

Impact Economy Digital Edition 2021



South Africa

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LEGAL AND POLICY FRAMEWORK

Legislation

- 1 | Has your jurisdiction enacted any primary or secondary legislation addressing environmental, social and governance (ESG) factors in banking, finance and corporate law, or legislation addressing the pursuit of other non-financial objectives by companies and investors?

The Constitution of the Republic of South Africa contains a Bill of Rights that includes several socio-economic and environmental rights that generally apply to the state as well as private persons (natural and juristic persons), and that are actionable by affected persons, either directly in terms of the Constitution, or in terms of statutes enacted in furtherance of specific aspects of the Constitution. Potentially relevant fundamental rights include (among others) the rights to human dignity, freedom and security and the right against slavery, servitude and forced labour, the rights to life, healthcare, food, water and social security, the right to an environment that is not harmful and the rights of access to information and to just administrative action.

The Broad-based Black Economic Empowerment (BEE) Act and public procurement regulations are central instruments in a long-term national scheme to incentivise and facilitate investment in enterprises that are conducted by, or which benefit, black South Africans (as defined in the legislation), women, people with disabilities and the youth. Within that framework, the Financial Sector Charter seeks to encourage development of intermediaries and suppliers that meet those criteria ('previously disadvantaged individuals'), within the financial services ecosystem. The Financial Services Conduct Authority (FSCA), the regulator of pension funds, collective investment schemes, insurers, asset managers and financial intermediaries, issued Guidance Note 1 of 2019, in which it defines the term 'ESG factors' to mean: 'environmental, social and governance factors. In the South African context, and specifically in respect of assets located in South Africa, these factors include, but are not limited to, the manner in which broad-based black economic empowerment is advanced'.

Regulation 28 to the Pension Funds Act 1956 (the Pension Funds Act) regulates a fund's assets spreading requirements and prescribes an obligation on a pension fund's board of trustees to consider any factor that may materially affect the sustainable long-term performance of the assets the fund intends investing in, as well as ongoing consideration of assets it is already invested in, including, but not limited to, those of an environmental, social and governance character. The regulation's impact extends beyond the immediate scope of trustees' duties and liabilities due to the extent to which pension assets dominate South Africa's national savings, local stock exchanges and the portfolios of insurers that provide policies to pension funds and administrators and asset managers who manage pension monies.

The National Environment Management Act and National Water Act place duties of care and obligations of mitigation and remediation on persons owning, controlling or using land and water resources, and in practice these statutes affect the due diligence and investment practices of investors and lenders.

South Africa has a carbon tax and offset regulations, and the Climate Change Bill of 2018 (not yet enacted) proposes mandatory carbon budgets.

The Companies Act 2008 (the Companies Act) obliges certain entities, including state-owned corporations and public listed companies, to constitute a social and ethics committee of the board of directors, whose duties include monitoring the entity's approach in regard to matters relating to social and economic development including specific reference to the 10 United Nations Global Compact principles, good corporate citizenship and the impact of the entity's activities, products or services on environment, health and public safety. Obligated entities must publish annual integrated reports, based on the Integrated International Reporting Council definition as a 'concise communication about how an organisation's strategy, governance, performance and prospects, in the context of its external environment, lead to the creation of value in the short, medium and long term'.

South Africa has ratified the Paris Agreement (as a non-annex 1 country) in terms of the United Nations Framework Agreement on Climate Change, and accordingly is committed to an Intended Nationally Determined Contribution in respect of greenhouse gas emissions. In May 2019, the national government published a draft National Climate Adaptation Strategy for comment from the public.

Prudential Standard GOI 3 requires an insurer's investment policy to take into account any factor that may materially affect the sustainable long-term performance of an insurer's assets, including ESG factors.

Policy guidance and development

- 2 | How would you describe the general level of policy guidance and development regarding ESG, impact investing and purpose-driven companies in your jurisdiction?

The National Development Plan, a long-term South African development plan which, among other things, aims to eliminate poverty and reduce inequality by 2030, is very closely aligned to the United Nations' Sustainable Development Goals that were designed to be a 'blueprint to achieve a better and more sustainable future for all'. During the 2020 state of the nation address, President Ramaphosa confirmed the National Development Plan as central to South Africa's national development policy.

The National Treasury is currently leading a sustainable finance initiative that aims to, among other things:

- define sustainable finance in the South African context;

- incorporate perspectives from all parts of the financial sector, including banking, pension funds, insurance, asset management and capital markets; and
- provide recommendations on a national strategic approach and the role of regulatory agencies and industry stakeholders.

The Sustainable Finance Working Group comprises financial sector regulators and industry associations. Its members include the South African Reserve Bank, the FSCA, the Banking Association South Africa, the Council of Retirement Funds for South Africa (Batseta), the Association for Savings and Investment South Africa, the South African Insurance Association and the Johannesburg Stock Exchange.

Various climate change-related measures are being considered in line with South Africa’s National Climate Change Response Policy of 2011, the National Development Plan, and South Africa’s commitments in relation to the United Nations Framework Agreement on Climate Change.

