A guide to the application of King III for non-profit organisations (“the non-profit organisation” or “the organisation”)
**Glossary of terms**

In this Practice Note:

‘**Assets**’ shall mean an item of property owned by a person or company, regarded as having value and available to meet debts, commitments or legacies.

‘**Board Charter**’ means a document approved by the governing body and adopted by the governing body for the purpose of setting out the governing body’s role and responsibilities as well as the requirements for its composition and meeting procedures.

‘**Terms of Reference**’ means a document approved by the governing body that sets out the role and responsibilities of governing body committees to whom the governing body has delegated certain functions, as well as the requirements for its composition and meeting procedures.

‘**DSD’s Code**’ means the Department of Social Development’s Code of Good Practice for South African Non-profit Organisations (2001)

‘**Fiduciary duties**’ means the duties that members of the governing body of a non-profit organisation have as a result of their having the assets belonging to another under their control. The fiduciary duties of members of the governing body of an organisation require them to act in good faith, for a proper purpose and the best interest of the organisation.

‘**Governing body**’ means those charged with governance in a non-profit organisation and includes councils, boards of directors and trustees.

‘**Non-Profit Organisation (NPO)**’ means organisations established not for profit, whether they are incorporated as companies under the Companies Act No.71 of 2008 (NCPs), statutory bodies, trusts or voluntary associations; and irrespective of whether they are registered as Non-Profit Organisations under the Non-profit Organisations Act No. 71 of 1997 or Public Benefit Organisations under the Income Tax Act No.58 of 1962.


‘**Sustainability**’ means conducting operations in a manner that meets existing needs without compromising the ability of future generations to meet their needs. Sustainability also refers to the ability of an organisation to consistently, continually and efficiently raise, manage and deploy funds with which to implement programmes and to achieve set goals that ultimately benefit the communities in which they operate.

1. Introduction

Voluntary governance codes applicable to the non-profit sector have been established in South Africa and internationally. In South Africa the King Report on Governance for South Africa, 2009 and the King Code of Governance for South Africa (King III, King III Report or King III Code as applicable) are generally accepted as the source documents for what constitutes sound governance. However, there is also other guidance on and requirements for good governance applicable to non-profit organisations. These include: SANGOCO’s Code of Ethics for Non-profit Organisations (1997), Department of Social Development’s Code of Good Practice for South African Non-profit Organisations (2001) and The Independent Code of Governance and Values for Non-profit Organisations in South Africa (2012). This Practice Note is primarily based on King III but references to the abovementioned guidelines and requirements are included. Please note that referencing of these does not denote an endorsement by either The Institute of Directors in Southern Africa (IoDSA) or the King Committee.

The King III Report and Code can be publically accessed, free of charge on the IoDSA website at www.iodsa.co.za. The King III Code and Practice Notes can be printed and the full King III Report viewed in i-paper format.

This Practice Note is a living document and its aim is to continually accommodate developments in the non-profit sector.

1.1 What is ‘King III’?

- An internationally recognised code;
- Which details best practice standards for good governance;
- Which may be used by all entities; and
- Which is voluntary.

1.2 How is King III relevant to my NPO?

Although the King III Code is wide enough to deal with the most complex of corporates, it may also be used as a tool by NPOs to:

- Assess their governance processes against best practice standards;
- Assess potential risk;
- Develop strategies to build organisational resilience; and
- Provide assurance to funders that governance principles have been considered and implemented, where appropriate.

1.3. Purpose and target audience

The purpose of this Practice Note is to provide guidance to Non-Profit Organisations on how to apply and interpret King III. For the purposes of the practice note we attach the meaning as set out in the glossary to the term, ‘Non-Profit Organisation’.

This Practice Note provides guidance to governing body members and decision-makers of Non-Profit Organisations, e.g. directors, trustees, secretaries, chief executive officers (CEOs), financial officers and operations officers on how King III’s principles should be interpreted and applied at Non-Profit Organisations.

1.4. Implementation of King III in Non-Profit Organisations

**Key points to consider:**

- King III allows for flexibility in application according to the nature, size and complexity of the organisation.
- King III is aspirational and therefore perfect implementation is expected to be a continual journey.
- Not applying a King III recommendation because it is not in the best interest of the organisation achieves

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1 An example of an international code is ‘The World Bank Handbook on Good Practice for Laws Relating to “THE ORGANISATION”’s’ (Discussion draft), May 1997.
2 The King III Report contains the principles and complete practice recommendations that are necessary to establish good governance. The King III Code constitutes an executive summary of the King III Report.
The King III principles have largely been drafted in general terms so that all entities, including non-profit organisations could apply these in order to measure and achieve good governance. There are certain considerations to keep in mind when implementing King III in non-profit organisations.

