ANALYSIS OF CORPORATE FAILURES: A CASE STUDY OF TWO SOUTH AFRICAN BANKS

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DECLARATION

I, Xitshembiso Mqomboti declare that the work contained in this thesis is my work and none of it has been submitted to any tertiary institution for a degree.

Xitshembiso Mqomboti

February 2023

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ABSTRACT

This study analysed the factors that contributed to the failure of Venda Building Society Mutual Bank (VBS) and African Bank Limited and the impact it had on their key stakeholders. The specific objectives of this study were to evaluate African Bank and VBS bank's operational risk management processes and controls, the role of ethical failures at VBS bank and African Bank; and assess how the failures affected their stakeholders.

The population sample of the study included African Bank and VBS. The study adopted a qualitative research method. Existing reports from both African Bank and VBS were used to collect data. The study adopted a thematic data analysis method, which includes data coding and the development of themes. The data analysis framework was derived from a defined set of research propositions and seven (7) themes were derived from this analysis method.

The failure in operational controls of both banks and ineffective risk management structures including unethical conduct by the executive management and board of VBS bank, irregular financial transactions and weakened external auditing function resulted in an unaccountable executive relationship and reckless lending decision-making.

This research study will expand on the existing body of knowledge on the failures and near-failures of banks in the South African banking sector. The South African banking industry and its regulatory bodies will be better equipped to strengthen their corporate governance in risk controls to mitigate future collapses and near collapses of banks.

Keywords: corporate governance, operational risks, internal controls, ethics, three lines of defence, stakeholder inclusivity

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CHAPTER 1: INTRODUCTION AND OVERVIEW OF THE STUDY

1.1. Introduction

This chapter provides a brief background of the research study, the problem statement and the research goals. The chapter further discusses the research aims and objectives, the significance of the study and the outline of the chapters.

1.2. Background

While the profit generated is a measure of return on investment for the shareholders, various stakeholders need to be considered during this pursuit of revenue and profits (The Banking Association South Africa, 2017). Risk and controls together with good corporate governance should be maintained throughout the operations of the organisation (IoDSA, 2016). In the banking sector, the requirement for stringent risk control measures, good corporate governance and stakeholder transparency and inclusivity are non-negotiable as banking institutions are entrusted with the financial assets of various stakeholders (IoDSA, 2016).

1.3. Risk controls and corporate governance

According to Pyle (1999), the banking industry like any other industry is exposed to different types and levels of risks. Banks are expected to have measures in place to mitigate, control, transfer or eliminate the risk. Recently, internal risk controls have been extended to governance and ethics controls (Aloqab, Alobaidi and Raweh, 2018). To ensure the effectiveness of these controls, management and members of the respective boards of directors have legal and moral responsibilities to follow the rules and regulations of banking sectors in their respective countries to limit the possibility of business failure (Fassin and Gosselin, 2011). The King Code on corporate governance from its inception has grown into an accepted self-regulatory code of good corporate governance that applies to all industries. Its main focus is on how organisations should conduct themselves ethically and responsibly to serve the interests of all their stakeholders, including the practical implementation guidelines thereof (IoDSA, 2016).

The three lines of defence model is being adopted more as an operating model for managing operational risks in organisations. According to Luburic, Perovic, and Sekulovic (2017), the model entails three lines of defence that the bank must implement when managing its operational risks. This model enables organisations to identify structures and processes in place to achieve the organisation's objectives and facilitate strong governance and risk management (The Institute of Internal Auditors, 2020). The Basel Committee on Banking Supervision (BCBS) (2011) and the King Code reports highlight some fundamental principles of operational risk management that should be taken into consideration when managing banks' operational risks. These principles are essential tools for banks to consider and refer to when developing operational risk policies, processes, and risk management systems (BCBS, 2011).

The King Code on corporate governance and the three lines of defence are deemed effective, but the failure of implementation can result in corporate failures (Davies and Zhivistkaya, 2018; Mabwe et al, 2017; Wiwanto, 2020). The effectiveness of King code is highlighted by Dzingai and Fakoya (2017) in a research study that focused on Socially Responsible Investment (SRI) in the mines listed in the Johannesburg Stock Exchange (JSE). The cited study was focused on the effectiveness of an independent board (as recommended by King IV) on Return On Investment (ROI) performance. The study found that there was a positive corelation to the financial performance of the company (ROI) and an independent monitoring board.

Similarly, there is scholarly evidence of effective impact from the application of the three lines of defence on risk management and controls, which is covered under the Basel Accord. Bantleon,d"Arcy, Eulerinch, Hucke, Pedell and Ratzinger-Sakel (2021) in a study conducted across various government stakeholders in Australia, Germany and Switzerland found that communication and coordination at cross functional levels of an organisation eliminate working in silos and facilitate a culture of embracing a collaborative relationship with internal audit and risk compliance teams. This enabled effective risk management and control in the organisations studied in the cited study.

According to Piesse et al. (2006), corporate failures refer to bankruptcy, and corporates going through a fragile financial state. Piesse et al. (2006) describe some of the conditions that define corporate failure as the market value of the assets of the company being less than its total liabilities, the company being unable to pay its debts when due, and when the company continues trading under court protection. The impact of corporate failures varies from one sector to another. Bank failures can have devastating consequences on the economy due to the sizeable financial assets they look after (Havemann, 2019). The reasons for these failures are often complex in the banking sector due to the nature of transactions that take place; some contributing factors can be attributed to regulatory and funding issues, assets mismatch, as well as poor risk management decisions among other factors (Bommarito, 2012).

1.4. The South African banking industry

The banking sector in South Africa plays a significant role in developing the country's economy (The Banking Association South Africa, 2017). The banking institutions operate as a depository for individuals and institutions that wish to save their funds and receive accrued interest on their deposits (The Banking Association South Africa, 2017). Banking institutions operate as a bridge between individuals with funds to invest and those who require loans to support their financial needs (The Banking Association South Africa, 2017). In a country like South Africa where stokvels are used by poor communities as a saving vehicle, their existence is critical for the sustainability of such communities (Matuku and Kaseke, 2014). Furthermore, poor South African communities need to access unsecured loans due to their lack of assets required as security for financial lending in most banking institutions, hence the financial sustainability of unsecured lending institutions is critical to these communities (Pakgadi, 2016). These transactions play a critical role in growing a financially inclusive and stable economy of a country. The banking sector in South Africa is regarded as generally sound, stable, and resilient. It is governed by stringent regulations and supervision (SARB, 2018). However, the South African banking sector still experiences challenges.

1.5. Problem statement

Historically, South Africa has seen over 10 bank failures in the past 30 years (BusinessTech, 2018). The most recurring and prominent contributing factors to these failures are bad management and liquidity problems (BusinessTech, 2018). Even though the sector has seen few failures in the last decade, some failures are more recent. Examples of banks that have failed recently include New Republic Bank (2002), Saambou Bank (2002), African Bank Limited (2014), and Venda Building Society Mutual Bank (VBS) (2018) (BusinessTech, 2018). The research study analysed the two South African banks that failed recently.

African Bank Limited is an unsecured lending institution founded in 1975. The founding members of the bank chose an operating model that was focused on providing unsecured loans to the large unbanked population of South Africa, the bank has kept this operating model to date (African Bank, 2015). In 2014, the bank started experiencing financial challenges that led to the bank being placed under curatorship, in what was widely reported as a near failure (BusinessTech, 2018). The major contributing factors to this near failure were identified as poor management of bad debt around unsecured lending (BusinessTech, 2018).

VBS mutual bank was established in 1982 to service the poor communities who were using stokvels for generating financial savings and burial societies but were not welcome to bank these savings in the retail banks (VBS, 2016). Initially, the bank succeeded in achieving its objective but later deviated from this original objective and started engaging in a series of transactions contravening the mutual bank's regulations (BusinessTech, 2018). The bank used the municipalities as a vehicle to access and facilitate irregular transactions, thus contravening the Municipal Financial Management Act (Motau, 2018). The funds accumulated were reported to have financed the lavish lifestyles of the bank's executive management and some associated high-profile individuals (BusinessTech, 2018). Subsequently, the bank could not fulfil the withdrawal requirements of the rightful depositors, the stokvel groups and burial societies and later liquidated.

Due to the significance of this type of institution to the poor and largely unbanked communities of South Africa, its failures and near failures attracted a lot of interest from the banking industry and South African society.

1.6. Research aim

This research aimed to analyse some of the contributing factors to the failures of VBS and African Bank and the impact it had on their stakeholders.

1.7. Research objectives

The objectives of the research are to:

1. Evaluate African Bank and VBS Bank operational risk management processes and controls.
2. Evaluate the role of ethical failures at VBS and African Bank.
3. Assess how African Bank and VBS failures affected their stakeholders.

The period over which this is covered is from 2012 to 2014 for African Bank Limited and from 2014 to 2016 for VBS Mutual Bank.

1.8. Significance of the study

The literature describes different factors that contribute to corporate failures, including failures in the banking sector (Enoos, 2021) . However, there is limited research conducted on banking failures within the South African context. Thus, the significance of this study is to contribute to the existing body of knowledge and limited research in the context of South African Banking sector failures. This research will contribute to improving industry management practices by assisting with recommendations that can be implemented by management and industry practitioners in the banking sector to reduce the risks of future failures.

1.9. Chapter outline

This study comprises six chapters. Chapter one provided a brief introduction and background of the study. This chapter also gave an overview of the research aim and the research's objectives. Chapter two provides a more detailed discussion of the concepts defined in chapter one through a literature review. Chapter three describes the methodology utilised to undertake the study. Chapter four presents the findings of the study in line with the objectives. Chapter five discusses the findings from the data analysed. Lastly, chapter six concludes the study and give recommendations for management practice and further research.

CHAPTER 2: LITERATURE REVIEW

2.1. Introduction

The preceding chapter outlined the background of the study. It presented the problem statement, the objectives, and the methodology followed to gather information for this particular study. This study focused on two South African financial institutions, which were profiled in the previous chapter.

This chapter provides insights into stakeholder theory, which, is the underpinning theory of this particular study. The chapter outlines the application of stakeholder theory in the banking/ financial industry, touching on who the stakeholders are, stakeholder legitimacy, corporate governance, business ethics, and operational risk management, as well as the critique and limitations of the theory. The three lines of defence model and their applications are discussed in detail as financial institutions to mitigate and control operational risks in their business operations mainly use this model. The operational application of these concepts in the literature is also discussed in this chapter.

2.2. Stakeholder theory

Stakeholder theory focuses on ensuring that the business is aware of the impact on all its stakeholders and seeks to minimise it through the responsible and ethical manner in which it conducts its business (Freeman and Reed, 1983). The theory further emphasises the importance of businesses investing in relationships with their stakeholders, to create long-term value (Freeman, 2004). According to Freeman (2004), for organisations to truly succeed and be sustainable, businesses can no longer ignore their stakeholders as they play a role in the success of businesses. This means that without stakeholders' support, organisations might cease to exist in the long term.