In 2019, South Africa joined the Global Steering Group for Impact Investing (GSG), a global body promoting impact investing, becoming the first African country to do so. It is represented on the GSG by the National Task Force for Impact Investing South Africa, which is a coalition of public and private sector high-level decision makers whose role is to identify gaps on the supply and demand sides of the impact investing market in South Africa and work together to address those. The National Task Force’s activities include enabling policy and building market infrastructure, as well as advocacy, education and training.

South Africa’s policy approach has been criticised for being explicit in intent, but sparse with regard to specific targets for measuring compliance and for achieving the proposed outcomes.

INVESTMENT

Regulatory and fiduciary duties

- 3 | Are institutional investors and financial intermediaries legally required to consider ESG factors when making investment decisions? Must any additional non-financial principles and objectives be considered?

Pension Funds are required to consider any factor that may materially affect the sustainable long-term performance of the asset they are invested in or plan to invest in including, but not limited to, those of an ESG character. Regulation 28 to the Pension Funds Act supports the approach to deploying capital into markets that will earn adequate risk-adjusted returns suitable for the fund’s specific member profile, liquidity needs and liabilities. As such, investments have to be cognisant of their suitability with reference to the fund’s current and future membership.

Prudential Standard GOI 3 requires an insurer’s investment policy to take into account any factor that may materially affect the sustainable long-term performance of assets, including ESG factors.

Subject to the general duty of care owed to its members and clients, there is no legal requirement for other institutional investors such as alternative investment funds or collective investment schemes (CIS) to take into account ESG factors for investors (unless its constitutional documents or mandate prescribe that).

Voluntary standards and best practices

- 4 | What voluntary standards and best practices are commonly followed in your jurisdiction with regard to integrating ESG factors and other non-financial principles into investment decisions?

The Code for Responsible Investing in South Africa (CRISA) is a voluntary code that applies to both institutional investors (e.g., pension funds,

insurers and CISs) and their service providers (asset managers, fund managers and consultants). CRISA provides guidance on how institutional investors should execute investment analysis and investment activities and exercise their rights so as to promote sound governance.

The King Codes of which The King IV Report on Corporate Governance for South Africa, 2016 (King IV™) is the latest iteration, sets out ‘voluntary principles and leading/recommended practices’ as guidelines to promote good corporate governance across all kinds of organisations in South Africa. In terms of the Companies Act and the Johannesburg Stock Exchange (JSE) Listings Requirements certain companies are obliged to report on their application of King IV principles and recommendations in their annual integrated reports; however, many companies and other entities, including institutional investors, also utilise the King IV framework on a voluntary basis. The King IV principles promote the notion of the responsible corporate citizen, adopting a stakeholder approach and practising responsible investment to promote good governance and the creation of value by the companies in which it invests.

As of November 2019, there were 63 South African-headquartered signatories to the UN supported Principles for Responsible Investment.

The Association for Saving and Investment SA (ASISA) is a body voluntarily mandated by companies in South Africa’s investment management industry, long-term insurance industry and retirement fund industry. ASISA represents its members’ interests in discussions and negotiations with regulators, policy makers and other stakeholders. ASISA also has a number of codes, standards and guidelines that its members must abide by, which, among other things, promote the idea of responsible investment and ownership practices.

The South African Banking Association’s 2014 Guidance on Sustainable Banking has been an influential instrument in guiding sustainable banking practice. It is also not uncommon for financiers of South African capital projects to apply the Equator Principles in the assessment of the projects’ legitimacy and ‘bankability’.

Measurement, reporting and disclosure

- 5 | What voluntary and statutory measurement, reporting and disclosure frameworks are followed in your jurisdiction with regard to ESG and other non-financial factors?

A 2018 study carried out by Genesis Analytics and Impact Amplifier found very little use by investors, intermediaries and investees of formal impact measurement techniques in South Africa, with the UN Sustainable Development Goals, Impact Reporting and Investment Standards, Donor Committee for Enterprise Development standards, and ESG criteria (eg, MSCI ESG metrics) being the most commonly used. The majority of respondents cited the use of in-house metrics.

The Global Reporting Initiative standards and recommendations have been influential in the reporting of ESG and other non-financial factors in South Africa.

King IV is the primary voluntary instrument for companies that are not obliged to subscribe to it.

The CRISA principles are also commonly referenced among institutional investors, and publishing annual reports and disclosures on the application of CRISA is voluntary, with no formal oversight methodology or mechanism.

Most of South Africa’s significant institutional investors, including most notably the Government Employees Pension Fund and its state-owned asset manager the Public Investment Corporation, are signatories to the UN Principles for Responsible Investment.

A number of investors have adopted the principles and recommendations of the Task Force on Climate-related Financial Disclosures (TCFD). While the TCFD is not mandatory or encapsulated in legislation, a number of lenders require disclosure to be in line with the TCFD

requirements and many require climate change impact assessments to be provided before advancing funds. The Equator Principles are also relatively commonly applied in relevant investments.

The Sustainable Development Goals inform the National Development Plan, a national government blueprint for socio-economic development until 2030, and they are becoming more commonly adopted by developmental NGOs, corporate foundations and municipal governments in defining investment objectives.

Ratings, indices and guidelines

6 | What ratings, indices and guidelines are used to benchmark adherence to ESG principles and other non-financial factors in your jurisdiction?