King III allows for flexibility when it is implemented due to its ‘apply or explain’ regime. This is different to ‘comply or explain’, which was the approach followed in King I and King II. Although there is a subtle difference, this change represents a fundamental shift in understanding the nature of corporate governance. ‘Comply or explain’ potentially denotes a rules-based compliance where an organisation either complies or does not. In contrast to this the ‘apply or explain’ approach is a much more nuanced approach. ‘Applying’ (as opposed to complying) allows for the non-profit organisation to consider different approaches to achieving the objective of the principle in question. The King III Report was drafted by stating the governance principle as a heading, followed with recommendations on how the objective of the principle may be achieved.

Furthermore, application always takes place within a context, namely what is in the best interest of the particular organisation. The ‘apply or explain’ regime provides the opportunity for each organisation to apply King III as is appropriate to the size, nature and complexity of its operations. The size, nature and complexity of an entity can be categorised with reference to a variety of measures, e.g. the number of employees, total income, number of members, geographical reach, etc. King III’s practice recommendations are applicable to these different entities in varying degrees depending on the variables in terms of the size, nature and complexity as set out above. If, therefore, a non-profit organisation has considered all of the information and alternative measures to achieve the objective of the principle and decided not to apply practice recommendation as it is not in the best interest of the organisation, compliance is achieved. Ideally, the rationale for the decision needs to be explained in sufficient detail to donors, members and other stakeholders.

In order to implement King III judiciously in the interest of the organisation, the governing body – including senior management – needs to have a sound understanding of governance in general and King III specifically. As such, the governing body needs to understand what purpose each principle sets out to achieve. It is only when there is a sound understanding as a basis that it is possible to interpret the principles and best practice recommendations for how they may be applied in the best interest of the organisation.

The other factor to note when considering implementation is that King III has been drafted to be aspirational. NPO’s should strive for a gradual improvement in the application of the Code. Good governance is not only about structures, processes and policies, but also about fostering the right culture and behaviour along the overarching principles of responsibility, accountability, fairness and transparency. Ultimately a non-profit organisation needs to take into account what structures, processes and policies will serve these principles and as such it will remain a continual journey.

The fact that King III is non-mandatory, that it has been drafted in order to allow for flexibility and that it is aspirational are to be kept in mind as non-profit organisations weigh up the points listed below under the headings ‘Key points to consider in relation to ....’. It should therefore not be seen as a compulsory list (which denotes compliance), but rather as aspirational recommendations for consideration within the context of the specific organisation.

1.5. Benefits of implementing King III in non-profit organisations

**Key point to consider:**
Sound corporate governance builds reputation and trust so that an organisation is able to source funding and obtain suitable persons to serve on its governance body.

We strongly believe that governance should be harnessed to the benefit of the organisation and its stakeholders. Good governance is not an end in itself nor does it take place in a vacuum. Application of good governance as envisaged by King III will benefit non-profit organisations in many ways, including enhancing relationships with donors, and ensuring greater accountability to beneficiaries and other stakeholders. Being able to demonstrate good governance will also strengthen the organisation’s ability to find suitable members to serve on its governing body. Sound governance is a prerequisite for donors when reviewing funding applications. Therefore, ensuring good governance will support an organisation’s fundraising strategy which will in turn allow for the necessary resources, thus creating a virtuous cycle enabling the organisation to grow.
Non-profit organisations source their funds from donations, grants and membership fees, while profit entities obtain their equity from shareholders. However, in both instances there is a need for the entity to account for the use of the funds advanced by the donor/member or shareholder. Governance is one of the key measures of an organisation’s health and accountability in this regard, and is imperative for the achievement of an organisation’s long-term objectives.

Below, we provide guidance to non-profit organisations on how to apply the specific principles in King III.

2. The governing body’s role

2.1. The governing body as ethical leader

King III, Principle 1.1 and 2.3: The board should provide effective leadership based on an ethical foundation

King III, Principle 1.3 and 2.5: The board should ensure that the company’s ethics are managed effectively

‘Ethical leadership’ involves both ethical governance and the governance of ethics. It means that the governing body is required to govern the organisation in an ethical manner by displaying the ethical values of responsibility, accountability, fairness and transparency. It should also oversee that management actively cultivates a culture of ethical conduct and sets the values to which the organisation will adhere.

Reference to other industry codes:

The Independent Code highlights the following areas in relation to exercising effective leadership:
- Vision, purpose and value
- Accountability and transparency
- Fundraising, sustainability and risk
- Collaboration and synergy
- The board and other governance structures
- Procedural governance.

