



BBBEE COMMISSION MAKES FINDING AGAINST THE MTN ZAKHELE FUTHI SCHEME

By Pieter Steyn, Director

LEGAL BRIEF AUGUST 2019

The Broad Based Black Economic Empowerment (BBBEE) Commission has published its findings and recommendations following its investigation of the MTN Zakhele Futhi Scheme. This is only the fourth case in respect of which final findings have been published by the Commission. The Commission found that the Scheme contains “elements of fronting” in that the black shareholders and directors of MTN Zakhele were “restricted or inhibited from participating in the activities of” MTN Zakhele, MTN Group and MTN South Africa. These restrictions included that dividends required MTN Group’s consent, the chairperson of the MTN Zakhele board was appointed by MTN Group, the consent of a MTN Group appointed director was required for certain matters and a quorum of the MTN Zakhele board required the presence of a MTN appointed director. Black investors in MTN Zakhele were “essentially passive investors in the scheme”. The Commission noted that MTN disagreed with the preliminary findings of the Commission that there had been an “apparent violation of the BBBEE Act”, but had expressed a willingness to remedy the concerns raised by the Commission.

The Commission’s recommendations included that:

- > MTN Zakhele be granted the right to nominate a director to MTN Group’s board and that the above restrictions are removed;
- > disciplinary proceedings be instituted by MTN Group and MTN South Africa against its “officials” who had “defied” the Commission’s initial “advice” on the Scheme;
- > MTN Group issues a public apology for such “defiance”;
- > certain senior managers and the directors of MTN Group as well as MTN Zakhele’s directors must undergo training on the BBBEE Act and corporate governance; and
- > the MTN Group must develop a compliance programme for BBBEE.

If these recommendations are not implemented, the Commission “may”:

- > refer MTN Group and its directors to the South African Police Service or National Prosecuting Authority for criminal prosecution for contraventions of the BBBEE Act;
- > consider instituting court proceedings to restrain any breach of the BBBEE Act;
- > refer its findings to the National Treasury for possible inclusion of MTN Group and MTN South Africa in the register of tender defaulters; and

- > refer its findings to the Independent Communication Authority of South Africa (ICASA) for investigation and possible withdrawal of MTN's licences.
- > This case raises several issues of concern. Restrictions and undertakings are common practice in BBBEE ownership and financing transactions and the Commission gives no guidance on when such restrictions and undertakings may in its view raise a BBBEE concern. This causes uncertainty as such restrictions and undertakings may be commercially justifiable and reasonable protections for the measured entity, its other shareholders and funders especially where favourable commercial terms are offered to the BBBEE shareholders (black people acquired MTN Zakhele shares at a 20% discount to their market value).

MTN Zakhele only has a 4% shareholding in MTN Group, yet the Commission has recommended that MTN Zakhele be granted a right to nominate a director of MTN Group. A 4% minority shareholding would generally not justify a right to appoint a director in normal commercial practice and the Codes of Good Practice on BBBEE issued in terms of the BBBEE Act do not require a BBBEE shareholder to have this right. Furthermore, the composition of a company's board of directors is measured for BBBEE purposes under the management control element in terms of the Codes and not the ownership element so there is no basis in the Codes for the Commission's requirement. The Codes permit both indirect shareholdings and "passive" investments by black people. BBBEE shareholders are not required by the Codes to be involved in the management of their underlying investments. The Commission however appears to view the absence of a right to appoint a director as constituting a fronting risk. This arguably amounts to imposing an additional BBBEE ownership requirement to those already expressly set out in the Codes. As the Codes may only be amended by the Minister of Trade and Industry, this approach is open to challenge.

Section 13J(5) of the BBBEE Act provides that if the Commission is of the view that a fronting practice may have occurred, it is legally obliged to refer the practice to the National Prosecuting Authority (NPA) and South African Police Force (SAPS). This is an unqualified obligation. The Commission accordingly has no discretion to make remedial recommendations or to enter into negotiations with the relevant parties if it believes a fronting practice may have occurred. The Commission's approach of making recommendations together with a threat of referral to the NPA, SAPS or other regulator, is accordingly open to challenge. The Commission is also not empowered by the BBBEE Act to impose penalties or fines and its findings are not legally binding on a court.

It is not yet clear what MTN's response to the Commission's findings is. An acceptance of the Commission's robust recommendations may (notwithstanding MTN disputing the Commission's findings) negatively affect MTN's image and reputation, especially as the required public apology and disciplinary proceedings against MTN employees is likely to be perceived as evidence of at least some wrongdoing by MTN. This case may be a precedent for future and existing cases so its final outcome needs to be carefully monitored.

The MTN Zakhele scheme has allowed over 120 000 black people to acquire shares in a JSE listed company. This achievement is fully consistent with the object of the BBBEE Act to promote and support the broad-based empowerment of black people. The Commission's narrow focus on certain terms and conditions of the scheme and its aggressive remedial approach carries the risk of disincentivising such schemes in future to the ultimate detriment of ordinary black people.

Legal notice: Nothing in this publication should be construed as legal advice from any lawyer or this firm. Readers are advised to consult professional legal advisers for guidance on legislation which may affect their businesses.

CONTACT THE AUTHOR



PIETER
STEYN

Title: Director
Office: Johannesburg
Direct line: +27 (0) 11 535 8296
Fax: +27 (0) 11 535 8696
Email: psteyn@werksmans.com

Click [here](#) for his profile

> Keep us close

The Corporate & Commercial Law Firm
www.werksmans.com

A member of the LEX Africa Alliance

ABOUT WERKSMANS ATTORNEYS

Established in the early 1900s, Werksmans Attorneys is a leading South African corporate and commercial law firm, serving multinationals, listed companies, financial institutions, entrepreneurs and government.

Operating in Gauteng and the Western Cape, the firm is connected to an extensive African legal alliance through LEX Africa.

LEX Africa was established in 1993 as the first and largest African legal alliance and offers huge potential for Werksmans' clients seeking to do business on the continent by providing a gateway to Africa.

With a formidable track record in mergers and acquisitions, banking and finance, and commercial litigation and dispute resolution, Werksmans is distinguished by the people, clients and work that it attracts and retains.

Werksmans' more than 200 lawyers are a powerful team of independent-minded individuals who share a common service ethos. The firm's success is built on a solid foundation of insightful and innovative deal structuring and legal advice, a keen ability to understand business and economic imperatives and a strong focus on achieving the best legal outcome for clients.