Freeman and Reed (1983) argue that the purpose of the business is defined by its overall value creation for the business's stakeholders; this should be managed in the interest of all its stakeholders. Stakeholder theory further provides a basis in which to categorise the structural relationship framework between managers and different stakeholders into three pillars. The *normative pillar* indicates why organisations should consider their stakeholders, the *descriptive pillar* proves that businesses have stakeholders, and the *instrumental pillar* emphasises the fact that businesses that consider their stakeholders devise successful strategies (Freeman and Reed, 1983). Due to the scope and limitations of this study, the above-mentioned pillars will not be discussed further. However, Himaj (2014) highlights the importance of these pillars when dealing with banks as they are multi-constituency businesses due to their 'special' groups of stakeholders, such as bondholders, depositors, regulators, and other stakeholders.

Since its early formulation, the stakeholder theory has provided substantial attention and support to corporate governance, and it is used to address morals, ethics, and values whilst managing a business (Himaj, 2014). Stakeholder theory is a theory of organisational management and ethics. Freeman and Reed (1983) maintain that businesses and their managers will be better off if they not only consider the needs of the shareholders but also consider the needs of other groups who can affect or be affected by the achievement of the firm's objectives. The underpinning argument is that the business will enhance its ability to create value.

According to Freeman and Reed (1983, p.91), stakeholders can be defined as *"any identifiable group or individual who affects the achievement of an organisation's objectives or who is affected by the achievement of an organisation's objectives. It is a group or individual on which the organisation is dependent for its continued survival".* This definition supports Freeman and Reed's (1983) argument that there is a relationship between the business and its stakeholders; they cannot survive without each other.

Freeman and Reed (1983) identify stakeholders as public interest groups, protest groups, trade associations, unions, employees, customers, suppliers, government agencies, shareowners, financial institutions, and any other stakeholders. According to the Basel Commission (2015,) legitimate stakeholders in the banking industry are shareholders, depositors, market participants, and other stakeholders recognised by the industry. All these stakeholders exert pressure on the bank through their expectations and demands, and each one of these stakeholders has a different stake and power rank, and level of pressure on the bank.

2.3. Stakeholder legitimacy

Parmar, Freeman, Harrison, Wicks, Colle, and Purnell (2010) highlight the importance of identifying legitimate stakeholders that the business and its managers should focus on. In essence Parmar et al. (2010) further affirm the argument that stakeholder theory does not assume that all groups that claim to be stakeholders of a particular business should be considered. Phillips (2003) mentions two types of legitimate stakeholders the business should focus on, which are normative and derivative stakeholders. These two types of legitimate stakeholders are discussed below.

Normative legitimate stakeholders refer to the stakeholders whom the organisation holds a moral obligation of acting fairly, thus the moral commitment of an organisation is the primary driver of engagement with this particular stakeholder. Freeman, Wicks, and Parmar (2004) refer to these stakeholders as internal stakeholders or the inner circle; these stakeholders include employees, customers, investors, suppliers, governments as well as trade associations among other groups that define the organisation's business operations. Managers should pay attention to these key stakeholder relationships based on moral commitments rather than on using stakeholders to solely maximise profit. Based on this statement, it can be argued that moral obligations must be central to the organisation and the strategies that it uses.

Derivative legitimate stakeholders refer to all the groups whose claims and actions are accounted for by managers, as failure to do so will result in these stakeholders negatively affecting the well-being of an organisation and its normative stakeholders. Freeman, Wicks, and Parmar (2004) refer to these stakeholders as the external stakeholders or the outer ring. These include competitors, special interest groups, and the media. These stakeholders can affect or be affected by the organisation's business operations or influence the existing relationship between the organisation and its key stakeholders. For example, favourable or unfavourable news coverage of an organisation by the media can affect its reputation among informal stakeholders.

2.4. Corporate governance

2.4.1. Corporate governance defined

Corporate governance is defined as a system of checks and balances that ensures that firms discharge their accountability to all their stakeholders and act in a socially responsible way while conducting their business activities (Sison, 2010). Moreover, corporate governance may be considered as a web of relationships that is not only between the firm and its shareholders but also between the firm and its various stakeholders (Ţurlea, Mocanu and Radu, 2018). According to Hopt (2021, p.22), *"the primary objective of corporate governance should be safeguarding stakeholder's interests in conformity with public interest on a sustainable basis".* Concerning retail banking, it can be argued that shareholders' interest would be secondary to depositors' interest (Basel Commission, 2015). Furthermore, according to Basel Commission (2015), the supervisory board should ensure that the interest of depositors is protected and consider that the interest of legitimate and other relevant stakeholders are met. Based on these statements, it can be argued that corporate governance plays a critical role in holding the firm's leaders accountable to its stakeholders as business leaders are trusted to safeguard the interests of these stakeholders.

Parmar et al. (2010) present corporate governance as one of the areas that is growing under stakeholder theory. This pertains to the fiduciary duties of board members/directors as custodians of the business who must oversee the interest of the shareholders and all the other stakeholders of the business.

2.4.2. King Code Reports

One of the widely used and respected blueprint documents for stakeholder theory and corporate governance that provides guidelines for practical application is the King Code Report on corporate governance (IoDSA, 2016). According to the Institute of Directors Southern Africa (IoDSA) (2016), stakeholder inclusivity and corporate governance emphasise the interdependent relationship between the organisation and its stakeholders. The ability of an organisation to create shared value and be attuned to the challenges and opportunities that the business and its stakeholders are exposed to, whilst seeking to meet reasonable and legitimate needs, interests and expectations of material stakeholders. Corporate citizenship states that organisations form an integral part of society, and thus hold responsibilities and obligations towards society and the natural environment in which the business operates.

The preceding King Code III and King Code IV reports both emphasise the stakeholder inclusive approach and corporate citizenship (IoDSA, 2016). The King III report is mainly based on an inclusive stakeholder approach and integrated reporting (IoDSA, 2016). Integrated reports provide a holistic view of the organisation's performance in terms of both finance and sustainability. IoDSA (2016) emphasises that by issuing integrated reports, an organisation can increase the trust and confidence of its shareholders, increase the legitimacy of its business operation and business opportunities as well as improve the organisation's risk management processes.

King Code IV's report further extends corporate citizenship to the expectation that the business must carry out its activities in an ethical manner. This is essentially about ethical leadership which finds its expression through the governing body setting an appropriate example and tone of ethical governance by implementing appropriate policies and practices (IoDSA, 2016).

Therefore, based on these arguments it appears that there is an intertwined relationship between business and stakeholders. Because of this interdependent relationship, business organisation activities and decisions will always come under scrutiny and are evaluated against societal expectations. Corporate governance seeks to facilitate this creation of 'shared value' for both the shareholders of the business and its various stakeholders.

Banks represent the main source of external finance for various businesses, they play a major role in capital allocation, creating liquidity, and influencing the money supply of an economy, banks have a higher risk of fraud and self-dealing transactions compared to other firms that are considered non-financial entities (Ţurlea, Mocanu and Radu, 2018). Duties imposed on banks are much stricter, more detailed, and mandatory compared to those of other corporations. Therefore, banks' corporate governance is an ongoing task for regulators, supervisors, and legislators, most importantly for the banks themselves. Highlighting this point of view, Hopt (2021) emphasises the fact that ethics are indispensable in banking, therefore, the tone from the top matters.

2.5. Business ethics

According to Ogbo, Okechukwu and Ukpere (2013), business ethics is concerned with issues of exploring moral principles which can be used to evaluate business organisations regarding their impact on people and the environment. Additionally, business ethics is about taking meaningful actions and commitments to raise ethical standards, rather than global conventions and making statements that support business ethics (Ogbo, Okechukwu and Ukpere, 2013). The focal point of the above arguments is that businesses are expected to take a genuine interest backed by practical actions in ethically pursuing their objectives.

Every organisation has an ethical responsibility, its record and perception of its ethics can affect the reputation of the organisation which will determine the long-term success or failure of that organisation (Green, 1989). A good reputation ensures long-term success, which at times can be attributed to an organisation’s good strategy and prudent management. However, no business survives for a long time with a record of cheating, defrauding, and exploitation (Green, 1989). Similarly having a strong sense of ethics does not guarantee that an organisation will always do the right thing. According to Khang (2005), the key component to achieving the best ethical organisations is leadership that is visible through its actions and commitment to ethical practices, as well as setting the moral tone from the top and translates ethical principles into behaviour that is expected from every person acting on behalf of the organisation. Based on these statements, ethical leadership plays a role in achieving a firm’s good reputation by setting a tone that translates ethical principles to all members of the organisation.

According to Green (1989), the role of a banker is one of stewardship that is based on trust. Therefore, banks are trusted by those that ask the banks to look after their money, as well as the duty to lend money responsibly (Green, 1989). However, the financial industry, in general, is often exposed to moral dangers that do not exist in non-financial industries. Green (1989) further argues that money has a mystical attraction, so it is hardly surprising that those who work in the financial industry may be much more vulnerable to the temptation of what money can provide. Consequently, internal control measures should be put in place to ensure that unethical business practices are reduced even if they cannot be eliminated.

The employees in any firm are a collective body who reflect on the business's ethical stance, (Green,1989). Therefore, the employees must know what principles guide their conduct for them to reflect the ethical stand of an organisation. Other businesses use mission statements as a way of communicating what is expected from the employees, and what values and ethics the organisation stands for. However, Sullivan (2009) argues that business ethics not only attempt to set standards in which the staff can know what to expect, but, it is an attempt to encourage the managers, board members, and employees to think about and make decisions through the prism of a shared set of values.

As the world moves more to the technological era and changes how financial transactions are made across the world, there is a potential for greater abuse (Green, 1989). Computers may not have morals, but the human beings who operate these computers should have morals. Therefore, bankers should avoid the danger that the rules of conduct, as well as the business ethics, could be eroded in the tide of competition, and pressures of meeting targets that could lead people into unethical practices (Green, 1989). Based on the above arguments, it can be stated that business ethics should be the cornerstone of every decision and activity in an organisation, regardless of the type of transaction, potential benefits, and level of technological intervention.

2.6. Risk management: operational risk

Operational risks refer to the exposure of an organisation to potential losses that might arise because of inadequacies or failures in the execution of the organisation's operations (Young, 2010). These losses may be caused by internal or external failures. Therefore, to address these risk factors, it is important that the organisation analyses the cause of the risk exposure, develop and implement mitigation and control measures (Young, 2010).

According to Young (2010), four pillars can be used by organisations as control measures for operational risks; these pillars are a requirement for good corporate governance. *Structure:* the organisational structure ensures that specific roles and responsibilities are allocated for effective operational risk management. *Policies and procedures* are important for risk management to provide consistency and discipline within an organisation and ensure the overall definition and allocation of specific roles and responsibilities for managing risks. *Internal controls*: should be established to ensure the effectiveness of policies and procedures. *Risk reporting*: this is where an organisation reports on risk internally through its management information systems, and externally to its shareholders and stakeholders. Therefore, these pillars form the basis for control measures that organisations can use to control and mitigate operational risks. This will further assist organisations to make decisions that are in line with the requirements of corporate governance and shared value.

Young (2010) highlights that corporate governance and operational risk management disciplines are being adopted by many countries, including South Africa. These disciplines are starting to claim their rightful place as critical determinants in any organisation's management structure. As such, in South Africa, an initiative to develop a corporate governance framework for risk management was launched in the form of the King Code of corporate governance as discussed in the previous section. The King Code report's main objective was to promote the highest standards of corporate governance in the country, by initiating and developing a corporate governance framework for risk management that promotes these standards (IoDSA 2016). According to IoDSA (2016), this risk framework must give assurance as part of the organisation's corporate governance regarding issues such as (i) business sustainability, (ii) effectiveness and efficiency in operations, (iii) safeguarding assets, (iv) compliance with applicable law, (v) behaving responsibly towards stakeholders, and (vi) reliability of reporting.