Key points to consider in relation to ethical leadership:
- Does the governing body set the values that the organisation adheres to; and are these values documented in a code of conduct?
- Are the deliberations, decisions and actions of the governing body based on the governance principles of fairness, accountability, responsibility, and transparency?
- Do the members of the governing body, in performing their fiduciary role, live the five moral duties, namely conscience, care, competence, commitment and courage?
- Does the organisation understand where it is at risk of ethical failures such as fraud?

2.2. The governing body as focal point of governance

King III, Principle 2.1: The board should act as the focal point for and custodian of corporate governance.

King III, Principle 2.14: The board and its directors should act in the best interests of the company.

This principle means that the governing body carries ultimate responsibility for the organisation and its operations. The governing body is the structure that is held accountable for the prosperity of the organisation.

Reference to other industry codes:

SANGOCO’s Code requires organisations to ‘specify the frequency of governance structures’ meetings, quorums and the role and powers of the governance structures’ and to ‘ensure the governance structure understands and is responsible for overall policy-making and accepts ultimate responsibility for governance of all aspects of the organisation.’
The DSD’s Code states that:
‘For an NPO to perform well, its governing body and staff leaders need commitment, enthusiasm and initiative. The governing body and staff leaders have both distinctive and overlapping roles and responsibilities to achieve this.

The governing body of an NPO tends to emerge from the circumstances that gave birth to the organisation they serve. As the nature and structure of the organisation changes and grows, so the governing body finds itself faced with changing roles. At any stage of its life it is important for a governing body to clarify its responsibilities. A governing body that meets the legal standards of its constitution and registration, in the performance of its duties, also positions the organisation for success through good management and ethical practices.

Service on a governing body is very important for the organisation, and the performance of duties must be taken seriously. Each individual governing body member, and the body as a whole, is held accountable for actions with respect to the organisation. They may delegate some of the work to outsiders, but they cannot delegate their final responsibility.’

Key points to consider in relation to the governing body being the focal point of governance:

- Does the governing body have a charter/operating rules that clearly sets out its role and duties?
- Does the governing body meet at least four times each year?
- Does the governing body have reasonable access to the organisation’s management, information, records, documents and property?

3. Legal duties of governing body members

3.1. Overview of duties of members of the governing body

The governing body is entrusted with the governance of the organisation, which entails managing the funds and other assets belonging to the organisation. As the governing body is controlling assets belonging to another, it and each member of the governing body individually is in a relationship of trust (fiduciary relationship) towards the organisation. In accordance with its fiduciary duties, the governing body is expected to act in the best interest of the organisation.

Further to their fiduciary duties, members of the governing body also have the duty to exercise due care, skill and diligence. In addition, members of the governing body have statutory duties imposed by various laws (e.g. the Companies Act, the Trust Property Control Act or the common law), the incorporation documentation of the organisation (e.g. the Memorandum of Incorporation of a Non-profit Company, trust deed of a trust or founding document/constitution of a voluntary association) and any agreements entered into by the organisation (e.g. the appointment letter of employment contract of a member of the governing body).

Members of the governing body should understand their duties in order to avoid personal liability that may follow from breach thereof.

Many members of governing bodies of non-profit organisations receive no or minimal remuneration in return for serving as such. Regardless of no or limited remuneration, breach of these duties could still result in accountability and personal liability.

Reference to other industry codes:

DSD’s Code defines the governing body’s duty of care as ‘to act as an ordinary, wise person would – in the same circumstances: applying careful, attentive and informed participation. There is no measure of just how much time, skill and attentiveness an individual must bring to her or his actions as a governing body member. This standard requires that governing body members base their decisions on adequate information.

Governing body members don’t have to be experts at everything that comes before them. However, any member with special expertise is expected to contribute that specialised knowledge in his or her activities as a governing body member. Each member need not be fully involved in every action and decision of the governing body. The duty of care

3 A King III Practice Note providing an example of a board charter can be found on IoDSA’s website: www.idsa.co.za. Governing bodies can utilize the example to customize a governing body charter for their own environment.
permits delegation to other members, committees, staff or even outsiders, within reason.’

The DSD Code also refers to the governing body’s **duty of loyalty**, defined as ‘to act in good faith, in the best interests of the organisation’.

**Key points to consider in relation to legal duties:**

- Are all members of the governing body familiar with their duties in terms of their appointment letters/contracts, the organisation’s constitution/memorandum of incorporation/trust deed, all legislation and regulations applicable to the organisation?
- Do all members of the governing body ensure that they dedicate sufficient attention and time to the execution of their duties so that informed decisions are reached?
- Are members of the governing body permitted to take independent advice related to their duties; and will the organisation pay for such advice?

