DRAFT CODE FOR RESPONSIBLE INVESTING BY INSTITUTIONAL INVESTORS IN SOUTH AFRICA

1 September 2010

This draft Code has been issued by the Committee on Responsible Investing by Institutional Investors in South Africa. The Committee is composed as follows:

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INTRODUCTION

The institutional investor has a critical role to play in making the overall corporate governance system effective. South Africa has a hybrid regime of corporate governance. This means that, where governance is not prescribed by statute, companies voluntarily apply the governance principles and practice recommendations of King III or explain how they have applied them differently or why they have not applied them. The institutional investor has by virtue of its share ownership the responsibility to influence and encourage the companies in which it invests to voluntarily apply sound governance principles and practices.

PURPOSE

The purpose of this Code is, together with the applicable governance standard such as King III, to provide a voluntary framework that can be used to ensure that sound governance is practised. The framework relates to the governance role of boards of companies, institutional shareholders and the ultimate beneficiaries.

APPLICATION

Legally, the institutional investor, who is the asset owner, has fiduciary responsibilities and is accountable to the ultimate beneficiaries of these investments. If institutional investors appoint service providers, as defined below, to execute any aspect of the investment activities dealt with in this Code, this accountability is not diminished and proper oversight should be exercised. However, due to their position in the investment value chain, service providers also have a pivotal role in promoting sound governance. Therefore, this Code applies to both institutional investors and service providers.

Institutional investors and service providers should adopt the principles and practice recommendations in this Code on an “apply or explain” basis.

Where there is conflict between the Code and applicable legislation, the legislation will prevail.

DEFINITIONS

In this Code, unless the context indicates otherwise:-

Book value means the value of a company as expressed in its balance sheet, profit and loss statement and the related notes, as most recently audited.

Code of conduct means the code developed by a company by which it expects all its stakeholders to behave, particularly its directors, managers, employees and suppliers.

Company means a company in which an institutional investor invests or considers investing as a shareholder.

Corporate citizenship means responsible corporate citizenship. This implies an ethical relationship of responsibility between the company and society. Therefore, in addition to rights, companies have legal and moral obligations in respect of the economy, society and the natural environment. As a responsible corporate citizen, the company should protect, enhance and invest in the well-being of the economy, society and the natural environment.

Duties means the directors' common law fiduciary duties of acting in good faith and in the best interest of the company and acting with care, skill and diligence, and includes statutory duties relevant to directors' standards of conduct.

ESG means environmental, social and governance.

Institutional investor means any person or institution referred to in the definition of financial institutions (Section 1, Financial Services Board Act 97, 1990) or any medical aid scheme (Section 1, Medical Schemes Act 131, 1998) to the extent that these persons or institutions own or invest in the equity of a company.

Integrated reporting means a holistic and integrated representation of the company's performance in terms of both its finance and sustainability.

King III means The Report and Code of Corporate Governance for South Africa, 2009.

Service providers means those who act as agents of the institutional investor for any of the investment activities dealt with in this Code, including asset and fund managers and consultants.

Supply chain code of conduct means the code of conduct by which a company expects its suppliers to behave and by which the company undertakes to conduct itself in its relationship with the supplier. The code includes conduct in terms of ethics and sustainability.

Sustainability means the sustainability of a company in conducting operations in a manner that meets existing needs without compromising the ability of future generations to meet their needs. Sustainability includes the impact that the business operations have on the life of the community in which it operates. Sustainability includes environmental, social and governance issues.

Total economic value means the value of a company incorporating its book value but in addition thereto future earnings potential, its debt/equity ratio and its intangible assets including, but not exhaustively, its reputation, the sustainability issues pertinent to its business and the quality of its board of directors and management, having due regard to the provisions of King III.

Transparent means easy to understand or recognise; obvious; candid; open; frank, relevant and accessible to stakeholders.

Ultimate beneficiaries means those end-beneficiaries or underlying investors to whom institutional investors owe their duties, including the individual retirement fund beneficiaries and the individuals in whose names on whose behalf unit trusts and policies are held.