Concerning risk management, the King Code reports outline some of the responsibilities that should be undertaken by the board members of the organisation. These include: (i) disclosing risk management in the annual reports, (ii) ensuring that processes and outcomes of key risk indicators are undertaken annually, (iii) ensuring that the internal audit function provides an independent assurance that the internal controls ensure effective risk management, (iv) ensuring compliance with applicable regulations, and (v) appoint a board committee or a dedicated committee that should review the risk management process and significant risks facing the organisation (IoDSA, 2016).

Based on the above-mentioned responsibilities of ensuring effective risk management in line with the requirements of good corporate governance, it can be argued that there is a relationship between effective risk management and the components of good governance that should be applied in organisations, including banks. Young (2006, p.6) further emphasises the direct link between components of corporate governance and risk management, stating, *"if organisations like banks can assure compliance with good corporate governance requirements, it would most likely attract the attention of potential investors".* Therefore, organisations including banks must establish a solid commitment to good corporate governance and risk management practices to ensure transparency, thus leading to the protection of the interests of the firm's stakeholders.

2.7. The application of stakeholder theory

While the importance of stakeholder theory and its effectiveness in ensuring that the business does not negatively affect its stakeholders and vice versa cannot be disputed, businesses are not negatively affected by neglecting their stakeholders. Stakeholder theory is critiqued on its relevance and application (Key, 1999; Maharaj, 2008; Mansell, 2013). Although Key (1999) acknowledges that stakeholder theory's presentation of identifiable actors provides valuable strategic tools to management, the theory does not offer enough theoretical basis for explaining firm behaviour and that of the individual actors. Key (1999) further presented four ways in which the stakeholder theory can be criticised which include: (i) *inadequate explanation of the process*, (ii) *incomplete linkage of internal and external variables,* (iii) *insufficient attention to the system within which business operates and levels of analysis within the system*, and (iv) *inadequate environmental assessment*.

The above-mentioned critical observation of the stakeholder theory is acknowledged. However, there is substantial literature that supports the validity and effectiveness of the stakeholder theory in providing the value sought by stakeholders and business ethics (Al-Shamali, Sharif, and Irani, 2013; Harrison and Wicks, 2013; Harrison, Freeman, and Cavalcanti Sá de Abreu, 2015). Harrison, Freeman, and Cavalcanti Sá de Abreu (2015) conducted a study on stakeholder theory as an ethical approach to effective management: applying the theory to multiple contexts. The authors found that the stakeholder theory offers opportunities to interpret a wide range of concepts, phenomena, and models across different disciplines (Harrison, Freeman, and Cavalcanti Sá de Abreu, 2015). Therefore, based on the discussions made in the sections above of this paper and the conclusions of the cited studies, the stakeholder theory applies to this particular study.

2.8. Application of operational risks and stakeholder theory in the financial sector

This section of the literature review highlights the applications of stakeholder theory to operational risk management in the banking sector. Furthermore, the importance of corporate governance and stakeholders' interest in financial institutions are outlined.

Grais and Pellegrini (2006) conducted a study that focused on corporate governance arrangements aimed at protecting stakeholders' financial interests as it is applied in Islamic financial services. The study emphasised the importance and ability of good corporate governance to protect the interest of the business's stakeholders which goes beyond financial interest to include ethics and compliance with the laws (Grais and Pellegrini, 2006). According to Grais and Pellegrini (2006), Islamic institutions are generally less transparent in their financial dealings compared to their counterparts. Therefore, Islamic financial institutions must create a culture of transparency to protect all their investors, and information dissemination should provide equal, timely, and cost-effective access to all relevant users (Grais and Pellegrini, 2006). It is essential to create a corporate structure that will enable these financial institutions to implement good governance through Islamic law operations for the stability and efficiency of Islamic financial services. The research study cited above concluded that the introduction of corporate governance structures, as well as reinforcing the existing ones provided stakeholders with sufficient comfort in the actions taken by management and other organs of financial institutions (Grais and Pellegrini, 2006).

Barakat and Hussainey (2013) conducted a study that provides details on bank governance, regulation, supervision, and risk reporting: evidence from operational risk disclosures in European banks. In this study, the authors investigated the direct and joint effects of bank governance, regulation, and supervision on risk reporting quality in the banking industry. Barakat and Hussainey (2013) highlighted that theories such as agency, legitimacy, and stakeholder suggest that strict supervision, heavy regulation, and bank-level governance structures can shape the bank management's discretionary decision to report risk information. The authors further argued that the disclosures on operational risk exposure and management thereof present a unique opportunity to consistently evaluate the discretionary decision to provide risk disclosures of a certain quality by bank management (Barakat and Hussainey, 2013). The cited study concluded that evidence was found that banks with a higher proportion of outside board directors, lower executive ownership, non-government ownership; and more active audit committees provided their stakeholders with higher-quality operations risk disclosure. It can be observed from this study that good corporate governance is important to ensure transparency, consequently leading to the protection of the interests of the stakeholders.

It is clear from the above sections that financial institutions have to find suitable risk management models to mitigate and manage risks. This is crucial in managing operational risks that negatively affect stakeholders and risk damaging the much-needed interdependent relationship. However, there are various models available for financial institutions that can be used to mitigate and manage operational risks in financial institutions.

2.9. Framework for operational risks

2.9.1. Three lines of defence

The three lines of defence model is a framework that has been adopted in various business sectors to address operational risks (Luburić, 2017). In the financial sector, the model has been standardised as a model that can be used to prevent risks and manage uncertainty (Doughty, 2011). According to the Institute of Internal Auditors (IIA) (2013, p.2), the model *"provides a simple and effective way to enhance communications on risk management and control by clarifying essential roles and duties".* The model can be used in any organisation of different sizes and complexity to address how specific duties that relate to risks and control can be coordinated and assigned within the organisation (Anderson and Eubanks, 2013). The three lines of defence model is depicted in figure 1 below.

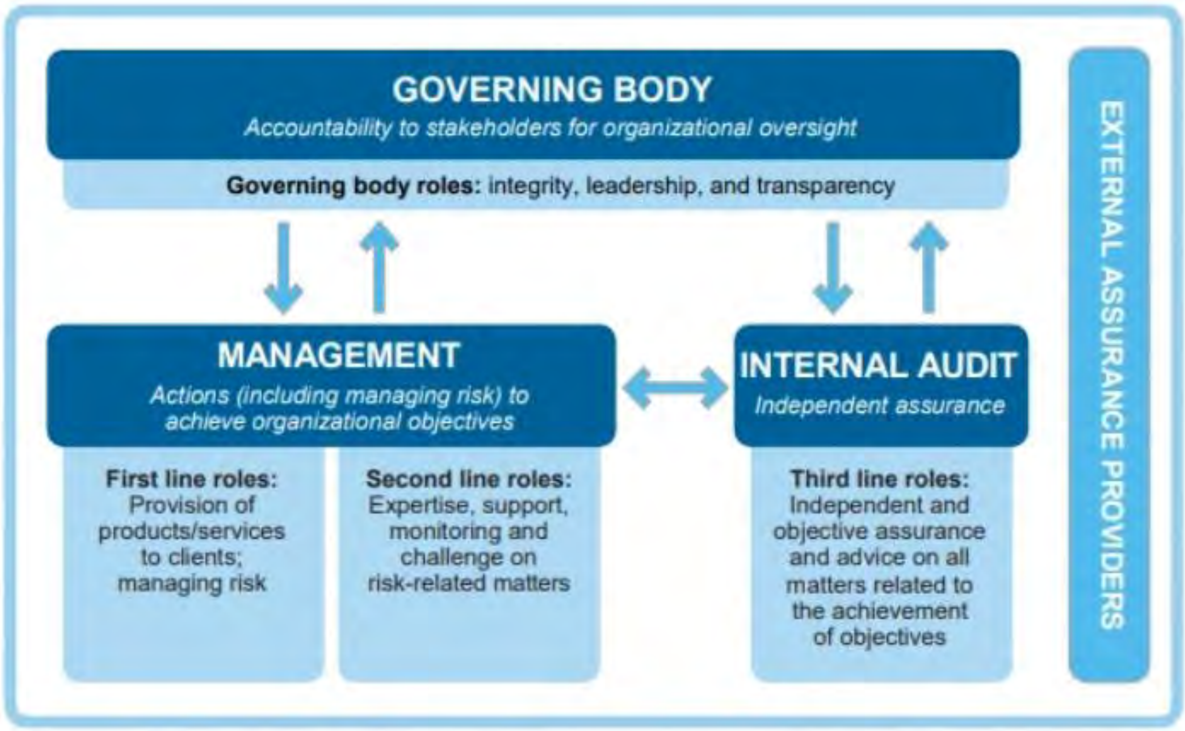

Figure 1. The Three Lines of Defence Model (Anderson and Eubanks, 2013)

Furthermore, the model offers clarity on the different relationships between the organisation's assurance and other monitoring activities which can be misunderstood if not clearly defined (Anderson and Eubanks, 2013). It appears that the three lines of defence is a framework that has been accepted in the financial sector as an effective tool for operational risk management (Anderson and Eubanks, 2013). Therefore, it is important to unpack the three lines of defence in more detail to understand how it works and the value that it adds to operational risk management in financial institutions.

Table 1 below outlines the roles and responsibilities of each line of defence for effective management and risk control within the organisation (Anderson and Eubanks, 2013). According to Luburić (2017), the first line of defence consists of business line managers who are also referred to as risk owners. Their role is to identify risks and execute actions to manage and treat these risks. The second line of defence consists of professionals whose responsibility is to identify risks, establish, and develop risk management frameworks. The third line of defence is an internal audit function that provides independent assurance regarding the management of the risk and control. The main responsibilities of these three lines are outlined in Table 1 as follows:

Table 1. Three lines of defence responsibilities

First Line (Operational Management)	Second Line (Risk Management)	Third Line (Internal Audit)
- Identifies, assesses, and manages the risks on daily basis. - Develops and implements risk management policies and procedures. This line is expected to be fully aware of the risk factors that should be considered in every decision and action. - Maintaining and executing effective internal control in the business units, as well as implementing risk and control procedures daily. - Manage risk/implement actions to manage and treat risk. - Perform corrective actions to address process and control deficiency. - Perform adequate management and supervisory controls that ensure compliance and highlight inadequate process and control breakdown and any unexpected events. - Execute risk assessments and identify emerging risks.	- Risk management development, monitoring process, and implementation of overall risk management. - Monitor and ensure that all business functions being implemented are following risk management policies and standard operating procedures established by the organisation. - Monitor and report to departments with the highest accountability on complete organisation's exposure to risks. - Provide training and guidance on risk management processes. - Provide a strategic link for the enterprise in terms of risk. - Provide guidance and coordination among all constituencies. - Risk reporting to the management. - Provide oversight on certain risk areas e.g. credit risk.	- Review and evaluate the design and implementation of risk management holistically. - Ensure the effectiveness of the first and second layers of defence - Liaise with senior management and board. - Rationalise and synthesize risk management processes followed by the second line of defence. - Assure that risk management processes are equated and appropriate.