Regarding sustainability benchmarks that are taken into consideration in South Africa, the MSCI South Africa ESG Leaders Index is a capitalisation-weighted index that offers exposure to companies with high ESG performance relative to other South African entities. It shows that ESG leaders recorded 14.45 per cent annualised gross returns over a 10-year period compared with 9.75 per cent for MSCI South Africa – an index tracking the performance of South African equities.

In 2015, the JSE partnered with FTSE Russell to produce the FTSE/JSE Responsible Investment index series, which comprises all eligible companies who achieve the required minimum FTSE Russell ESG rating.

Earlier this year, the JSE released for public comment the proposed amendments to its debt listing requirements for the new Sustainability Segment, which will include sustainability instruments under the International Capital Market Association green bond principles, social bond principles and sustainability guidelines. The new segment aims to facilitate trades in sustainability-linked instruments and provide a platform to raise funds for sustainable projects.

Incentives, benefits and financial support

7 | Are any fiscal incentives or other benefits available in your jurisdiction to encourage institutional investors and financial intermediaries to integrate ESG and other non-financial factors into their investment decision-making?

There are no fiscal incentives specifically encouraging investors to integrate ESG and other non-financial factors into their investment decision-making.

The main tax incentive for investors is the venture capital company regime, but it does not specifically include ESG criteria.

Some other fiscal incentives do refer to ESG type criteria, but they are focused on the taxpayer itself, not on investors. These include limited deductions and allowances available for expenditure related to renewable energy, energy efficiency savings, environmental rehabilitation and conservation.

Special economic zones (SEZs) also enjoy certain tax incentives, including a preferential 15 per cent corporate tax rate. Certain SEZs are, for example, intended to incentivise cooperation between the manufacturing and renewable energy sectors, as part of the South African government's Renewable Energy Independent Power Producers Programme.

In addition, 'small business funding entities' that provide funding for small, medium or micro-sized enterprises, on a non-profit basis and with an altruistic or philanthropic intent could qualify for an income tax exemption.

While the Department of Trade and Industry offers a number of incentives, none of these expressly focuses on ESG criteria. However, a number of these incentives, such as the Black Industrialists Scheme, include ESG-type criteria such as job creation and green technology.

Impact investing

8 | In addition to ESG factors, what considerations and practices are commonly integrated into impact investment strategies?

The following considerations or practices are commonly integrated into impact investing strategies in South Africa:

- a theory of change or strategic impact objective;
- an impact theme (eg, education, health, access to finance, housing, renewable energy – often aligned with one or more sustainable development goals);
- due diligence;
- location and geography;
- impact measurement and management;
- structuring and tax considerations;
- financing and funding;
- return expectations and exits;
- ticket and investment sizes;
- investment type; and
- underlying asset classes and impact classes.

The objectives of the B-BBEE laws (to address inequalities brought about by the apartheid system and to empower previously disadvantaged individuals through job-creation, supplier development, investment, favourable credit terms, accelerated payment arrangements, enterprise ownership and management, etc) are commonly integrated in impact investment strategies. Companies report on such activities to independent Broad-based Black Economic Empowerment (BEE) verification agencies that award BEE or 'Empowerment' accreditation at various levels of compliance and achievement.

PURPOSE-DRIVEN COMPANIES

Legal recognition and certification

9 | What legal forms or statuses are used in your jurisdiction to establish purpose-driven companies?

There are two types of company that may be incorporated in South Africa: a profit company and a non-profit company. A profit company (which may be a private, personal liability, public or state-owned company) is incorporated for the purpose of financial gain for its shareholders. A non-profit company is a company incorporated to pursue a public benefit or an object relating to one of more cultural or social activities, or communal or group interests. (There is no specific legal form or company status similar to the 'benefit corporation' established in some states in the United States.)

There is no specific public certification for companies that pursue social or environmental purposes. In the context of taxation, a non-profit company or 'public benefit organisation' (PBO) may apply for tax exempt status under the Income Tax Act if it pursues one or more statutorily prescribed public benefit activities (PBAs). In the non-profit space, a company may register and be certified as a non-profit organisation under the Non-profit Organisations Act.

Section 12J of the Income Tax Act allows investors to deduct the full amount invested in a Section 12J venture capital company from their taxable income while still enjoying the return on the full investment. Venture capital companies are specifically designed to concentrate investment expertise in favour of local small to medium enterprises.

Insofar as private certifications are concerned, it is possible for a company to pursue a 'triple bottom line' purpose to enable it to become a certified B Corporation. To date, there are nine certified B Corporations in South Africa.

It is possible for a foreign purpose-driven company to register in South Africa as an external company.

Purpose and mission

10 | What rules and standard practices govern the establishment of companies' social or environmental purposes and mission?

The Companies Act and a company's constitutional document, the Memorandum of Incorporation (MOI), govern the establishment of a company's social or environmental purposes.

As a first step, the incorporators must determine whether to incorporate a profit company with the purpose of generating financial gain for shareholders, or a non-profit company with some public benefit or other object. Once incorporated, a company is a juristic person that has all the legal powers and capacity of an individual, except to the extent that it is incapable of exercising any such power (eg, to vote) or having any such capacity, or the MOI provides otherwise.

The purposes of a company may be described in more or less detail, and may be expressly restricted, in the MOI. While some companies will publish mission statements, there is no statutory obligation to do so.