3.2. **Conflict of interest**

Conflicts are defined in many ways; however the basic tenet of any of these definitions is the tension between multiple competing interests, whether personal or financial. This usually manifests in the entanglement of the private and professional interests of an individual. An example of such a conflict is a member of the governing body participating in a vote in favour of purchasing products and services from a company that the member owns.

Not only actual conflicts but also perceptions of conflicts should be managed. The perception of a conflict is influenced by whether and independent observer might question whether the governing body members’ professional actions were motivated or influenced by a potential personal financial gain.

The Companies Act requires directors of non-profit companies to declare all personal financial interests and to follow the procedures as set out in the Act. King III determines that certain conflicts of interest are fundamental and should be avoided and that other conflicts (whether real or perceived) should be disclosed in good time and in full detail to the governing body and then appropriately managed.

**Reference to other industry codes:**

DSD’s Code states that the ‘**duty of loyalty imposes safeguards and standards of fairness in situations where there are conflicts of interest**’. The legal standards address this concern by requiring activity such as: full disclosure, approval by the majority of governing body members, and getting good deals for the organisation.

SANGOCO’s Code requires organisations to:

- develop a policy that prohibits direct and indirect conflict of interest by members of governance structures, members, employees and volunteers
- ensure that members of governance structure and staff excuse themselves from decisions where they have or are perceived to have, a vested interest
- in the case of an independent Board or Trust, adopt a policy that discourages members from submitting tenders to organisations or applying for staff positions within the organisations; this policy must stipulate that if they desire to do either, they must resign from the governance structure, and
- ensure the governance structure approves the annual budget, appoints independent auditors and receives audited statements.

The Independent Code refers to a number of areas where conflict may arise, such as in the case of community members where the community members are not only the beneficiaries but also serve on the Non-profit organisation’s executive committee. It also mentions the appointment of relatives and friends as employees or appointing them as paid consultants or service providers as examples of conflict. It proceeds to recommend that the Companies Act should be followed as best practice for dealing with conflict even where the organisation is not a company. The process prescribed by the Companies Act involves the following:

- disclosure of interest and its general nature
- disclosure of any known material information relating to the matter
- disclosure of any observations or pertinent insights relating to the matter
recusal from decision-making in the matter by the conflicted party.

Key point to consider in relation to conflict of interests:
Do members of the governing body disclose real and perceived conflicts of interest to the governing body; as well as manage conflicts appropriately?

4. Governing body – composition and appointment

4.1. Balance of power

King III, Principle 2.18: The board should comprise a balance of power, with a majority of non-executive directors. The majority of non-executive directors should be independent.

Balance of power is important in the interest of objectivity and having a balance of views at governing body level. Good corporate governance practice requires that the governing body act in the interest of the organisation and not only in the interest of some of its stakeholders. Independent and diverse views are imperative for the effective functioning of the governing body.

Reference to other industry codes:

SANGOCO’s Code requires organisations to, ‘within financial constraints ensure the governance structures reflect the race and gender composition of South African society and various target constituencies that the organisation works with, with regard to both their composition and their geographic spread.’

DSD’s Code states that ‘the mark of an effective and maturing non-profit organisation is one whose governing body members do not get involved in the day-to-day running of the operation, and do not become involved in the interpersonal relationships of staff, or the controls of the CEO.’

Key points to consider in relation to balance of power:

- Is there a balance of power and authority within the governing body, such that no one individual or grouping has unfettered powers of decision-making?
- Does the governing body comprise a majority of non-executive members?
- Are the majority of the non-executive members on the governing body independent?

4.2. Appointment of directors

King III, Principle 2.19: Directors should be appointed through a formal process.

It is important to have a formal process in place for appointments to the governing body, as this will ensure that the persons that are appointed will contribute relevant skills, experience and knowledge to the governing body’s decision-making. Absence of a formal appointment process may lead to appointments being ill-considered and not being suitable to the needs of the organisation.

Key points to consider in relation to the appointment of directors:

- Does the governing body make recommendations for election of governing body members based on the knowledge, skills and experience gap on the governing body; the integrity of the candidate; and the knowledge, skills and experience of the candidate?
- Do at least one third of non-executive governing body members rotate every year?
- Does the governing body recommend whether retiring non-executive governing body members should be eligible for re-election based on past performance, contribution and the objectivity of business decisions?