Source: (IIA, 2013)

The governing body, which includes the board of directors and the executive management team, sits above the three lines of defence. The governing body provides oversight and is responsible for risk management strategies that inform the three lines of defence activities and controls. According to Nalukenge, Nkundabanyanga, and Ntayi (2018), the governing body plays a critical role in enabling a culture that leads to successful risk management.

2.9.2. Critique of the three lines of defence

Despite the three lines of defence model being considered to be useful in providing a simple guide to monitor the effectiveness of risk management in organisations while permitting businesses to own their risk, the model still has critics (Davies and Zhivistkaya, 2018; Mabwe et al, 2017; Wiwanto, 2020). Wiwanto (2020) presented a critique of the three lines of defence and discussed some of the weaknesses in the model as providing *(1) unclear roles and responsibilities*: the organisation's adopted principles in implementing the model do not flow down into a detailed job description that everyone across the three lines understands. This then creates confusion and dilutes individual accountability thereby leading to a false sense of security. (*2) Lack of knowledge and motivation at the first line*: An insufficient emphasis is placed on the first line's responsibilities in managing the risks and in implementing the corrective actions whereas all lines have an equal share in the organisation's fate. *(3) Natural conflict between the first and second line*: this conflict lies in the natural order that the first line of defence will always want to take more risks, whereas the second line of defence always wants to keep the risks below the perceived threshold of tolerance.

The above-mentioned critical observation of the three lines of defence model is acknowledged. However, there is substantial literature that supports the validity and effectiveness of the three lines of defence model in organisations and financial institutions, respectively (Ribaj and Bejtja, 2016; Hakim, 2017; and Skoczylas-Tworek, 2019) on the three lines of defence model and banks found that the three lines of defence clarify roles and responsibilities and improves the effectiveness of risk management. Therefore, there is sufficient evidence indicating that the three lines of defence model is applicable for the effective management of operational risks in the banking sector.

Notwithstanding the critique from the literature on the three lines of defence, there are areas where the model has been applied successfully within the banking sector.

2.9.3. Application of the three lines of defence

The above sections discussed the three lines of defence model in detail; this section highlights the applications of the three lines of defence model in the banking sector. Lastly, the importance and effectiveness of the model in different financial institutions is outlined.

The three lines of defence is a framework that has been accepted in the financial sector as an effective tool for operational risk management. This model provides structure around risk management and internal controls within an organisation by defining different roles and responsibilities within the business (De, 2013). Lack of internal control systems and defective operations may cause companies that are vulnerable to operational risks to experience negative financial performance and competitiveness of the business (Mihaela and Iulian, 2012).

Mihaela and Iulian (2012) describe internal control systems as representing all the approved policies, processes, and systems that are used by management for both the first and second line of defence to achieve effective management of a business and associated risk. Auditors provide a warranty to reduce risks of distortions within the business, to establish confidence within the market and to protect investors. These policies, processes, and systems must remain sufficiently robust given that operational risk management evolves, and the business environment constantly changes.

Ribaj and Bejtja (2016) conducted a study that explains the three lines of defence model and banks in Albania highlighting the main challenges faced by the organisation. Among the challenges Ribaj and Bejtja (2016) identified is to ensure that the perceptions, contributions, and expectations of the executive management, audit committee, and the board of directors of the bank are aligned and information related to risk management is symmetric, effectively, and consistently obtained for use and analysis by internal control system personnel. The new regulation was passed in Albania to set an effective internal control system using the three lines of defence model. The objective was to assist banks to develop sound and reliable control systems and ensure the effective functioning of business operations that can contain the risks. The study concluded that in the three lines of defence model, the management of risk is much stronger when there are three clear and separate identified lines of defence where each line has a unique positioning and responsibilities and is coordinated in a way that does not compromise their effectiveness. Ribaj and Bejtja (2016) further recommend that the three lines of defence model must be functional in all Albania banks regardless of their complexity and size. Therefore, based on the conclusion of the above-mentioned study, the model can be adopted to reinforce the effectiveness of operational risk management functions in financial institutions.

Similarly, in the South African context, ABSA bank is the first of the major banks (FNB, Standard Bank, Nedbank and Capitec) to report on its application of the three lines of defence model. ABSA bank in its 2018 Risk management report provided an overview of the application of the organisation's three-line of defence model with clear accountability for managing, overseeing, and independently assuring risks (ABSA, 2018). The bank applies three lines of defence model in its operations to govern risks that might arise across all business functions and to ensure that the appropriate responses are in place to protect the bank as well as its stakeholders (ABSA, 2018). ABSA’s first line develops and implements standards and procedures as well as proposes and agrees on risk appetite and supporting limits with the second line of defence. The second line provides an independent review and challenges the business unit's risk appetite, underlying limits, and profiles; while also serving as a centre of excellence for specified risk types. Lastly, the third line provides independent assurance to the board of directors and executive management over the effectiveness of governance, and risk management control over current, systematic, and evolving risks through its internal audit.

This confirms how local financial institutions effectively apply the three lines of defence to manage the risks and protect the stakeholders from loss. It can be argued based on the above studies that the adoption of the three lines of defence in operational risk management for this particular study is consistent with existing literature on risk management and supported by effective risk management results observed in institutions that have adopted it.

2.9.4. Basel accord and King Code reports

The Basel Committee on Banking Supervision (BCBS) (2011) and the King Code reports highlight some fundamental principles of operational risk management that should be taken into consideration when managing banks' operational risks. These principles are essential tools for banks to consider and refer to when developing operational risk policies, processes, and risk management systems (BCBS, 2011). Similarly, Anderson and Eubanks (2013) identified five (5) components of internal controls that an organisation can adopt for operational risk management. When these components and principles are integrated into the overall operational risk management framework across the organisation, operational risk culture is established which further enables the organisation to enhance its ability to achieve its business objectives and improve business practices and processes (Maré, 2019).

The Basel principles of the sound management of operational risk (BCBS, 2011) and King code IV’s principles are outlined in this paper’s annexures 1 and 2. This paper focused on only the principles applicable to the operational risk controls demonstrated in the effective control systems components detailed below. According to Anderson and Eubanks (2013), effective control systems should consist of the following five components.

(i) A control environment

This component reflects the board of directors and management's commitment to internal controls. According to BCBS (2011), the board of directors is responsible for managing the company by ensuring that a prudent risk management framework is in place and providing oversight of risk management responsibilities that must be carried out by the company's executive management. Therefore, the board of directors and senior management should lead in establishing strong and sound risk management culture, and prudent corporate culture that is guided by strong risk management throughout the organisation. Establishing policies such as ethics policy and code of conduct that sets clear expectations of ethical values and integrity will ensure that the employees understand their roles and responsibilities and their authority to act when risks occur (BCBS, 2011). Similarly, principle 2 of the King code IV outlines the need for the governing body to govern organisational ethics in a way that supports the establishment of ethical culture (IoDSA, 2016).

According to BCBS (2011, p.6), *"senior management should develop for approval by the board of directors clear, effective and robust governance structures with well defined, transparent and consistent lines of responsibility".* This translates to senior management being able to assign responsibilities, authority, and reporting relationships that encourage and maintains accountability by both management and staff. Furthermore, senior management should ensure that the processes of management oversight are appropriate for the inherent risks. Hakim (2017) suggests that it is essential to establish committees such as audit, risk monitoring, and compliance committees that can assist in fulfilling corporate governance and oversight responsibilities, failure to do so could result in significant overlaps and gaps in the overall risk management processes.

Based on the above statements, management should create an environment that is conducive to controlling and managing risks throughout the organisation. This is emphasised in principle 11 of King code IV's on corporate governance, which indicates the need for the governing body to govern risk in a way that supports the organisation in setting and achieving its strategic objectives (IoDSA, 2016).

(ii) Risk assessment

This component involves the identification, measurement, and analysis of risks that may arise because of the controllable/uncontrollable, internal or external business of the organisation (Anderson and Eubanks, 2013). Therefore, there is a need for management to assess all risks faced by the organisation as uncontrolled risks can jeopardise business operations and prevent the organisation from achieving its objectives. Additionally, Anderson and Eubanks (2013) highlight that an effective risk assessment process assists the organisation to determine the potential risks, controls needed, and how the risk should be managed before it can negatively affect the organisation's operation. According to King code IV principle 5, these risk assessments are made possible by sound and comprehensive reporting that enables the various stakeholders to assess the business performance in all its key performance indicators. Risk is one of the key performance indicators of an organisation and based on this King code IV principle, it will be possible to assess the risk from the reports.

(iii) Control activities

One of the principles in the BCBS (2011) focuses on the need for banks to have a strong control environment that utilises practices, policies, and procedures as well as appropriate internal controls and risk mitigation strategies that assist the organisation's personnel in carrying out the board and management's directives. These controls are needed to provide reasonable assurance that ensures the banks have efficient and effective operations, reliable financial reports, and compliance with applicable regulations and laws governing them.

For these controls to be successful, proper segregation of duties and dual controls should be put in place to avoid conflicting duties for individuals or teams that may enable the concealment of errors and losses and other inappropriate actions (BCBS, 2011). Consequently, areas that present a potential conflict of interest should be identified and subjected to independent monitoring and reviews. Consistent with principle 8 of King code IV, the governing body needs to ensure arrangements of delegation within organisational structures and promote independent judgment and effective discharge of duties (IoDSA, 2016).

(iv) Information and communication

Internal communication must capture and convey relevant and timely information in a way that will enable the board and management as well as employees to perform their responsibilities (Anderson and Eubanks, 2013). Adequate information and communication enable the employees to understand their roles in the broader risk control system and how these roles relate to others and their accountability to the organisation. Furthermore, according to BCBS (2011, p.18) principles, *"a bank's public disclosures allow stakeholders to assess its approach to operational risk management"*. This component focuses on the need for the bank to disclose its operational risk management in a way that allows the bank's stakeholders to establish if the bank effectively identifies, assesses, monitors, and controls operational risks.

Consistent with the Basel principle for sound management of operational risk, King code IV highlights two aspects that can assist organisations to improve risk management processes. These include an inclusive stakeholder approach and integrated reporting (IoDSA, 2016). The inclusive stakeholder approach ensures that the interest and expectations of stakeholders are considered while decisions are taken in the best interest of the organisation. The issuing of integrated reports that holistically indicate the organisation's performance in terms of both finance and sustainability will further increase the trust and confidence of shareholders, enhance the legitimacy of the business's operation and increase business opportunities and improve risk management processes (IoDSA, 2016).

(v) Monitoring and assurance

Monitoring includes the need to carry out internal audits and continuous activities that ensure effective corporate governance, risk management, and compliance (Anderson and Eubanks, 2013). Monitoring further assists internal auditors to review the effectiveness of internal controls and report to management with suitable recommendations where necessary.

King code IV's principle 15 charges the governing body to ensure that assurance functions and services enable an effective control environment and support the integrity of information for internal decision-making and external reporting (IoDSA, 2016). The governing body should assume this responsibility by setting clear direction regarding the arrangements for assurance functions, and the internal audit structures needed to provide objective and relevant assurance that will contribute to the effectiveness of risk management and control processes as well as good governance (IoDSA, 2016).