The MOI is legally binding:

- between the company and each shareholder;
- between or among the shareholders of the company, and
- between the company and each director, prescribed officer, or member of a board committee, in each case in the exercise of their respective functions within the company.

The MOI may be amended by a special resolution of the shareholders (generally 75 per cent approval), or in compliance with a court order. Unless the MOI provides otherwise, the board of directors may amend a MOI to vary authorised but unissued shares, or to determine the rights, limitations and other terms attaching to such shares.

The MOI of a non-profit company without members may be amended by its board of directors.

Companies may pursue social or environmental purposes even if they are not a direct source of profit. Under the Companies Act a profit company is one that has been incorporated for the purpose of generating financial gains for shareholders. However, that purpose (to generate profits) does not exclude a company from pursuing social or environmental purposes.

There are no restrictions applicable to certain business sectors regarding the establishment of social or environmental purposes by a company.

Profit distribution, winding up and remuneration

11 | What rules and restrictions govern profit distributions for purpose-driven companies in your jurisdiction?

Profit companies

The ordinary rules and restrictions that govern profit distributions would apply to a purpose-driven profit company. A company must not make any proposed distribution unless three requirements are met. First, the distribution must be pursuant to an existing legal obligation of the company or a court order, or the board must have authorised the distribution by resolution. Second, it must reasonably appear that the company will satisfy the solvency and liquidity test, set out in section 4 of the Companies Act, immediately after completing the proposed distribution. Third, the board of the company must have, by resolution, acknowledged that it has applied the solvency and liquidity test, and concluded that the company will satisfy that test immediately after completing the proposed distribution (the S&L Resolution).

Once a distribution has been approved by the board, a company must carry it out fully, subject to certain provisos. If the distribution has not been completed within 120 business days of the S&L Resolution, the board must reconsider the solvency and liquidity test with respect to the

distribution to be made, and the company must not proceed with such distribution unless the board has adopted a further S&L Resolution.

In the context of fundamental transactions, a company that is the subject of an offer is subject to restrictions on 'frustrating action' – action that could effectively result in an offer being frustrated or shareholders being denied an opportunity to decide on its merits – which preclude the making of a distribution that is abnormal as to timing and amount.

A company's MOI may include additional rules and restrictions governing profit distributions.

Non-profit companies

As a general rule, the income and property of non-profit companies is not distributable to its incorporators, directors, members (if any), officers or persons related to them.

12 | What rules and restrictions govern the winding up of purpose-driven companies?

Profit companies

There are no specific rules and restrictions governing the winding up of purpose-driven profit companies. There are three methods by which a profit company may be wound up, each with its own rules and requirements. First, de-registration if a company is no longer carrying on business or is not in operation. Second, a voluntary winding up by way of a special resolution (ordinarily 75 per cent approval) at the instance of the shareholders, either in terms of a solvent (members') winding up, or an insolvent (creditors') winding up. Third, a compulsory winding up by means of an application to court by the company itself, the shareholders, the creditors, or any combination thereof.

Non-profit companies

Upon the winding up or dissolution of a non-profit company:

- no past or present member or director of that company, or person appointing a director of that company, is entitled to any part of the net value of the company after its obligations and liabilities have been satisfied; and
- the entire net value of the company must be distributed to one or more non-profit companies, registered external non-profit companies carrying on activities within South Africa, voluntary associations or non-profit trusts.

The distribution must be to an entity or entities that have objects similar to the main object of the non-profit that is being wound up or dissolved, as determined: in terms of the company's MOI; by its members (if any) or its directors, at or immediately before the time of its dissolution; or by the court, if the MOI, or the members or directors fail to make such a determination.

13 | What rules and restrictions govern the remuneration of directors, officers, employees and third parties?

Profit companies

Except to the extent that the MOI of a company provides otherwise, a company may pay remuneration to its directors for their service as directors, subject to subsection, but only in accordance with a special resolution (generally 75 per cent approval) approved by the shareholders within the previous two years.

Non-profit companies

A non-profit company must not pay any portion of its income or transfer any of its assets to any incorporator, member, director, or person appointing a director, of the company, except as reasonable

remuneration for goods delivered or services rendered to or at the direction of the company.

The remuneration of officers, employees and third parties is generally determined by contractual agreement (employment, consultancy or supply agreement).

Measurement, benchmarking and reporting

14 Are purpose-driven companies legally required to measure, benchmark and report the social and environmental impact of their business?

There is no generally applicable legal requirement for purpose-driven companies to measure, benchmark and report the social or environmental impact of their businesses. The MOI of a company may include provisions that require the measurement, benchmarking or reporting of social or environmental impacts of that company's businesses. Additionally, similar requirements may apply in terms of contractual agreements concluded by the company.

In the context of broad-based black economic empowerment (B-BBEE), Johannesburg Stock Exchange (JSE)-listed companies, public entities and organs of state are required to submit annual B-BBEE compliance reports to the B-BBEE Commission within 30 days of the approval of the entity's audited financial statements or within 90 days of the end of the relevant financial year, and to publish such reports on their websites.