4.3. Induction and ongoing training
**King III, Principle 2.20: The induction of and ongoing training and development of directors should be conducted through formal processes.**

Formal induction programmes should familiarise new governing body members with the organisation’s operations, environment and relevant sustainability issues. New governing body members that lack sufficient governing body experience should be trained and/or mentored regarding their duties, responsibilities and potential liabilities.

**Key point to consider in relation to induction and ongoing training:**
Does the content of the induction programme for new governing body members aim to familiarise them with the organisation’s operations, business environment, and relevant sustainability issues; as well as introduce them to members of senior management and their individual duties and responsibilities?

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**4.4. Chairperson**

**King III, Principle 2.16: The board should elect a chairman of the board who is an independent non-executive director.**

**King III, Principle 2.16: The CEO of the company should not also fulfil the role of chairman of the board.**

The chairperson should be an independent non-executive governing body member who can provide the direction necessary for an effective governing body. One of the main responsibilities of the governing body is to oversee management. The CEO as an executive is not sufficiently independent to lead the governing body.

The chairperson provides the direction necessary for an effective governing body. Electing a chairperson with strong leadership skills could be the difference between an effective and dysfunctional governing body. An independent non-executive chairperson is best able to fulfil this role. The chairperson’s key functions are:

- presiding over governing body meetings and ensuring that time in meetings is used productively; the chairperson should encourage collegiality among governing body members without inhibiting candid debate and creative tension among governing body members;
- acting as the link between the governing body and management and particularly between the governing body and the CEO;
- ensuring that governing body members play a full and constructive role in the affairs of the organisation and taking a lead role in the process for removing non-performing or unsuitable governing body members from the governing body;
- ensuring that complete, timely, relevant, accurate, honest and accessible information is placed before the governing body to enable governing body members to reach an informed decision; and
- ensuring that good relations are maintained with the organisation’s major stakeholders, and presiding over member’s meetings (if applicable).

For a detailed list of the chairperson’s duties please consult the King III Report.

**Key points to consider in relation to the chairperson:**
- Is the chairperson independent and non-executive?
- Does the chairperson fulfil the functions as set out above?

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**4.5. Chief Executive Officer**

**King III, Principle 2.17: The board should appoint the Chief Executive Officer (CEO) and establish a framework for the delegation of authority.**

**Reference to other industry codes:**

DSA’s Code encourages the governing body to select and appoint the CEO, support the CEO and review the CEO’s performance.

**Key points to consider in relation the CEO:**
- Does the governing body appoint the CEO and clearly define in writing the duties and performance measures of
4.6. Evaluation

King III, Principle 2.22: The evaluation of the board, its committees and the individual directors should be performed every year.

Reference to other industry codes:

DSD’s Code requires the governing body to measure its own performance and more specifically that ‘every two or three years the governing body should give itself an opportunity to examine its own progress and performance. This is most effective if each governing body member joins the organisation with an agreed standard of performance or job description in place. Progress can be measured at an evaluation workshop, or by interviews with each member conducted by the chairperson and/or the CEO. Minimum criteria against which performance can be measured could include: knowledge of the organisation; commitment to the organisation; influence in the client or donor community; ability to give; willingness to work.’

Key points to consider in relation to the performance evaluation of governing body members:
- Are annual evaluations of the governing body and individual members’ performance conducted?
- Are the results of performance evaluations constructively used to identify training and development needs for members of the governing body?
- Is there an appropriate benchmark; i.e. agreed performance measures, in place to evaluate the performance of the CEO?
- Does the assessment of the performance of the CEO and other executive governing body members as employees take place annually and do the results of this assessment affect remuneration?

5. Board structures

5.1. Board Committees

Principle 2.23: The board should delegate certain functions to well-structured committees but without abdicating its own responsibilities.

The purpose of establishing committees of the governing body is to alleviate its workload and to create committees that can function more effectively due to its composition consisting of a smaller grouping that can focus on key areas. The governing body should determine which committees are required by assessing which are key risk areas for the organisation. Examples of committees that could be established include committees for audit, finance, social and ethics, fundraising, human resources and risk or a combination of some of these.

5.2. Audit Committee

King III, Principle 2.6: The board should ensure that the company has an effective and independent audit committee.

The best practice recommendations regarding audit committees in King III may be difficult to achieve for most non-profit organisations. However, it is important for the governing body to consider the functions suggested for the audit committee below and to be satisfied that, in the absence of an audit committee, those functions are addressed by the governing body.

Key points to consider in relation to an audit committee or the audit functions:
- If there is an audit committee, is the chairperson of the audit committee an independent and non-executive?
- If there is an audit committee, does its membership comprise individuals who are literate in financial reporting?
and related internal controls?

