Audit committees, the governance of risk, the use of information technology, compliance with the laws, codes, rules and standards, Internal audit, Governing stakeholder relationships and Integrated reporting and disclosure

4.1 Ethical leadership and corporate citizenship

The underlying philosophy of the King III Report revolves around leadership, sustainability and corporate citizenship. On the issue of leadership, the King III Report requires the board of directors to provide effective leadership based on an ethical foundation (Cassim et al 2012). Ethics or integrity is the foundation of and very reason for corporate governance. An ethical corporate culture constitutes more than social philanthropy or charitable donations (Nevondwe 2012). The reasoning behind the ethics of corporate governance, which requires the board of directors to ensure that the government institutions and department is run ethically, is that, as this is achieved, the national government earns the respect and approval of those affected by and affecting its operations.

The South African government i.e. the national, provincial and local government should conduct its business in an ethical manner. The board should set the values on the departments and ensure the formulation thereof in a code of conduct. Nevondwe points out that the board should ensure that the company's ethics are managed effectively (Nevondwe 2012). This does not apply only to Companies but also to all municipalities in South Africa. According to Nevondwe (2012) the board should ensure that an ethical corporate culture is built and sustained in the company. It determines ethical standards which are clearly understood by the company and that the company ensures adherence in all aspects of it business, adherence to the ethical standards is measured. The risk management process incorporates ethical risks and opportunities; the ethical performance of external business partners is aligned around the ethical standards of the company.

4.2 Boards and Directors

The King III Report differentiates between executive and non-executive directors. An executive director is involved with the day-to-day management of the

company or government departments. He or she is in the full-time salaried employment of the government and is generally under a contract of service with the government whether national, provincial or local. Whereas a non-executive director, on the other hand, is a part-time director. He or she is not involved in the management of government institutions and organisations, but plays an important role in providing objective judgment, independent of management, on issues that are faced facing. Generally, non-executive directors contribute to the development of management strategies and monitor the activities of the executive directors.

In Fisheries Development Corporation of SA Ltd v Jorgenses and Fisheries Development Corporation of SA Ltd v AWJ Investment (2002), the court stated that non-executive directors are not bound to give continuous attention to the affairs of the company. Their duties are of an intermittent nature, to be performed at periodical board meetings and at any other meetings that may require their attention. Non-executive directors are expected to attend board and relevant board committee meetings and to acquire and maintain a broad knowledge of the economic environment, industry and business of the company. The role of non-executive directors and the independence that they are believed to bring to the board of directors has been a consistent theme of corporate governance theories, policies and programmes (Nevondwe 2012).

Nevondwe (2012) also states that an independent non-executive director is a director who is required to be independent in character and judgment. There should be no relationships or circumstances that are likely to affect, or could appear to affect, their independence. In this context, 'independence' means the absence of undue influence and bias that could be affected by the intensity of the relationship between the director and the company, rather than any particular fact such as length of service or age. Not only should the director be independent in fact, but he or she should also appear to be independent in the perception of a reasonably informed outsider. The board of directors is the most important governance structure, as it is ultimately responsible for the performance and affairs of the government in South Africa. Several investigations after recent corporate collapses and municipal failures pointed towards a lack of effective accountability within the South African spheres of government. The board of directors can therefore be seen as the vocal point of any government poor service delivery elimination, and the Code as part of its recommendations lists the duties and responsibilities of the board of directors from a government institutions point of view

4.3 Audit committee

An independent audit committee fulfils a vital role in the South African government. The audit committee is a critical component in ensuring the integrity of integrated reporting and financial controls, the proper identification and management of financial risks and the integrity of the reporting practices (King III Report 2009). The Report points out that at each AGM, the shareholders of a public company, state-owned company or any other company that has an audit committee must elect an audit committee. The nomination committee (where there is one) should present shareholders with suitable candidates for election as audit committee members. The audit committee should meet to perform its functions, but it is usually recommended that the audit committee meets twice a year. The committee should also meet with the internal and external auditors at least once in a year without the management being present. Nevondwe (2012) further provides that the audit committee should comprise at least three members who should be suitably skilled and experienced independent nonexecutive directors. Section 94(4) of the Act prescribes further requirements to qualify as a member of the audit committee. A member of the audit committee must be director of the company who satisfies any minimum qualification requirements set out by the Minister of Trade and Industry as being necessary to ensure that the committee comprises persons with adequate relevant knowledge and experience to equip the committee to perform its functions. From the above it can be noted that the audit committee is currently viewed as one of the most important governance structure within the modern South Africa. Nevondwe (2012) attests that the Companies Act also regulates the appointment, role and composition for all public companies and state-owned entities while on the other hand the King Code furthermore stipulates that the board should ensure that the company has an effective and independent audit committee

The Report furthermore states that the audit committee should review arrangements made by the company/government to enable employees and outside whistle-blowers (including customers and suppliers) to report in confidence concerns about possible improprieties in matters of financial reporting, or compliance with laws and regulations, that may have a direct or indirect effect on financial reporting.