THE CODE

Principle 1: An institutional investor should incorporate ESG considerations into its investment analysis and activities as part of the delivery of superior risk-adjusted returns to the ultimate beneficiaries.

1. An institutional investor should develop a policy on how it approaches incorporating ESG considerations into its investment analysis and activities. The matters to be dealt with in the policy should include, but not necessarily be limited to, assessment of:

    a. the total economic value of a company;

b. the quality of the company's integrated report on the social and environmental impact of the company's operations and how it plans to mitigate negative impact in future. If an integrated report has not been issued, due enquiry should be made on the reasons for this;

c. the manner in which the business of the company is being conducted based on the company's internal code of conduct and its supply chain code of conduct.

2. An institutional investor should ensure implementation of the policy on ESG considerations and the establishment of processes to monitor that it is complied with.

Principle 2: An institutional investor should demonstrate its ownership approach in its investment arrangements and activities.

3. An institutional investor should develop a policy for share ownership regardless of whether active or passive investment policies are followed. The policy should include, but not necessarily be limited to, dealing with the following:

   a. Standards to be applied (e.g. King III) for the identification of ESG concerns at a company.

   b. Mechanisms of intervention and engagement with the company when concerns have been identified and the means of escalation of activities as a shareholder if these concerns cannot be resolved.

   c. Voting at shareholder meetings, including the criteria that are used to reach voting decisions, processes for management of conflicts and publication of full voting records.

4. Where the institutional investor outsources to a third party service provider, there should be processes to ensure that the service provider applies the provisions of this Code and the relevant policies of the institutional investor.

5. The institutional investor should introduce controls that prevent it from receiving information or acting on information in a manner that makes it an 'insider' in terms of the Security Services Act. These controls should be applied when engaging with the company, and when seeking any information it requires, whether this is to fulfil its duties or to act within the guidelines of this Code.

Principle 3: Where appropriate, institutional investors should consider a collaborative approach to promote acceptance and implementation of the principles of this Code and other codes and standards applicable to institutional shareholders.

6. An institutional investor should consider a collaborative approach to, where appropriate, promote acceptance and implementation of this Code and other applicable governance codes and standards. This should not be done in a manner which could result in any institution being a 'concert party' in terms of the regulations of the Takeover Regulations Panel, established in terms of the Companies Act 71 of 2008.[1]

Principle 4: Institutional investors should be transparent about their policies how the policies are implemented, and how the Code is applied to enable stakeholders to make informed assessments.

7. An institutional investor should, at least quarterly, fully and publicly disclose to its stakeholders, including the ultimate beneficiaries, to what extent it applies this Code. If an institutional investor does not apply some or any of its principles or recommendations or applies them differently from how they are set out in the Code, it should transparently explain the reasons for this.
8. The disclosure by institutional investors should not be limited to the integrated report but also be made accessible through publication on its website, quarterly client reporting and through other appropriate means of communication to stakeholders.
9. The following policies should be disclosed publicly on a quarterly basis:
   a. Policy on incorporation of ESG considerations into investment analysis and decision-making processes with reference to the matters as set out under Principle 1.
   b. Policy in regard to share ownership, including the following matters as set out under Principle 2:
      i. Standards to be applied (eg. King III) for the identification of ESG concerns at a company;
      ii. Mechanisms of intervention and engagement with the company when concerns have been identified and the means of escalation of activities as a shareholder if these concerns cannot be resolved; and

[1] Refer to Securities Regulations Panel website http://www.srpanel.co.za for examples of acting in concert.

iii. Voting at shareholder meetings, including the criteria that are used to reach voting decisions, processes for management of conflicts and publication of full voting records.

10. Disclosure of policies should be reinforced by clear explanation of how the commitments made in the policies were practically implemented during the reporting period.

11. There should be disclosure by institutional investors of processes to ensure that service providers apply this Code and the requirements of the institutional shareholder's policies.

RESEARCH REFERENCES

United Nations Principles for Responsible Investment
ICGN Statement of Principles on Institutional Shareholder Responsibilities, 2007
UK Stewardship Code
Fiduciary Responsibility by UNEP FI Asset Management Working Group (AMWG), July 2009