Based on the above-mentioned components, it is clear that the management and governance of risk processes are considered the responsibility of the board and senior management. Therefore, it is important that the governing body set, review and approve the risk appetite and tolerance for operation risks, which articulates the types, nature, and levels of risk the organisation is willing to accept. BCBS (2011) highlights the incorporation of strong risk management with effective governance structures as the best practices that banks can adopt.

2.10. Conceptual framework

The conceptual framework as outlined in figure 2 below illustrates different variables derived from the literature that guided the data collection and analysis of this study. It further maps out how these different variables relate to each other and provides a visual representation and the expected relationship between these specific variables.

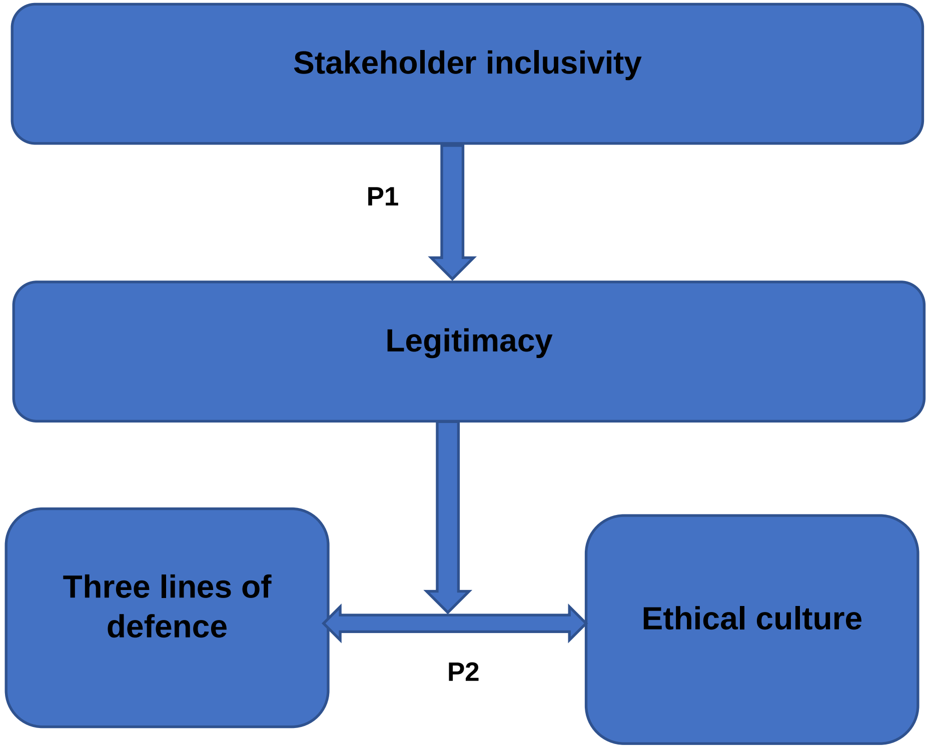

Figure 2. Conceptual framework

2.10.1. Propositions

Based on the above literature review, the conceptual framework is designed as presented in Figure 2 above. From this conceptual framework, two propositions have been developed to support the research problem and to guide data analysis that will lead to addressing the research problem.

P1. The governing body should adopt a stakeholder-inclusive approach that balances stakeholder needs, interests, and expectations as well as the best interest of the organisation over time. This entails an organisation's effective consultation with its key stakeholders during decision-making and communicating the decisions taken. They take into consideration stakeholders' interests and expectations, as well as the impact that it has on both the organisation and stakeholders. Subsequently, this affects the overall impact on the sustainability of the organisation.

P2. An effective governing body governs organisational ethics in a way that supports the establishment of ethical culture in the bank, and develops effective, well-defined, transparent, and consistent lines of responsibility that encourage and maintain accountability by management and staff. The expectation is for the organisation to demonstrate ethical leadership guidance through effective ethical leadership structures, adhering to the King Code of corporate governance, establishing an ethical code of conduct and applying decisive consequence management for unethical conduct and wrongdoing at all levels of the organisation. Ultimately, the ethical environment in the organisation will set the tone for its employees and management conduct which has a direct impact on its performance.

2.11. Conclusion

The literature review chapter discussed the stakeholder theory and its application in operational risk management in financial institutions. The stakeholder theory as the underpinning theory of this study provided insights about who the stakeholders are, stakeholder legitimacy, corporate governance, and business ethics as well as the respective critical arguments of its limitations. The three lines of defence model was discussed in detail as the model that is used by financial institutions to mitigate and control operational risk in their business operation. The purpose of discussing the three lines of defence model was to emphasise the importance of applying the three lines of defence model and highlighting its effectiveness in different financial institutions. Additionally, the model was used in the next chapters to assess the internal controls and corporate governance of both VBS mutual bank and African bank before their collapse.

According to the above literature review, operational risk management appears to be the main challenge affecting the banking industry, thus affecting the stakeholders in one way or another. Therefore, based on the literature reviewed it is important to analyse the contributing factors to the failures of the two South African banks and the impact it had on their key stakeholders.

CHAPTER 3: METHODOLOGY

3.1. Introduction

This chapter discusses the methodology that was adopted in this research study. It outlines how the research was conducted and describes the research methods and research techniques adopted to address the problem statement and the objectives of the study. Lastly, the outline relating to ethical consideration is provided.

This research study is located within the post-positivism paradigm. A deductive research approach and pattern matching were adopted for this research study guided by the set-out research propositions. A mono-method approach complemented by some quantitative analysis was possible using a descriptive case study method with two subjects on a longitudinal basis.

3.2. Research design

According to Saunders, Lewis, and Thornhill (2019), a research design is a general plan of how the research questions of the study will be answered, the sources specified from which the data will be collected, how data will be collected and analysed; and outlines ethical considerations and limitations. This particular study was guided by this method of research design.

3.2.1. Research paradigm

The research paradigm is defined as, *"the abstract beliefs and principles that shape how a researcher sees the world, and how the researcher interprets and acts within that world. It is a lens through which a researcher looks at the world"* (Kivunja and Kuyini, 2017. p.26). This particular study adopted a post-positivism paradigm. According to Creswell (2013), post-positivism holds firmly to a deterministic philosophy where causes determine outcomes, this reflects the need to identify and assess the causes that influence the outcomes. Therefore, this paradigm is an applicable research philosophy for this study as the research will be analysing hard and behavioural data, which involves the organisation's information on operational performance and implementation effectiveness, including the ethical culture and demonstrated conduct of management and staff.

3.2.2. Research methods

The research followed a qualitative data analysis method using a case study research approach. According to Yin (1981, p.59), this research method is better suited for this type of research study as it is a method that attempts to analyse *"a contemporary phenomenon in its real-life context, especially when the boundaries between phenomenon and context are not evident".* Yin (1981) further explains that a case study research method investigates a phenomenon within its real-life context. In this case, the research study lands itself within the descriptive case study research. According to Kumar (2011) descriptive research attempts to describe a situation or phenomenon and offer a precise and comprehensive description of that phenomenon. This is what this research seeks to achieve, therefore the case study method is applied to this particular study.

3.2.3. Multiple case study design

The two banks that were analysed were chosen as a dual multiple case design. This research approach explores real-life multiple bonded systems through in-depth and detailed data collection that involves multiple sources of information (Creswell, 2013). Using a multiple case design enables the researcher to understand the differences and similarities of the phenomenon being studied (Creswell, 2013). According to Leonard-Barton (1990), a single case study approach is subject to the limit in generalisability and potential biases such as misrepresentation of a single event and exaggeration of data, whilst a multiple case study approach guards against bias and exaggeration. This research study analysed the contributing factors to the near collapse of African Bank and the collapse of VBS; therefore, bias and exaggeration should be guarded against to ensure the true reflection of the sequence of events that took place at both banks.

3.3. Data collection

Data collection is the process of gathering information in an established system that enables the researcher to answer research questions, evaluate outcomes, and test hypotheses (Wilson and Miller, 2014). This research study was conducted using a structured framework derived from a defined set of research propositions along with a secondary data collection method in the form of document analysis. According to Wagner et al. (2012, p.141), document analysis refers to, *"an integrated and conceptually informed method, procedure and technique for locating, identifying, retrieving and analysing documents for their relevance, significance and meaning".* Bowen (2009) argues that document analysis involves gathering useful data from organisational documents and electronic records. To conduct this research, secondary data such as organisational annual reports and investigative reports, press media articles, as well as communication statements made by both African Bank and VBS banks were sourced. The source documents for VBS include those of the years 2015, 2016, 2017 and 2018, for African Bank source documents from 2012, 2013, 2014 and 2015 were used. This information is available in the public domain and was used to gather data wherein careful analysis was conducted to conclude this body of related documents. The statements from these documents were documented and recorded in a table that links these statements to the research proposition (see Table 2). Bowen (2009) highlights that documents of all types can assist the researcher to uncover certain meanings, develop understanding as well as assist in discovering insights that are relevant to the problem being researched. Therefore, this data collection method is suitable for this study.

Sixty-two (62) questions were developed, guided by the literature review and the propositions of this study. To illustrate the formulation of these questions, two propositions were derived and the questions were developed in line with these two propositions. The detailed questions and sub-questions are listed in a table in Table 2 below.

Table 2. Questions used for data collection

Questions	Sub-Questions	Source/ Justify	Proposition
How did the banks demonstrate commitment to integrity and ethical values?		**Source**: King III report (IoDSA, 2016) **Justification**: The report indicates that organisations should be governed in a way that supports the establishment of ethical culture. Therefore, there is a need to assess how the banks demonstrated commitment to integrity and ethical values.	P2
In what way did the banks' code of ethics prove to be effective in ensuring that the banks establish a good ethical culture? How did clearly defined roles, responsibilities, and reporting structures assist the banks' management to ensure accountability by both management and staff? How did the lack of clarity in roles, responsibilities and reporting structures result in limitations in ensuring accountability for both management and staff?	Did the bank have a clearly defined code of ethics?	**Source**: King III report (IoDSA, 2016) (Ogbo, Okechukwu and Ukpere, 2013) **Justification**: Emphasis is placed on the fact that there is an expectation on a business to take a genuine interest backed by practical actions in ethically pursuing its objectives. Therefore, the questions seek to assess if the roles, responsibilities, and reporting structures resulted in ensuring accountability for both management and staff.	P2
How did the management of the banks demonstrate commitment to ethical behaviour and practices that is expected from every person acting on behalf of the organisation?		**Source**: (Green, 1989). **Justification**: The employees as a collective body who reflect on a business's ethical stance must know what principles guide their conduct. This question will clarify how the banks demonstrated their commitment to this ethical conduct.	P2