4.4. The governance of risk

The King III Report requires that the board of directors be responsible for the governance of risk and determine the levels of risk tolerance that the company is able to bear in the pursuit of its objectives. Risk is defined as the taking of risk for reward. The board of directors should determine the levels of risk tolerance at least once a year. It

should review these limits during periods of increased uncertainty or any adverse changes in the business environment (Cassim et al. 2013). It is recommended that the board's responsibility for risk governance be expressed in the board charter. In addition, the board's responsibility for risk governance should manifest in a documented risk management policy and plan, which should be widely distributed throughout the company and reviewed by the board at least once a year. The board should also comment in its integrated report on the effectiveness of the system and process of risk management (Nevondwe 2012).

4.5 The governance of information technology (IT)

The governance of IT is dealt with for the first time in the King III Report. As acknowledged by the King III Report, IT has become an integral part of doing business and is fundamental to support, sustain and grow the business. The King III Report states that IT governance is not an isolated discipline, but an integral part of overall corporate governance (Nevondwe 2012). Information technology governance can be considered as a framework that supports the effective and efficient management of IT resources to facilitate the achievement of a company's strategic objectives. The IT governance framework should include the relevant structures, processes and mechanisms to enable IT to deliver value to the business and to mitigate IT risks. It should focus on the governance of the information as well as the governance of technology (Nevondwe 2012).

Nevondwe (2012) states that the King III Report requires the board of directors to be responsible for IT governance. The board may appoint an IT steering committee or similar forum to assist with its governance of IT. It is recommended that the Chief Executive Officer (CEO) appoints a Chief Information Officer (CIO) to be responsible for the management of IT. There is an increased risk to organisations that embrace IT and its directors should ensure that the reasonable steps have been taken to govern IT.

The board should monitor and evaluate significant IT investment and expenditure. The board should specifically focus on value for money, return on investment and the protection of intellectual property and also the assurance on IT internal controls should also include outsourced services (Nevondwe 2012).

IT should form an integral part of the company's risk management: Management should regularly demonstrate to the board that sufficient disaster recovery procedures are in place and that the board should also ensure that the company complies with all IT-related laws and regulations (Nevondwe 2012). Nevondwe (2012) further provides that it is therefore held that a risk committee and audit committee should assist the board in carrying out its IT respon-

sibilities. The risk committee should ensure that IT risks are adequately addressed and assurance should be obtained regarding controls in place. It is further recommended that IT should be considered by the audit committee in relation to financial reporting and going concern, it should also be considered how the use of IT could improve audit coverage and efficiency.

4.6 Compliance with Laws,Rules,Codes and Standards

The King III Report requires the board of directors to ensure that the company complies with all applicable and relevant laws and that it considers adherence to non-binding rules, codes and standards. A compliance culture should be encouraged through leadership, establishing the appropriate structures, education and training, communication and the measurement of key performance indicators relevant to compliance. The board has a duty to take necessary steps to ensure the identification of laws, rules, codes and standards that apply to the company. Details must be disclosed by the board in its integral report on how it has discharged its responsibility to establish an effective compliance framework and process.

The King III Report goes as far as to require the board and each individual director to have a working understanding of the effect of the applicable laws, rules, codes and standards on the company and its business. Directors should sufficiently familiarise themselves with the general content of applicable laws, rules, codes and standards to be able to adequately discharge their fiduciary duties and their duty of care, skill and diligence in the best interest of the company.

4.7 Internal Audit

The Institute of Internal Auditors defines internal auditing as "an independent, objective assurance and consulting activity designed to add value and improve an organistaion's operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes." From this definition we can conclude that the internal audit department of a company can play an integral role as part of an effective corporate governance system (Thornhill & Cloete 2013).

The King III Report requires the board of directors to ensure that there is an effective risk-based internal audit. An internal audit should evaluate business processes, perform an objective assessment of the effectiveness of risk management and the internal control framework, systematically analyse and evaluate business processes and associated controls, and provide a source of information, as appropriate, regarding instances of fraud, corruption, unethical behaviour and irregularities. An internal audit plays an important role in providing assur-

ance to the board regarding the effectiveness of the system of internal controls and risk management of the company (Cassim et al. 2013). Internal audit should provide a written assessment of the effectiveness of the company's system of internal controls and risk management: the internal audit should form and integrated part of the combined assurance model as the internal provider of assurance. The internal audit should also focus on operational, compliance and sustainability issues, and not only on financial matters. It is also provide that the internal audit should provide a written assessment of the system on internal control and risk management to the board. Furthermore the internal audit should provide a written assessment of internal financial controls to the audit committee (Thornhill & Cloete 2013).

4.8 Government Stakeholder Relationships

Nevondwe (2012) posits that the King III Report adheres to the 'triple context' or integrated approach, which acknowledges that companies should act with economic, social, and environmental responsibility. Directors should consider economic, social and environmental factors when they manage the company.

Thus the Report advocates the notion that the board of directors is responsible not merely for the company's financial bottom-line, but rather for the company's performance within the triple context in which it operates ('triple bottom-line') (Nevondwe 2012). Nevondwe (2012) is of the view that Companies in South Africa are encouraged to adopt the inclusive approach to governance based on which companies are required to act in the best interest of all stakeholders. This section of the code provides guidance regarding the governance of stakeholder relationships.