Institutional investors are increasingly demanding the measurement and reporting of ESG and other non-financial factors by companies in which they are invested. For example, pension funds and insurers are required to consider ESG factors in their investment decision-making. Additionally, the Code for Responsible Investing in South Africa recommends that 'an institutional investor should incorporate sustainability considerations, including environmental, social and governance, into its investment analysis and investment activities as part of the delivery of superior risk-adjusted returns to the ultimate beneficiaries'.

15 What statutory and voluntary standards, guidelines and best practices are followed by purpose-driven companies in your jurisdiction with regard to the measurement and reporting of ESG and other non-financial factors?

Generally speaking, the measurement and reporting of ESG and other non-financial factors is unregulated and voluntary in South Africa at present. As such, there are many different approaches that may be used by purpose-driven companies to measure and report on such factors: principles, ratings, performance indicators and targets, narratives, valuation and evaluation methodologies.

Measurement

A 2018 study carried out by Genesis Analytics and Impact Amplifier found very little use by investors, intermediaries and investees of formal impact measurement techniques in South Africa, with the UN Sustainable Development Goals, Impact Reporting and Investment Standards, Donor Committee for Enterprise Development standards, and ESG criteria (eg, MSCI ESG metrics) being the most commonly used. The majority of respondents cited the use of in-house metrics.

Initiatives such as the Impact Management Project, a forum for building global consensus on how to measure and manage impacts, will influence the evolution and adoption of impact measurement approaches in South Africa.

Reporting

The King IV Code of Corporate Governance, which focuses on value creation in a sustainable manner, promotes 'integrated reporting', based

on the Integrated International Reporting Council definition: it contemplates 'a concise communication about how an organisation's strategy, governance, performance and prospects, in the context of the external environment, lead to the creation of value in the short, medium and long term'.

The Global Reporting Initiative standards and recommendations have been influential in the reporting of ESG and other non-financial factors in South Africa.

Director liability and private enforcement

16 What rules govern the liability of directors of purpose-driven companies for compliance with social and environmental standards and principles? In addition to shareholders, are stakeholders entitled to hold directors accountable through private enforcement action?

The ordinary company law rules under the Companies Act and at common law primarily govern the liability of directors of companies and would apply to directors of purpose-driven companies.

The board of directors has primary responsibility for managing and directing the business and affairs of a company. Directors owe fiduciary duties to the company under the Companies Act and the common law, all of which flow from the overarching duty to act in good faith in the best interests of the company. Directors also have a duty to act with the degree of care, skill and diligence that may reasonably be expected of a person carrying out the same functions as that director, and having the general knowledge, skill and experience of that director. The Companies Act includes a business judgement rule that affords some protection to directors in carrying out their duties.

Under the Companies Act, directors are held liable in accordance with the principles of common law for any damages, loss or costs suffered by the company as a result of:

- a breach of a fiduciary duty as a consequence of a breach of their duties to disclose personal financial interests, to avoid a conflict of interest, to communicate information to the company, to act in good faith for a proper purpose or to act in the best interests of the company; and
- delict or tort law as a consequence of a breach of their duties of care, skill and diligence, or a breach of any provision of the Act or any provision of the company's MOI.

Under the Companies Act, certain stakeholders are entitled to hold directors accountable through private enforcement action:

- shareholders have a statutory right to apply to court for an appropriate order to rectify harm done to the securities holder by any of the company's directors, to the extent that they may be held liable;
- shareholders, directors or trade unions representing employees may apply to court to interdict a company from doing anything inconsistent with the Companies Act (the provisions of which may be referred to or incorporated by reference into a company's MOI);
- a company, shareholders, directors, company secretary, a trade union or employees' representative may apply to court for an order to declare a director delinquent or under probation in certain circumstances; and
- a statutory derivative action permits shareholders, directors, company secretaries, trade unions representing employees, or a person who has been granted leave by a court where the court is satisfied that leave is necessary to protect a right, to demand that the company bring or continue proceedings, or take related steps, to protect the legal interests of the company.

State supervision

17 | Is there any form of state supervision of purpose-driven companies in relation to their social and environmental purposes?

There is no specific state supervision of purpose-driven companies in relation to their social and environmental purposes. Companies incorporated in South Africa are generally subject to regulatory oversight by the Companies and Intellectual Property Commission, which has a mandate to, among other things, monitor proper compliance with the Companies Act.

Certain companies may be subject to regulatory supervision and oversight by one or more regulators insofar as their business activities, products or services are concerned. The Financial Sector Regulation Act 2017 established two new regulators: the Prudential Authority, within the South African Reserve Bank, tasked with prudential regulation; and the Financial Sector Conduct Authority (FSCA), tasked with market conduct regulation. The Prudential Authority is, among other things, responsible for the prudential regulation of insurers. The FSCA's functions include regulating and supervising the conduct of various financial institutions (particularly in relation to the provision of financial services), including pension funds, insurers and collective investment schemes, in accordance with applicable financial sector laws.

In the context of taxation, the South African Revenue Service Tax Exemption Unit may monitor the activities of a non-profit company or PBO that has been granted tax exempt status under the Income Tax Act 58 of 1962.

To the extent that the broad-based black economic empowerment framework applies, the B-BBEE Commission has a mandate to oversee, supervise and promote adherence to Broad-Based Black Economic Empowerment Act 53 of 2003.

Incentives and benefits

18 | Are any fiscal incentives or other benefits available for purpose-driven companies in your jurisdiction? What is the scope of these benefits and what requirements apply?