Questions	Sub-Questions	Source/ Justify	Proposition
How did the leaders of the banks demonstrate appropriate conduct according to the ethics principles and values of the organisations? What control environment activities did the bank's governing body and senior management implement to set the organisational tone for ethical values? What limitations in the control activities of the banks governing body and senior management led to unethical organisational values?	Did the control environment and activities prove to be effective?	**Source**: King IV report (IoDSA, 2016) Khang (2005) **Justification**: The key component to achieving the best ethical organisations is the leadership that is made visible through its actions and commitment to ethical practices and sets the moral tone from the top that translates ethical principles into behaviour that is expected from every member of the banks. The question will clarify how the leaders of the banks demonstrate appropriate conduct by following ethical principles and how management set the organisational tone for ethical values.	P2
How did the control environment and activities assist in ensuring a sustainable ethical culture in the banks? What were the shortcomings in the control environment that led to an unethical culture in the bank?	Did the banks have proper governance in place for organisational ethical culture?	**Source**: King IV report (IoDSA, 2016) (Basel Commission, 2015). **Justification**: The role of the board of directors as responsible for managing the company includes ensuring a prudent risk management framework and oversight of risk management. Therefore, it is important to clarify whether control activities ensured or fail to ensure a sustainable ethical culture in the banks.	P2
In what way did the banks' organisational structure clarify the roles of effective risk identification? In what way did the banks solicit stakeholders' feedback for risk identification?	How did the banks identify the risks? Was the banks' management qualified and competent to identify risks?	**Source**: (Luburić, 2017) (Andersen et al., 2012) **Justification**: The first line of defence is to identify risks and execute actions to manage and treat these risks. Therefore, it is important to understand how the risks were identified.	P2

Questions	Sub-Questions	Source/ Justify	Proposition
How effective are the banks' risk assessment structures and how often did the banks carry out these assessments? What were the weaknesses of the risk assessment structures?		**Source**: (Luburić, 2017) (Andersen et al., 2012) (Basel Commission, 2015) (IoDSA, 2016) **Justification**: It is important to understand how the risks were assessed.	P2
How did the banks ensure that the processes in place enabled complete, timely, relevant, accurate, and accessible risk disclosure to legitimate stakeholders? What were the weaknesses of the risk disclosure policies?		**Source**: (Luburić, 2017) (Andersen et al., 2012) (Basel Commission, 2015) (IoDSA, 2016) **Justification**: It is important to understand how the banks enabled or fail to enable complete, timely, relevant, accurate and accessible risk disclosure to stakeholders.	P2
In what way were the banks' policies and procedures developed, reviewed, and amended to ensure best practices? How did management ensure that these policies and procedures provide consistency and discipline within the organisation as well as ensure overall definition and allocation of specific roles and responsibilities for managing risks?	How did the risk committee assist the governing body to carry out the risk responsibilities? How do the banks determine how risks should be managed?	**Source**: (Luburić, 2017) (Andersen et al., 2012) (Basel Commission, 2015) (IoDSA, 2016) **Justification**: It is important to understand how the banks risk management policies were developed.	P2

Questions	Sub-Questions	Source/ Justify	Proposition
How adequate were the internal controls of the banks, and could these policies and procedures be implemented effectively? What failures in the implementation of policies and procedures resulted in ineffective internal controls?	How did management effectively execute their risk responsibilities to ensure that internal controls are effective?	**Source**: (Luburić, 2017) (Andersen et al., 2012) (Basel Commission, 2015) (IoDSA, 2016) **Justification**: It is important to understand how management effectively executed or failed to execute their risk responsibilities to ensure effective internal controls.	P2
In what way did management ensure that the risk control activities (approvals, authorisations, verifications, etc.) are carried out effectively? In what way did management ensure that the risk control activities (approvals, authorisations, verifications, etc.) are carried out ineffectively?	Did the staff comply with the supervisory and risk control measures?	**Source**: (Luburić, 2017) (Andersen et al., 2012) (Basel Commission, 2015) (IoDSA, 2016) **Justification**: It is important to clarify how management ensured risk control activities are carried out effectively.	P2
How did the banks enforce and reward accountability for organisational performance? How did the banks fail to enforce and reward accountability for organisational performance?	Does management and staff take accountability for their actions?	**Source**: (Luburić, 2017) (Andersen et al., 2012) (Basel Commission, 2015) (IoDSA, 2016) **Justification**: It is important to clarify how management ensured that corrective actions are carried out to address process and control deficiency.	P2

Questions	Sub-Questions	Source/ Justify	Proposition
How did the banks effectively monitor operational risk? How did the banks management execute internal audits and continuous activities to ensure effective corporate governance, risk management, and compliance? How did the banks fail to monitor operational risk?	What are the processes in place that assesses the quality of systems performance over time?	**Source**: (Luburić, 2017) (Andersen et al., 2012) (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To clarify how the banks monitored their operational risks.	P2
In what way did risk reporting positively affect business operations and stakeholders' perceptions? In what way did risk reporting negatively affect the business operations and stakeholders' perceptions? How effective, reliable, and comprehensive were the bank's risk reports? How did information flow across the organisational structures of banks?	How is information identified, captured, and communicated in a form and timeframe that enables people to carry out the allocated responsibilities?	**Source**: (Luburić, 2017) (Andersen et al., 2012) (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To understand how the banks' information was communicated across the organisational structures and how operational risks were reported to the stakeholders.	P2
How often did the banks conduct risk management training? How were the outcomes of the risk management training measured to ensure that the training is effective?		**Source**: (Luburić, 2017) (Andersen et al., 2012) (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To understand how risk training was conducted by banks and what were the outcomes of the training and how they were measured to ensure that the training is effective.	P2

Questions	Sub-Questions	Source/ Justify	Proposition
How did the bank's management respond to the identified risks? How did management demonstrate to the bank's board of directors the need to consider the appropriate risk responses and its implementation plans?		**Source**: (Luburić, 2017) (Andersen et al., 2012) (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To clarify the bank's risk response, guidance and coordination efforts.	P2
How did management facilitate, coordinate and monitor the effective execution of defence activities established by the first line of defence risk owners?		**Source**: (Luburić, 2017) (Andersen et al., 2012) (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To clarify the bank's risk management compliance processes that existed.	P2
What risk assessments were carried out by the bank to review their risk levels?		**Source**: (Luburić, 2017) (Andersen et al., 2012) (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To clarify the risk review processes and escalation levels that existed at the banks.	P2

Questions	Sub-Questions	Source/ Justify	Proposition
In what way did the bank's risk frameworks provide risk assurance that ensures business sustainability and compliance with applicable laws? In what way did the failures in bank's risk frameworks negatively affect the risk assurance sustainability and compliance with applicable laws?		**Source**: (Luburić, 2017) (Andersen et al., 2012) (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To assess if the bank's risk frameworks provided independent risk assurance and compliance with applicable laws.	P2
How did the internal audit assure these specific banks regarding compliance with good corporate governance requirements?		**Source**: (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To assess if the bank's risk frameworks provided independent risk assurance and compliance with good corporate governance.	P2
What effective process was followed by the internal audit in line with the three lines of defence model when providing written assessments?		**Source**: (Luburić, 2017) (Andersen et al., 2012) (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To assess processes followed by the internal auditors when providing written assessments for the banks.	P2
In what way did the internal audit give assurance about management's claims surrounding the effectiveness of internal control and risk management?		**Source**: (Luburić, 2017) (Andersen et al., 2012) (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To assess processes followed by the internal auditors when providing written assessments for the banks. **Source**: (Luburić, 2017) (Andersen et al., 2012) (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To assess the independence of internal auditors when auditing the banks.	P2

Questions	Sub-Questions	Source/ Justify	Proposition
How much independence did the audit firms have when auditing the banks? In what way did the bank's board and management enforce auditor independence and audit quality?	What status and authority did the internal audit have?	**Source**: (Luburić, 2017) (Andersen et al., 2012) (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To assess processes followed by the internal audit when providing written assessments for the banks. **Source**: (Luburić, 2017) (Andersen et al., 2012) (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To assess the independence of internal auditors when auditing the banks.	P2
What were the clearly defined roles and responsibilities of the audit committee at the banks, were they consistent with the three lines of defence model and corporate governance principles? How did the audit committee provide the board with an independent assessment of the effectiveness of the organization’s internal controls? How did the audit committee provide independent oversight of assurance functions and services of internal and external auditors?	Are these committees comprised of qualified, competent and independent members? Does the bank have clearly defined roles and responsibilities for the audit committee, and are these committees functioning effectively? How effective are the policies and controls that address the provision of services rendered by external auditors?	**Source**: (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To assess the roles and responsibilities of the bank's audit committees, and if the committees were consistent with the corporate governance principles.	P2

Questions	Sub-Questions	Source/ Justify	Proposition
What were the clearly defined roles and responsibilities of the risk committee at the banks, were they consistent with corporate governance principles? How did the risk committee provide independent oversight on risk policy creation and risk governance functions?		**Source**: (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To assess the roles and responsibilities of the bank's risk committees, and if the committees were consistent with the corporate governance principles.	P2
In what way did the board contribute and execute its oversight function to the banks? How did the governing body oversee and monitor risk management implementation and execution by management?	How does the governing body exercise oversight responsibility of the banks? How does the governing body ensure the integrity of both internal and external reports?	**Source**: (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To assess how the board of directors contributed and executed its oversight function to the banks.	P2
What measures did the banks put in place to ensure an effective control environment, and how effective were these measures?		**Source**: (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To assess the measures put in place to ensure an effective control environment for the banks.	P2
How did the banks enforce accountability for the governance and performance of the organisations?		**Source**: (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To assess the measures put in place to ensure an effective control environment for the banks.	P2

Questions	Sub-Questions	Source/ Justify	Proposition
How did the risk and monitoring committee provide oversight to the banks to ensure effective risk assessment and monitoring?	In what way did the banks conduct ongoing and separate risk evaluations?	**Source**: (Luburić, 2017) (Andersen et al., 2012) (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To assess how the banks monitored their operational risks.	P2
How did the compliance committee ensure that the banks complied with the regulation?		**Source**: (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To assess the roles played by the compliance committee to ensure that the banks comply with the regulations.	P2
How did the board of directors ensure that a robust operational risk management culture existed throughout the whole organisation?		**Source**: (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To assess the roles played by the compliance committee to ensure that the banks comply with the regulations.	P2
In what way did the senior management develop a practical and robust governance structure with defined, transparent and consistent lines of responsibility?		**Source**: (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To assess the roles played by the compliance committee to ensure that the banks comply with the regulations. **Source**: (Freeman and Reed, 1983) (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To assess how the bank's management ensured that the performance of the organisation is transparent and understood by all stakeholders.	P2

Questions	Sub-Questions	Source/ Justify	Proposition
In what way did the board of directors oversee senior management to ensure that policies, processes, and systems are implemented effectively at all decision-making levels?		**Source**: (Basel Commission, 2015) (COSO, 2013) (IoDSA, 2016) **Justification**: To assess the roles played by the compliance committee to ensure that the banks comply with the regulations.	P2
How did the bank's management ensure that the performance of the organisation is transparent and understood by all stakeholders?		**Source**: (Freeman and Reed, 1983) (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To assess how the bank's management ensured that the performance of the organisation is transparent and understood by all stakeholders.	P1
How did the bank's management ensure that the reports issued enabled stakeholders to make informed assessments of the bank's performance? In what way did the public disclosure of the bank's annual and financial reports allow stakeholders to assess the bank's approach to operational risk management?		**Source**: (Basel Commission, 2015) (IoDSA, 2016) **Justification**: To assess how the bank's management ensured that the reports issued enabled stakeholders to make informed assessments of the bank's performance.	P1
How did the bank's management take into account the legitimate and reasonable needs, interests, and expectations of all material stakeholders in the execution of their duties?		**Source**: (Parmar et al., 2010) (IoDSA, 2016) **Justification**: To assess how the bank's management took into account the legitimate and reasonable needs, interests, and expectations of all material stakeholders in the execution of their duties.	P1
In what way did the banks ensure that there are processes in place enabling complete, timely, relevant, accurate, and accessible risk disclosure to stakeholders?		**Source**: (Parmar et al., 2010) (IoDSA, 2016) **Justification**: To assess how the bank's management ensures that the processes in place enabled complete, timely, relevant, accurate, and accessible risk disclosure to stakeholders.	P1

Source: Own Formulation

3.4. Data analysis

The data analysis process involves various ways in which the researcher makes sense of their data (Wagner et al., 2012). This research study adopted a deductive thematic analysis and pattern matching method. This method involves identifying themes and patterns in a particular set of data, as well as seeking to understand a particular phenomenon by observing how various participants experienced a phenomenon (Wagner et al., 2012). Additionally, Pearse (2019) outlines the steps involved when using the deductive thematic analysis method and some of the outlined steps were adopted for this particular study. The steps adopted include (1) developing the coding manual (including labelling, defining and describing when the theme occurs), summarising data and identifying initial themes, and (2) connecting the codes and identifying the themes (Pearse, 2019).