- Is the audit committee or if no audit committee, the governing body informed when there is disagreement on auditing or accounting matters between the management and the external auditor or independent reviewer?
- Does the audit committee or if no audit committee, the governing body, review a written assessment (documented by management) of the going concern premise of the organisation?
- Does the audit committee or if no audit committee, the governing body review the disclosure of sustainability issues in the annual report to ensure that it is both reliable and not in conflict with the financial information?
- Does the audit committee or if no audit committee, the governing body recommend to members the appointment, reappointment and removal of the external auditor or independent reviewer?
- Does the audit committee or the governing body approve both the external auditor’s and independent reviewer’s terms of engagement and remuneration?
- Does the audit committee or the governing body monitor and report on the external auditor’s or independent reviewer’s independence?
- Does the audit committee or the governing body review the quality and effectiveness of the external audit or independent review process?

### 6. Governance duties of the board

#### 6.1. Remuneration

**Principle 2.25:** Companies should remunerate directors and executives fairly and responsibly.

**Principle 2.26:** Companies should disclose the remuneration of each individual director and certain senior executives.

**Principle 2.27:** Shareholders should approve the company’s remuneration policy.

Generally, non-executive governing body members serve on the governing body of non-profit organisations pro bono. However, where governing body members are remunerated for serving as such remuneration should be appropriate.

Executives should be remunerated fairly and responsibly in line with benchmarks for the non-profit sector.

**Key points to consider in relation to remuneration:**

- Are there remuneration policies and practices in place that address base pay and bonuses, termination of employee contracts, and severance and retirement benefits?
- Do remuneration levels reflect the contribution to the organisation’s performance by senior executives?
- Do members pass a non-binding advisory vote on the organisation’s remuneration policy every year? (Only applicable to NPCs with members.)
- Is the total amount spent on salaries of staff readily accessible by stakeholders of the organisation?

#### 6.2. Strategy, risk, performance, sustainability

**King III, Principle 2.2:** The board should appreciate that strategy, risk, performance and sustainability are inseparable.

Sustainability (as defined in the Glossary of Terms) does not necessarily imply that the organisation needs to strive to become independent of donor funding. To the contrary, it is imperative that the organisation demonstrates that it is operated in a sustainable manner to ensure that funding is attracted.

Non-profit organisations have always measured their performance not only in terms of achievement of their financial objectives, but also the advancement of social objectives. Non-profit organisations differ from for profit entities in that their main aim is not the payment of dividends and growth in share value. They create ‘value’ for their stakeholders (which includes but is not limited to the donors, communities and other beneficiaries), even if not measured in direct monetary
terms. However, in the same way as shareholders expect a return on investment, donors of non-profit organisations want to see a ‘return’ on their donation.  

The sustainability principles in King III require entities to contextualise financial performance by explaining how they have ‘performed’ with regards to society and the environment. It is now understood that the so-called non-financial matters have financial implications and vice versa. Non-profit organisations, which exist towards societal or environmental ends, and which are accustomed to reporting on and reconciling the non-financial matters to financial constraints, will find it easier to satisfy these requirements than most profit driven entities.

Reference to other industry codes:

SANGOCO’s Code requires organisations to have ‘a clear vision, mission, objectives and policies, and to adhere to them.’

The DSD’s Code recommends that governing bodies determine the organisation’s mission and purpose and states that:

‘The governing body must produce documents that set out the reasons for the organisation’s being - its mission statement, goals, objectives and policies. This includes a conflict of interest policy to guard against any possibility of personal gain, by governing body members or staff, being obtained from any of the organisation’s transactions. It should describe the needs or problems being met, the constituencies that it serves and the constituencies that support the work. Above all it should be able to explain the organisation’s uniqueness, and the compelling arguments that will attract funding. The governing body should take the lead in adhering to its constitution, policies and strategic plans.’

The Code further requires that the governing body to ensure effective organisational planning, ensure that the organisation has adequate resources, to manage the organisation’s resources effectively and to determine and monitor the organisation’s programmes and services.

Key points to consider in relation to strategy:

- Does the governing body contribute towards the development and approval of the organisation’s strategy?
- Does the governing body ensure that the strategy is aligned with the purpose of the organisation, the value drivers of its business, and the legitimate interests and expectations of its stakeholders?
- Is strategy translated into key performance and risk areas that include finance, ethics, compliance and sustainability?
- Are the associated performance and risk measures adequately identified and clear?