One implication of the right to vote being a right of property is that shareholders may choose not to exercise their right to vote at all. But if shareholders are passive, it undermines good levels of compliance by management (Nevondwe 2012).

Nevondwe (2012) further state that to encourage shareholders activism, an environment should be created where shareholders are not mere speculators, but owners concerned with the well-being of the company in which they hold shares, constantly checking whether the directors are practicing good corporate governance.

4.9 Integrated Reporting and Disclosure

Sustainability reporting has been the subject of the king II report. Sustainability reporting can be defined as reporting on those financial and non-financial matters that influence the company's ability to survive and prosper and sustain its business future. Where financial reporting tends to provide an historic account, sustainability

reporting and disclosures provide a balanced and integrated record of the economic, social and environmental performance of the company. This now generally referred to as "triple bottom line" reporting. The economic aspect of "triple bottom line" involves the financial aspects relevant to the business of the company, whilst the social aspect focuses on the values of the company, ethics, and reporting on the company's engagement with stakeholders. The environmental aspects include reporting on the effect of the company's products or services on the environment (Marx et al 2011).

The king III Report on Corporate Governance advocates the publication of an integrated report dealing with both financial and non-financial matters in integrated manner (Nevondwe 2012).

The board of directors should ensure the integrity of the company's integrated report. An integrated report means a holistic and integrated representation of the company's performance in terms of both its finances and its sustainability. The integrated report should be prepared every year (Marx et al 2011). Sustainability reporting and disclosure should be integrated with the company's financial reporting. The annual financial statements should be included in the integrated report, and the board should include a commentary on the company's financial results. This commentary should include information to enable a stakeholder to make an informed assessment of the company's economic value (Marx et al 2011). The board should ensure that positive and negative impacts of the company's operations, together with plans to improve the positives and eradicate or ameliorate the negatives in the financial year ahead are conveyed in the integrated report (Nevondwe 2012).

5. CONCLUSION AND RECOMMENDATIONS

In conclusion, it is evident that the Principles of Corporate Governance is the best way of building an effective and accountable nation away from corruption activities and maladministration's in government institutions, provincial departments and municipalities. The purpose of the King Report 1994 was, and remains, to promote the highest standards of corporate governance in South Africa. This means that even the municipalities cannot be exempted from corporate governance as mentioned. The integrated report should be prepared every year. Sustainability reporting and disclosure should be integrated with all the provincial departments and municipality's financial reporting. The annual financial statements should be included in the integrated report, and the board should include a commentary on the national, provincial and municipal financial results to be commented by the members of the public. It is therefore provided that this commentary should include informa-

tion to enable a stakeholder to make an informed assessment of the economic value in the country. The board should ensure that positive and negative impacts of the South African government operations, together with plans to improve the positives and eradicate or ameliorate the negatives in the financial year ahead are conveyed in the integrated report.

This means that for the provincial governments and municipalities to perform their duties effectively, government must do away with hiring the politicians who do not have skills or excellent educational background in order to promote and enforce all the principles of corporate governance. For it is through all this politicians that are being employed in the municipalities that we see municipalities being hid with irregularities and protests due to poor service deliveries. Politicians are not performing their functions in so far as the municipality is concerned but they are there to promote and safe guard the interest of their political parties.

Looking at the definition of corporate governance we could conclude that local government is also covered in the definition, it is not only about the companies. Corporate governance is generally understood to mean the way in which companies are directed and controlled. Thus, the emphasis is on those organs which play a vital role in corporative decision-making. It is widely accepted that corporate governance does not affect or apply exclusively to listed companies, as some writers insist. In order to simplify matters, a distinction needs to be drawn between corporate governance applicable to all companies and corporate governance applicable to 'affected companies' as defined by the King Committee on Corporate Governance.

Municipalities and provinces need an effective board of directors as provided for in the King III Report which provides that an executive director is involved with the day-to-day management of the company and he or she is therefore in the full-time salaried employment of the company; and is generally under a contract of service with the company. A non-executive director, on the other hand, is a part-time director, who is not involved in the management of the company, but plays an important role in providing objective judgment, independent of management, on issues facing the company. Generally, non-executive directors contribute to the development of management strategies and monitor the activities of the executive directors.

The Constitution of the Republic of South Africa recognises the importance of good governance. Section 195 deals with basic values and principles governing public administration. Our Constitution compels government in all of its forms, both through government departments and organs of state (including state-owned enterprises) to adhere to principles

of good governance. Therefore there is no doubt that corporate governance is a key element in improving the South African service deliveries to all the members of the society and eradicating corruption from its roots, It will also promoted economic efficiency and growth as well as enhancing investor confidence. This will be achieved only if there is consistency in applying the above mentioned principles. These principles will be the yardstick of pointing to the right direction as to who should be held accountable for all poor service deliveries as it will ensure that functions are assigned to rightful spheres of government and its employees in order to eliminate service delivery protest.

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