There are limited South African tax incentives or other benefits available for purpose-driven companies.

PBOs that conduct prescribed PBAs, and small business funding entities that provide funding for small, medium or micro-sized enterprises, on a non-profit basis and with an altruistic or philanthropic intent, qualify for an income tax exemption.

Taxpayers may also claim limited tax deductions for donations made to PBOs carrying on a more limited set of PBAs, including the funding of other qualifying PBOs.

There are also limited tax deductions and allowances available for, among other things, certain expenditure related to the production of renewable energy, energy efficiency savings, environmental rehabilitation and conservation.

Special economic zones (SEZs) also enjoy certain tax incentives, including a preferential 15 per cent corporate tax rate. Certain SEZs are, for example, intended to incentivise cooperation between the manufacturing and renewable energy sectors, as part of the South African government's Renewable Energy Independent Power Producers Programme.

While the Department of Trade and Industry offers a number of incentives, none of these expressly focuses on ESG criteria. However, a number of these incentives, such as the Black Industrialists Scheme, includes ESG-type criteria such as job creation and green technology.

Public procurement

19 | Do the public procurement rules and policies in your jurisdiction confer any advantages on companies for pursuing social or environmental purposes? If so, what conditions apply?

The public procurement rules and policies in South Africa have no specific set aside contracts for companies that pursue social or environmental purposes. These factors may be an advantage if they are specified as such or as qualification criteria for a specific contract. This is because in terms of section 217 of the Constitution, an organ of state is required to procure goods and services in a fair, transparent, competitive and equitable manner. Section 217(2) of the Constitution permits the government to implement a procurement policy that provides for categories of preference in the allocation of contracts, and for the protection or advancement of persons, or categories of persons, disadvantaged by unfair discrimination. The Preferential Procurement Policy Framework Act 2000 (PPPFA) and the regulations published under it in 2017 (the PPPFA Regulations) are the framework within which preferential procurement policies must be implemented. In addition to this regulatory framework, the BEE Act, which aims to address inequities resulting from the systematic exclusion of black people from meaningful participation in the South African economy, plays an important role in the award of government contracts. The BEE Act provides a legislative framework for the promotion of black economic empowerment and contains formulations to calculate a broad-based black economic empowerment (BEE) score, which is a level of empowerment used by organs of state when evaluating tenders or bids in accordance with the PPPFA.

In this regard, under the preferential procurement points system, bidders are given a score out of 100 points, of which 80 or 90 are based on price competitiveness, and 20 or 10 on the bidder's BEE status level or preference (depending on whether the contract is for 30,000 rand to 50 million rand, or above 50 million rand).

A bidder's BEE score will therefore influence its preferential procurement score for PPPFA purposes. Where two tenders have equal scores, the one with the highest BEE rating must be awarded the contract; where the BEE ratings are also equal, the one with the highest functionality points must be awarded the contract (unless there are objective criteria that justify the award to another bidder).

Economic sustainability and market competition

20 | How would you describe the level of economic sustainability and market competition of purpose-driven companies?

There is insufficient data to assess the level of economic sustainability and market competition of purpose-driven companies in South Africa. That said, there is evidence suggesting that companies (purpose-driven or not) that perform well on ESG factors outperform and are more likely to survive over time. Additionally, the competitive landscape appears to be changing in a direction such that companies without a purpose may find themselves at a competitive disadvantage in the medium to long term.

GOVERNMENT, NGO AND SUPRANATIONAL SUPPORT

Government support

21 Are there any governmental actors in your jurisdiction that are specifically dedicated to promoting and supporting socially and environmentally responsible investment practices, as well as purpose-driven companies? What purposes do they pursue and how do they do so?

South Africa's National Treasury released a technical paper on 15 May 2020, 'Financing a Sustainable Economy', which acknowledges that sustainable finance is essential for balanced and inclusive growth, based on the identification and mitigation of risks as well as the search for economic opportunities that are socially, environmentally and economically beneficial. The Treasury acknowledges that there is a need for greater policy coherence for the sector, along with regulatory guidance and oversight.

The government's stance is that addressing both climate change and South Africa's development agenda will require the reallocation of capital, the mobilisation of new financial resources and the strategic realignment of existing resources (public and private) over the short, medium and long term. The South African government has recognised the need for a just transition and various government agencies and departments, including the Treasury and the National Planning Commission, are working to understand what is needed and stimulate the creation of new jobs. By mobilising private sector funding of new and more sustainable projects, such as through the Renewable Energy Independent Power Producer Programme, the Treasury facilitates the shifting of green infrastructure investment off the national balance sheet into the private sector.

Climate change planning is becoming part of the budget process and fiscal risks monitoring by the Treasury. Economic modelling work is being undertaken and the Treasury is working towards climate classification and tagging in the budget to enable tracking of climate-related expenditure. Treasury capital appraisal guidelines, which are under review, will incorporate climate resilience. Fiscal allocations to support ecologically sustainable development through the Department of Environmental Affairs, Forestry and Fisheries are complemented with funding for public transport, clean energy and energy efficiency, water conservation and demand management.