Key points to consider in relation to risk:

- Has the governing body developed and approved a policy and a plan that provides for an effective system and process of risk identification and management?
- Does management demonstrate to the governing body that the risk responses provide for the identification and exploitation of opportunities to improve the performance of the organisation?

Donors want assurance that their funding has been employed to promote the objectives of the non-profit. Donors often want reassurance that organisations’ funding has been used for the proper purpose.
6.4. Information technology (IT)

King III, Principle 2.8: The board should be responsible for IT governance.

In most non-profit organisations, IT has become an integral part of the business and is fundamental to support, sustain and grow the business. Not only is IT an operational enabler for an organisation, it is an important strategic asset to create opportunities and to gain competitive advantage. Non-profits have made, and continue to make a significant investment in IT. Virtually all components, aspects and processes of organisations include some form of automation. This has resulted in organisations relying enormously on IT systems. Further, the emergence and evolution of the internet, e-commerce, electronic payments and electronic communication have also enabled companies to conduct business electronically and perform transactions instantly. These developments bring about significant risks and should be well governed and controlled. Therefore IT governance is of great importance.

The complexity of IT systems does create operational risks and when one outsources IT services, for instance, this has the potential to increase risk because confidential information is outside the company. Consideration has to be given to the integrity and availability of the functioning of the system; possession of the system; authenticity of system information; and assurance that the system is usable and useful. Concerns include unauthorised use, access, disclosure, disruption or changes to the information system.

The organisation’s governing body is responsible for overseeing its Information Technology (IT) by establishing a framework (including structures, processes and mechanisms) to enable IT to deliver value to the organisation and mitigate the IT risk.

**Key points to consider in relation to IT:**

- Are effective IT policies established and implemented, including a disaster recovery plan, safeguarding of IT equipment, and password protocols?
- Does the governing body ensure that there are effective process in place to identify and exploit opportunities to improve the performance and sustainability of the organisation through the use of IT?
- Does the organisation have a senior employee or access to a contractor that is responsible for IT that is suitably experienced in IT matters and has access to and interaction with the governing body?
- Does the governing body ensure that the organisation complies with IT laws and that IT-related rules, codes and standards are considered?
- Does the governing body ensure that an Information Security Management System is developed, recorded and implemented and does the Information Security Management System ensure security, confidentiality, integrity and availability of information?

6.5. Compliance

King III, Principle 2.9: The board should ensure that the company complies with applicable laws and considers adherence to non-binding rules, codes and standards.

Compliance with all laws and regulations applicable to the organisation is important for various reasons, the most important of which include that non-compliance could result in fines, criminal liability or even personal liability for members of the governing body (for example the CEO is personally liable for transgressions of the Occupational Health and Safety Act No.85 of 1993).

**Reference to other industry codes:**

DSA’s Code of Good Practice for Non-profit organisations states that the governing body’s duty of obedience requires the governing body ‘to act to ensure that the organisation operates within the laws, and rules governing its formation and status, and in accordance with its own constitution and mission. Actions taken that contradict the organisation’s own rules or that do not fit with the organisation’s purposes as described in its constitution, may be withdrawn if challenged.’

Refer to pages 14 – 17 of the Independent Code for useful pointers on legal requirements on incorporation of the organisation, consequences and benefits of registration under the Non-profit Organisations Act 71 of 1997 and the provision for approval as a public benefit organisation under the Income Tax Act.
Key points to consider in relation to compliance:

- Does the organisation know which laws, rules and regulations apply to it?
- Does the governing body assume responsibility for and monitor the organisation’s compliance with applicable laws and those non-binding rules, codes and standards that the organisation has voluntarily elected to comply with?
- Is the risk of non-compliance identified, assessed and responded to through the risk management processes?
- Has management established the appropriate structures to educate, train, communicate about, and measure compliance?
- Does a senior employee who is suitably experienced in compliance matters have access to and regular interaction on strategic matters with the governing body or appropriate governing body committee?
- Does the governing body receive assurance on the effectiveness of the internal controls intended to ensure compliance with laws, rules, codes and standards?

6.6. Internal control environment

While it is understood that very few non-profit organisation’s have a formal internal audit function, the underlying principles of internal audit are important.

King III, Principle 2.10: The board should ensure that there is an effective risk-based internal audit.

Reference to other industry codes:

DSD’s Code in dealing with financial management states:
“Unlike businesses that earn their income by selling goods or services, and unlike the government whose resources are provided by taxation, a non-profit organisation does not own the resources it raises. Non-profit organisations are expected to be careful and effective managers of the resources entrusted to them by donors, sponsors and the state. Financial management systems, no matter how simple and basic, need to be developed and maintained by an organisation’s office bearers to ensure the appropriate use of resources.”