A set of eight documents from each of the two banks were closely studied and analysed, resulting in 16 documents being analysed. These documents include three annual reports for each bank, Motau investigative report on VBS (VBS, 2018), and Myburgh investigative report on African Bank (Myburgh, 2016). The qualitative data, which includes statements from the documents analysed, were recorded as answers to the questions that were used during data collection. These statements were summarised and interpreted using deductive thematic analysis to assist in ensuring the trustworthiness of the findings.

Table 3 below provides an illustration of the proposition and the linkages to the codes derived from the literature reviewed. The table further outlines the areas of concern that were considered, and the description of the mentioned areas as outlined in the literature review.

Table 3. Code manual

Propositions	Areas of concern	Description
P1: The governing body should adopt a stakeholder-inclusive approach that balances the stakeholder needs, interests, and expectations as well as the best interest of the organisation over time.	Stakeholder legitimacy and inclusivity	Stakeholders that the organisation holds a moral obligation of acting fairly, and the groups whose claims and actions if not accounted for by management might negatively affect the wellbeing of the organisation.
	Corporate governance	The system provides checks and balances that ensure that the organisation discharge their accountability to their stakeholders and act in a socially responsible manner.

P2: The effective governing body should govern organisational ethics in a way that supports the establishment of ethical culture in the banks, and develops effective, well-defined, transparent, and consistent lines of responsibility that encourage and maintains accountability by management and staff	Ethical culture	How the organisation explores moral principles used to evaluate the business impact on people and the environment.
	Internal controls	A strong control environment that utilises practices, policies and procedures as well as appropriate internal controls and risk mitigation strategies.
	Risk management: operational risks	Organisational exposure to potential losses that arise because of inadequacies or failures of the organisation's operations.

Source: Own Formulation

After the completion of the coding process, the next step was to summarise and identify initial themes, as well as connecting the codes to the themes. Though the themes are the same for both banks, there is a slight difference in the wording of the themes. The events that took place at the two banks are similar but they had different causal factors explained in the findings in Chapter 4. Seven (7) themes were generated from both the initial and additional codes after exploring the data. Each theme consists of different sub-themes. According to Pearse (2019), themes represent a certain level of a pattern in the responses or a meaning derived from the analysed data. All the identified themes are described in detail in the findings chapter.

3.5. Quality criteria

The following quality criteria was undertaken to ensure the validity of the study. This includes credibility which was achieved by persistent observation of the documents analysed (Korstjens and Moser, 2018). Transferability was achieved by describing the context in which this research is carried out (Korstjens and Moser, 2018). Moreover, the research findings were presented transparently through a questionnaire and themes development and coding notes. According to Korstjens and Moser (2018), confirmability and dependability can be achieved by maintaining the audit trail of the research. For this research study analysis notes, reflective thoughts and other research material such as articles were used and saved to ensure the dependability and confirmability of this research study.

3.6. Ethical consideration and limitations

Ethical considerations for this study followed a few steps that were taken to ensure that all the ethical requirements for the research study are met. (1) no ethical clearance was to be obtained from the university faculty given that the researcher used publicly available data (2) the researcher was sensitive to the two bank's information obtained, and data was used only for this research.

Limitations of the study were that the information available for data analysis was only what is in the public domain. The researcher was not able to access the internal information at both banks due to the internal governance and policies as well as limited time for the study.

3.7. Conclusion

This chapter outlined the framework this research study followed to evaluate the outcomes of this study. Existing literature was reviewed on the methodology of the research study. The following chapter presents the research findings as well as the detailed interpretation of these findings.

CHAPTER 4: FINDINGS

4.1. Introduction

This chapter presents and discusses the findings of this study; the findings were gathered through qualitative methods using document analysis. The African Bank 2012 to 2015 annual reports and VBS 2015 to 2018 annual reports were used as reference documents to gather data; the reference documents included the Myburgh (2016) African bank and Motau (2018) VBS bank investigative reports. Further, a detailed discussion of the findings is provided, as well as the three lines of defence model and its application at both banks is provided in this chapter. A summary of both African Bank and VBS operations and an overview of each organisation's risk management structures are presented.

4.2. Overview and summary of African Bank and VBS

This section provides a brief overview of the African Bank and VBS, identifying risks that led to the near collapse of the African Bank and the collapse of VBS bank.

<u>African Bank</u>

African Bank Investment Limited (ABIL) was a holding company with three main subsidiaries i.e. furniture retail business (Ellerines), the insurance business (InsureCo), and the bank business (African Bank). African bank was a monoline lender lending unsecured loans mostly to low-income earners (African Bank, 2015). Historically, African Bank relied primarily on wholesale funding from bondholders including mutual and pension funds (African Bank, 2015). From 2008 when ABIL acquired Ellerines (the retail business), African Bank became the financial funding vehicle for Ellerines credit customers (African Bank, 2015).

In 2013, the bank started losing focus on risk management and controls, adopting relaxed credit and risk assessment policies, which resulted in a high percentage of customers defaulting on loans and credit repayments (African Bank, 2015). Subsequently, the bank's bad debt book grew substantially (Donnelly, 2016). The bank failed to implement industry-acceptable practices of bad debt write-off, which led to an unmanageable credit book (Myburgh, 2016). These poor risk management practices resulted in the bank being placed under curatorship by South African Reserve Bank (SARB) in 2014 (Donnelly, 2016).

<u>VBS</u>

VBS was a mutual bank that primarily focused on retail banking which secured deposits from burial societies and stokvels (VBS, 2016). The bank offered short-term loans and mortgages using bank deposits and clients' properties as collateral (VBS, 2016). On 11th March 2018, the SARB issued a formal written statement informing the industry and the public that VBS has been placed under curatorship to be carried out by Sizwe Ntsaluba Gobodo advisory services (SARB, 2018). Subsequently, the North Gauteng High Court issued an order for the final liquidation of VBS on 13th November 2018 (VBS, 2018).

The initial operating strategy of VBS was to mainly focus on small retail deposits and burial societies, and since its inception, there is no indication that the bank was struggling with profitability under the original operating model (VBS, 2016). VBS later abandoned its original operation strategy and adopted a new strategy of obtaining very large, short-term deposits from municipalities, which became too big to manage (Motau, 2018). This strategy was aimed at turning VBS into a significant profit-making enterprise since the bank was previously not making a profit (Motau, 2018).

This newly adopted strategy was inconsistent with the regulations that govern mutual banks and the conditions of their operating license (Motau, 2018). One of the regulations that prohibit the mutual bank to take a deposit from municipalities includes the Municipal Management Financial Act which states that a municipality may not open a bank account with an institution that is not registered as a bank in terms of the Bank Act of 1990 (Municipal Finance Management Act, 2003). VBS was operating in contravention of the above-mentioned regulations.

4.3. Risk management structures

The risk management structures and a brief overview of the activities undertaken during the stated periods under review in this study are discussed in detail in this section.

All committees for both banks are presented in Figures 3 and 4 below, however, only audit, group risk, and capital management, as well as ethics committees, are discussed in detail for African Bank as they are the committees that are related to this particular study. Similarly, for VBS the committees that the study focuses on are audit and risk, and compliance committees, only these committees will be discussed in detail.

Figure 3 below presents committees that assisted and supported the board of directors of African Bank to fulfil its risk management duties.

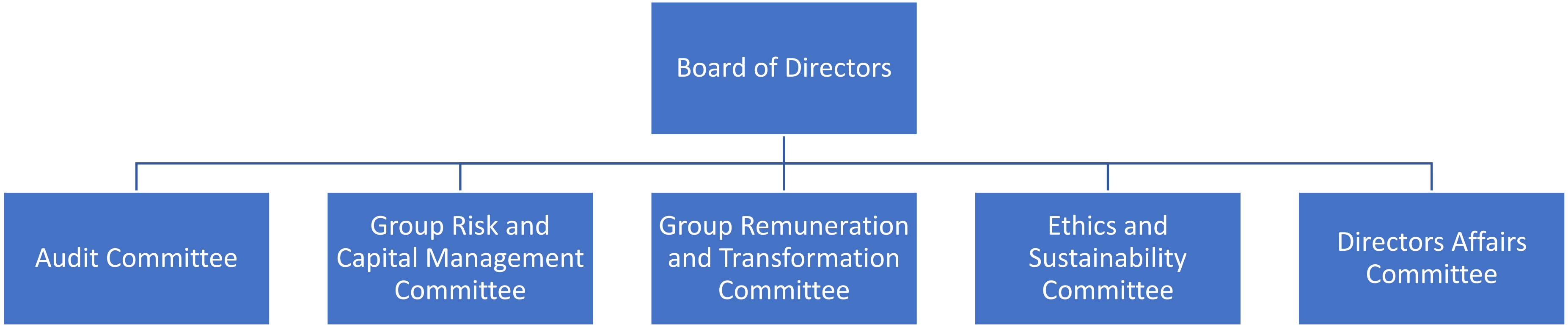

Figure 3. African Bank Board of Directors Committee Structure (African Bank, 2015)

Board of directors: A board of directors and senior management that claimed to be committed to the highest standard of corporate governance (African Bank, 2015) governed the bank. According to African Bank (2015), the board embraced the principles of good corporate governance as set out in King Code III and strived for high moral and ethical business standards as well as sound and transparent business practices. The board consisted of ten (10) board members of which six (5) were independent non-executive directors (INED) and five (5) executive directors (ED). Two members had BCom, two members held BPrac and LLB, one held a BA Law and five other members' qualifications were not listed on the list of board members (African Bank, 2015). The board members further held directorship in different organisations including non-profit organisations (African Bank, 2015). The detailed names, qualifications and experience of individual board members is detailed in Annexure 3.

Audit committee: This committee assisted the board in discharging its duties associated with the safeguarding of assets, the integrity of internal financial control processes and integrated reporting, accounting systems, and practices as well as the preparation of accurate financial reporting and statements in compliance with applicable accounting standards and legal requirements (African Bank, 2015). The committee had three (3) members who were independent non-executive directors (African Bank, 2015). These three members included the chairperson and two INED qualified in BCom Honours and LLB (African Bank, 2015). The Terms and Reference (TORs) of the board committees could not be found since the website is discontinued. According to African Bank (2015), the internal audit and external audit functions reported directly to the audit committee, and the external auditor of the bank was Deloitte.