At an intergovernmental level, the Treasury approach is to integrate climate responsiveness into provincial and municipal planning. This includes ensuring climate change-responsive budgeting through guidelines for provincial medium-term expenditure frameworks and built environment performance plans for metropolitan municipalities. Through a progressive integration and system reform, provinces and municipalities can create an intergovernmental project pipeline.

The Treasury is working with local and international partners to leverage climate change funding. The Department of Agriculture and the Treasury are working closely with the local insurance industry on an agricultural insurance product.

Another important area of focus for the Treasury is putting a price on carbon via the carbon tax, and the publishing of offset regulations to enable reduction of those taxes through climate-positive investments. This includes the Renewable Energy Independent Power Producers Programme, tax exemption for revenues earned from trading Certified Emission Reductions, accelerated depreciation allowances for machinery for renewable electricity generation and biofuels production, R&D tax incentives including for green technologies, tax incentives for biodiversity conservation, energy efficiency savings tax allowance and fiscal allocations, such as those to the Department of Environment Affairs, Forestry and Fisheries, for risk mitigation and job creation projects.

An Independent Power Producers office, run independently but set up jointly by the Department of Energy and the National Treasury, oversees a competitive bidding process, to inject privately supplied renewable energy into South Africa's fossil fuel-heavy generating mix and at the same time address the significant socio-economic challenges the country faces.

Although not specifically dedicated to supporting socially and environmentally responsible investment practices, the South African Reserve Bank (SARB) is also an important actor in this sphere. The SARB has recently joined the Network for Greening the Financial System, a voluntary network of central bankers, and is also a member of the Sustainable Finance Working Group.

South Africa recently joined the Global Steering Group for Impact Investing (GSG), a global body promoting impact investing, and is represented on the GSG by the National Task Force for Impact Investing South Africa, which is a coalition of public and private sector high-level decision makers who identify and address gaps on the supply and demand sides of the impact investing market in South Africa. The National Task Force's activities include enabling policy and building market infrastructure, as well as advocacy, education and training.

The Financial Services Conduct Authority (FSCA) recently indicated in Guidance Note 1 of 2019 that it will continue to work on refining the regulatory framework insofar as it relates to issues of sustainability, and that this could potentially lead to more detailed and refined requirements being incorporated into prudential and conduct standards. The FSCA also indicated its support of the National Treasury's development of a national strategic framework on sustainable finance and investments.

NGO support

22 Are there any non-governmental organisations (NGOs) operating in your jurisdiction that are specifically dedicated to promoting and supporting socially and environmentally responsible investment practices, as well as purpose-driven companies? What purposes do they pursue and how do they do so?

Companies whose shares are listed on the Johannesburg Stock Exchange are experiencing increased shareholder activism in respect of sustainability impact and ESG issues, from both institutional investors and NGOs, such as Just Share, the Raith Foundation and the Centre for Environmental Rights, and also international NGOs including UN supported Principles for Responsible Investment, Client Earth, the Thomson Reuters Foundation and Amnesty International.

NGOs are active in education, consumer awareness, shareholder activism (directly as minority shareholders, or by lobbying or pressurising institutional investors) and public interest litigation (usually as amici curiae or ('friends of the court') in constitutional matters).

Supranational support

23 Are there any supranational actors operating in your jurisdiction that are specifically dedicated to promoting and supporting socially and environmentally responsible investment practices, as well as purpose-driven companies? What purposes do they pursue and how do they do so?

There are a number of impact investors that are active in South Africa, including:

- the Rise Fund, which has a long track record and history of sustainability and environmental and social impact across Africa;
- the UN Green Climate Fund has invested in a South African Private Equity Fund with the intention to fund small to medium sized enterprises implementing renewable energy projects;

- Goodwell Investments BV, a Dutch-based investment firm that supports entrepreneurs in sub-Saharan Africa; and
- a number of developmental finance institutions are active in South Africa including the Dutch Development Bank (FMO), Norwegian Investment Fund for Developing Countries (Norfund), the German Corporation for International Co-operation (GIZ) and the German Development Bank (KfW), the British Council and the CDC Group, and the US International Development Finance Corporation (DFC, formerly OPIC), the International Finance Corporation (IFC). The German Development Bank, which is involved in funding South African projects focused on energy and climate, preventing domestic violence and preventing the spread of HIV/AIDS, collaborated with South Africa's National Treasury and the Cambridge Institute to produce an influential paper on green finance in 2018.

There are also a number of international programmes that South African institutions participate in, such as the United Nations Environment Programme's 'Principles for Responsible Banking', of which a number of South Africa's major banks and other institutional investors are members.

FINANCIAL TOOLS

Equity funds and loans

- 24** Does your jurisdiction regulate equity funds or other financial tools such as loans designed to scale up companies with social or environmental objectives? Even if not expressly regulated, are there venture funds specifically focused on investing in purpose-driven companies?

South Africa does not expressly regulate equity funds designated to scale up companies with social and environmental objectives, however there is an incentive regime established under section 12J of the Income Tax Act. Section 12J of the Income Tax Act provides for a tax deduction for investors investing in venture capital companies, and directs the investments of such venture capital companies towards high growing enterprises that are likely to create jobs.

In addition, there is also the BEE Act read together with the generic Codes of Good Practice on Broad-Based Black Economic Empowerment, which is aimed at incentivising and encouraging investments and engagement with businesses that are owned or operated by people defined as black South Africans.