Once the risks in an organisation are identified certain measures (also known as internal controls) should be put in place to effectively measure these risks. These risks include financial risk such as fraud but also other risks such as reputational risk (which are also likely to have financial implications).

Key points to consider in relation to the internal control environment:

- Is a senior employee or service provider responsible for establishing and maintaining an effective internal control environment? Is this senior employee or service provider independent and objective?
- Is the approach to the internal control environment informed by the strategy and risks of the organisation?

6.7. Stakeholder relationships

King III, Principle 2.11: The board should appreciate that stakeholders’ perceptions affect the company’s reputation.

Stakeholder management in the context of the non-profit sector is very important. Its survival depends on it. Stakeholders of a non-profit organisation may include all or some of the following: donors, members, employees, regulators, media, suppliers, clients, communities, partners, creditors, beneficiaries.

Reference to other industry codes:

The Independent Code refers to the following as the typical stakeholders of a Non-profit organisation:

- Donors
- Beneficiaries
- Members
- Employees
Key points to consider in relation to stakeholder relations:
- Are stakeholders that could materially affect the operations of the organisation identified; and are their legitimate interests and expectations understood and evaluated?
- Does management have a strategy and policies for the management of the relationship with each key stakeholder grouping?

6.8. Integrated annual report

King III, Principle 2.12: The board should ensure the integrity of the company’s integrated report

Non-profit organisations should consider the benefits that flow from auditing the financial statements, such as increased donor confidence. Local and international donors generally require project audits.

Note that King III refers to the ‘annual report’ as an ‘integrated report’ to denote the importance of integrating financial and sustainability performance. Many non-profit organisations still issue annual reports as opposed to integrated reports. Notwithstanding what it is called we are of the view that non-profit organisations should aspire to have integrated information in their formal reporting to stakeholders, i.e. the financial and sustainability aspects of the reporting should be connected and integrated. It has the benefit that it provides stakeholders with a holistic picture of both the organisations finances and the output or impact of its operations. It is also intended to be forward looking.

Non-profit organisations, that are used to taking into account a wide group of stakeholders, will also find application of King III principles in relation to integrated reporting, corporate citizenship and governing stakeholder relationships more easier than will most profit driven entities – if not in practical execution then at least in concept.

Key points to consider in relation to an annual report or integrated report:
- Does the governing body ensure that the organisation has implemented a system of review and authorisation designed to ensure the truthful and factual presentation of its financial position?
- Does the governing body include commentary on the organisation’s financial results in the annual integrated report? Does the governing body disclose in the organisation’s annual integrated report whether the it is a going concern and will continue to be a going concern in the year ahead; and if there is concern about the going concern status, the reasons therefore and the steps the organisation is taking to remedy the situation?
- Is a remuneration report included in the annual integrated report?
- Does the organisation disclose whether the chairperson is an independent non-executive governing body member, and if not, the reason for this?
- Does the report disclose the nature of the organisations dealings with stakeholders and the outcomes of these dealings?
- Does the report disclose an overview of the appraisal process of the governing body, governing body committees, individual governing body members; the results of this appraisal process; and action plans emanating from results of the appraisal?
- Does the governing body disclose the number of meetings held each year by the governing body and each governing body committee; and which meetings each governing body member attended (as applicable)?
- Does the report disclose whether the governing body committee has satisfied its responsibilities for the year in accordance with the formal terms of reference?
- Does the report disclose the names and qualifications of all members of the governing body committees during the period under review, and the period that each member has served on the committees?
- Does the report include a statement on whether the governing body is satisfied that the auditor or independent reviewer is independent of the organisation?
Does the report include commentary on the financial statements; the accounting practices; and the internal financial controls of the organisation?

6.9. Business rescue or other turnaround mechanisms.

*King III, Principle 2.15: The board should consider business rescue proceedings or other turnaround mechanisms as soon as the company is financially distressed as defined in the Act*

The business rescue mechanism is only available to organisations incorporated as NPCs in terms of the Companies Act. Other types of Non-profit organisations should consider other turnaround mechanisms when financially distressed. It forms part of the fiduciary duties of members of the governing body to ensure that the organisation has sufficient funds to pay its debts as they fall due, to develop, implement and monitor its fundraising strategy annually and to recognise financial distress that may lead to financial crisis and to manage this in the best interest of the organisation.

A useful guideline even for those non-profit organisations that are not companies to monitor whether the organisation is financially distressed and whether it appears reasonably unlikely that the organisation will pay its debts when due within the next six months; or likely that the organisation will become insolvent within the next six months.

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