Lastly, venture capital and private equity industries are largely funded by development financial institutions, which typically insist on a high level of compliance with environmental, social and governance requirements and reporting.

Outcomes funds

- 25** Does your jurisdiction regulate 'pay for success' investing models such as outcomes funds? Apart from specific regulation, are any of these mechanisms in force or in progress in your jurisdiction?

'Pay for success' investing models are not regulated in South Africa and there are no mechanisms in force in relation to them.

An example of an outcomes fund is the 488 million rand Green Outcomes Fund (GOF), a partnership between the National Treasury's Jobs Fund and green-economy non-profit GreenCape, the fund's implementation partner. The GOF seeks to incentivise local South African fund managers to increase investment in green small, medium and micro-sized enterprises.

Social and development impact bonds

- 26** Does your jurisdiction regulate 'pay for success' investing models such as social impact bonds and development impact bonds? Apart from specific regulation, are any of these mechanisms in force or in progress in your jurisdiction?

There is no legislation, regulation or accepted or endorsed mechanisms regulating 'pay for success' investing models.

In 2019, the Western Cape provincial government Department of Social Development launched its Impact Bond Innovation Fund to drive Early Childhood Development targets in the Cape, acting as the 'outcomes funder' together with the private-sector ApexHi Charitable Trust. It is a social and developmental impact bond that was researched and brokered by the Bertha Centre for Social Innovation and Entrepreneurship at the University of Cape Town's Graduate School of Business, and its investors are the Standard Bank Tutuwa Community Foundation, Futuregrowth Asset Management and LGT Venture Philanthropy.

Crowdfunding

- 27** Does your jurisdiction regulate crowdfunding initiatives aimed at scaling up companies with social or environmental objectives?

Crowdfunding is not specifically regulated in South Africa, and therefore there are no specific initiatives in this regard. However, crowdfunding activities may be subject to existing regulation under South Africa's general financial services regulatory frameworks, so initiatives affecting the financial services sector generally – such as the Financial Sector Charter – could have application in specific circumstances. For example, the activities may fall within the ambit of:

- the Banks Act 1990 where activities could be seen as deposit-taking;
- the Companies Act, where the business in question is a company and the crowdfunding activities amount to offers to the public of securities;
- the Collective Investment Schemes Control Act, in respect of pooled investments;
- the Financial Advisory and Intermediary Services Act 2002, where the crowdfunding platform can be seen to provide an intermediary service or advice in relation to a financial instrument or product;
- the Financial Markets Act 2012 where the online platform can be seen to operate as an exchange, matching investors with issuers or product providers; and
- the National Credit Act 2005 where crowdfunding is based on a lending model.

As crowdfunding is not specifically provided for in tax legislation, it contains inherent risk of tax consequences such as donations tax (20 per cent).

UPDATE AND TRENDS

Update and trends

- 28** What are the key recent developments, hot topics and future trends in your jurisdiction relating to social finance, purpose-driven companies and the impact economy in general? Are there any recent studies and initiatives to identify or quantify these market sectors? Are there any new or proposed regulations or taxonomies in this regard?

The National Treasury recently published a draft technical paper: 'Financing a Sustainable Economy', compiled by the Sustainable Finance Working Group, which intends to act as a framework for financial

institutions to better disclose public information on their green practices and investments, and enable stakeholders to better understand the extent of the financial sector's vulnerability to environmental and social risks.

The draft paper's aims include, among other things:

- identifying gaps in the existing regulatory framework and recommend actions required of regulators, financial institutions and industry associations;
- identifying market barriers to sustainable finance and the implementation of environmental and social risk management best practices; and
- defining sustainable finance for all parts of the South African financial sector including banking, retirement funds, insurance, asset management and capital markets.

While there have been no developments that expressly deal with impact investment, in a recent discussion document between South Africa's ruling party and major labour unions there was a push for domestic pension funds to drive economic growth and caution against relying on financing from international financial institutions. Furthermore, it stated that measures taken to drive growth must include, 'among others, impact investments, interchangeably developmental and productive-asset investment requirements'.

Recommendations

29 | Do you have any recommendations for legal models, fiscal treatment and public procurement in your jurisdiction in relation to social finance and purpose-driven companies? Do you see a need for regulatory intervention or is the market capable of self-regulation in these sectors?

As a traditionally common law jurisdiction, perceptions of investment best practice are largely driven by fiduciary duties of professionals acting in audit or supervisory capacities or acting as delegates under client mandates. Accordingly, in the absence of explicit permission or compulsion for investing in a way that is not purely directed at traditional investment measurements, the rate of uptake of alternative investment objectives, targets and measurements has not proven to be significant. On the other hand, legislation and regulation that creates indirect financial incentive or market access, such as BEE laws, are more likely to prove effective.

In our view, products such as social or development impact bonds, in the form of public-private partnerships for service delivery, hold much potential; however, such structures require a higher degree of understanding and exposure by procuring national, provincial and municipal governments and agencies.

Reconsideration of the fiscal treatment of for-profit organisations with high social impact objectives and performance (ie, with measurement as proof of mission) may be a key requirement in our jurisdiction, as tax incentives are limited to quite narrow concepts of 'charity' and public benefit at present.

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