Risk and capital management committee: this committee's role was to assist the board in ensuring the quality, integrity, and reliability of risk management in the bank (African Bank, 2015). The risk and capital management committee together with the audit committee were the oversight bodies for the implementation of effective internal control and efficient risk management frameworks (African Bank, 2015). The committee had four members. Three members were qualified in BCom Honours and one in LLB (African Bank, 2015).

Ethics and sustainability committee: the role of the ethics and sustainability committee was to assist the board and management to formulate and implement policies, principles, and practices that foster sustainability including a business model that creates value that is consistent with the long-term preservation of social, financial, and environmental capital (African Bank, 2015). This committee had three members who were qualified in BCom and Law respectively.

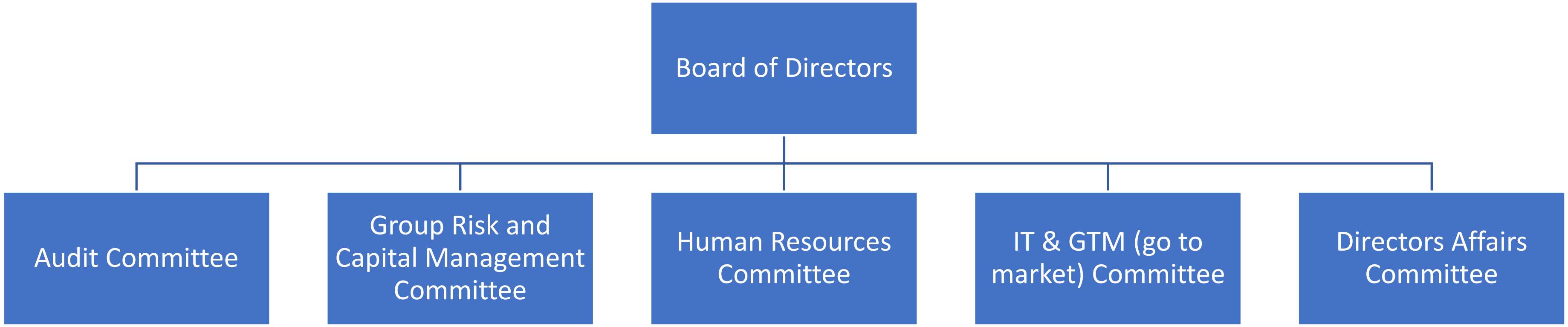

Figure 4. VBS Board of Directors Committee Structure (VBS, 2016)

Figure 4 above indicates the structure of the board of directors committees of VBS that assisted and supported the board to fulfil its risk management duties. Annexure 3 indicates the names, qualifications, and functions of the board, its achievement as well as its committee members.

Board of directors: The board of directors of VBS bank is comprised of fourteen (14) board members of which twelve (12) were independent non-executive directors and two (2) executive directors (VBS, 2016). The board delegated its functions to the structured committees that supported the board; however, it did not abdicate its responsibilities (VBS, 2016). The delegation was formal, and it included ensuring that formal terms of reference are established, approved as well as reviewed at least annually (VBS, 2016). Members who were qualified in BCom Accounting and registered CA (SA) including the chairperson of the board (VBS, 2016) made up the board of directors of VBS.

Of all the board members, seven members held a qualification in BCom specialising in accounting and registered as charted accountants (CA), one member held a Bachelor of Economics qualification. In addition, two members were qualified in LLB and LLM respectively, one in BSc and MBA, one was qualified in BCompt (Hons), one possessed a junior secondary teacher's certificate and one member posing a certificate in bookkeeping.

Audit committee: According to VBS (2016), the audit committee was advisory in nature, and it assisted the board and management concerning integrated reporting, internal and external audits, combined assurance and development of internal audit programmes, maintenance of adequate accounting methods, development and maintenance of effective internal controls as well as reporting on financial related matters.

Risk and compliance committee: similar to the audit committee, the risk and compliance committee was also advisory in nature, and it assisted the board and management with risk management oversight, the development, maintenance, evaluation, and monitoring of compliance policies (VBS, 2016). Furthermore, the committee's role was to assist in establishing a risk management infrastructure that was capable of addressing identified risks, as well as recommend to the board the bank's compliance plan (VBS, 2016).

The above section provided an overview of the functions of African Bank and VBS structures that were put in place to assist the board of directors to discharge their fiduciary duties and responsibilities of maintaining good corporate governance (IoDSA, 2016). According to Sison (2010), corporate governance provides checks and balances that ensure that organisations discharge their accountability to all their stakeholders and act in a socially responsible way while conducting their business activities. In the case of African Bank and VBS, it appears that they set up these structures to put focus on the risk management part of the board of directors' fiduciary responsibilities. It must be highlighted that at this stage these appear to be structures that indicate the intention to manage risks, however, the effectiveness of these structures still needed to be tested.

4.4. Themes

Seven (7) common themes emerged during the coding process of both African and VBS banks. The individual themes and the subthemes that contribute to each main theme are discussed in detail in this section. These themes and sub-themes explain the findings drawn from the data collection process of this particular research study. Coding processes were created using Ose's (2016) 10-step method of using Microsoft Excel and Word to structure qualitative data. Each theme was labelled alphabetically from A to G respectively as shown in Table 4 below.

Table 4. Themes for African Bank and VBS

Code	**African Bank Themes**	**VBS Themes**
A	Lack of leadership commitment in governance	Lack of leadership commitment in governance
B	Lack of ethical leadership and poor consequence management	Lack of ethical leadership and poor consequence management
C	Weak internal controls	Collapsed internal controls
D	Ineffective leadership structures	Ineffective leadership structures
E	Non-compliance to regulatory requirements	Non-compliance to regulatory requirements
F	Irregular financial management	Irregular financial management
G	Non-inclusive stakeholder relations	Non-inclusive stakeholder relations

Source. Own Formulation

<u>African Bank</u>

The areas of concern identified in these themes are discussed below with reference to African Bank Integrated Reports from 2012 to 2015 and Myburgh Investigative Report (2016).

Theme A: Lack of leadership commitment in governance

This theme highlights the issues that are relevant to the lack of leadership commitment at the bank.

<u>Governance:</u> The board of directors embraced the governance principles as set out in King Code III of good corporate governance to ensure that an ethical foundation exists and

promotes responsibility, accountability, fairness, and transparency. However, there is no evidence indicating how the board and bank management practically executed internal audits and continuous activities that ensure effective corporate governance, risk management, and compliance.

Theme B: Lack of ethical leadership and poor consequence management

The second theme describes the lack of ethical leadership and poor consequence management, in the areas described in detail below.

Code of conduct: The data collected indicates that there was no code of conduct in place at the bank. Subsequently, management did not take any decisive remedial actions after being warned about the liquidity crisis the bank was heading for.

Code of ethics: The data collected indicates that there was no code of ethics in place and no ethical guidance for the rest of the organisation. Staff and management up to the level of the CEO and the board were not guided on matters of ethics and the desired ethical culture of the organisation.

Lack of consequence management: Senior management and the board were expected to carry out their responsibilities to take action against those involved in wrongdoing as part of enforcing good governance and conduct in the organisation. However, no action was taken against any wrongdoings. This lack of consequence management resulted in a culture of deliberate non-compliance by the bank staff, knowing that there will be no action taken against them.

Theme C: Weak internal risk controls

Weak internal risk controls is the third theme that was derived from the coding process, the areas below contribute to the discussion of the main theme.

Responsibility: The available data indicates that there was no evidence of an existing code of conduct and defined responsibility for risk management and ethics. The appointed risk managers and governance structures failed to take responsibility for managing risks within the areas that they were accountable.

Internal risk controls: Employment of an unqualified Chief Risk Office and non-implementation of documented internal risk controls by management and staff. On the other hand, the roles and responsibilities of the risk committee were unclear and undefined. It appears that in the bank structures, there was non-compliance with International Accounting Practices and Standards, as well as the adoption of a relaxed bad debt write-off policy. The identified extensive non-compliance with risk controls extended to risk management policies and procedures and employees were not held accountable, demonstrating a lack of consequence management. There is no evidence indicating that proper risk assessment and due diligence were done by management when acquiring new businesses outside the banking industry (i.e. the acquisition of Ellerines Retail Group). The bank in some instances did not comply with the national credit regulator risk frameworks and the bank was fined for this non-compliance.

Audit: There is no evidence of historical internal audits carried out by management. The internal audit department failed to provide advice and insights on the bank's risky and non-compliant activities. Management failed to act on the risk and compliance warnings carried out in Deloitte's external audit report for the financial year 2012/13. Management and the board did not treat internal audits as a priority in risk mitigation.

Reports: Reports appeared to have lacked transparency and integrity; this is demonstrated by non-disclosure by management of some identified risks.

Theme D: Ineffective leadership structures

The fourth theme is ineffective leadership structures, and it is discussed in detail below.

Accountability: It appears that the bank had the required risk committees in place for reporting to the board and ensuring accountability by both management and staff. However, evidence from the data indicates that the structures became ineffective, and subsequently, staff and management were not held accountable. The data indicates that even when the National Credit Regulator (NCR) made damning findings regarding reckless lending by the bank, management did not take any action or accountability. In the bank's EXCO, only two members were willing to take accountability. In many cases, the CEO who took most of the decisions mostly overpowered management.

Oversight: The board of directors met seven (7) times in 2012. The board of ABIL was the same as the African Bank resulting in a conflict of interest in terms of the director's fiduciary duties. This made it impractical to ensure that the bank continued to remain a sound institution and it was exposed to the risks from group companies. In addition, the bank had a group risk committee that met quarterly to discuss risk issues. However, the data does not indicate how the bank carried out the risk assessment, and how effective were the decisions taken by the risk committee in mitigating the risks of the bank. Management went along with the CEO even though they did not agree with his views.

The executive met with the board, and special meetings would be called to address pressing issues at that time. To highlight this practice, in a special meeting of the board on 18 October

2013, the CEO told the meeting that an additional large amount was required by the bank due to a duplum adjustment the bank had to undertake. The group risk committee met quarterly to discuss risk-related issues. However, the CRO could not make any meaningful contribution to the committee.

Theme E: Non-compliance to regulatory requirements

Non-compliance: The board approved an independent compliance function established in terms of Regulation 49 of the Banks Act, 94 of 1990 as part of the compliance policy. Data indicates that the bank's accounting practice did not comply with the requirements of IAS39 regarding the cash flow to accounts that had reached in duplum status. These accounts should have been discounted to the original effective rate, instead the bank discounted them to zero. This was a deviation from the market practice relating to the definition of "default" and Non Profit Loans (NPL) write-offs. The failures in the bank's risk frameworks resulted in non-compliance with the National Credit Regulator (NCR).

Theme F: Irregular financial management

The area discussed under irregular financial management consists of the reckless lending which is discussed in detail below.

Reckless lending: In 2011, the NCR fined the bank for adverse findings of reckless landing at their Dundee branch. According to African Bank (2015), this was caused by the manipulation of bank's IT and Phoenix systems to allow repeat customers to be granted new loans without settling the existing loans. The data shows no evidence of decisive corrective action that was taken by the bank when NCR made these findings of reckless landing, this indicates a lack of accountability by management.

Theme G: Stakeholder non-inclusivity

Non-inclusivity: The bank produced integrated reports annually and had meetings with investors and shareholders. It appears that the bank's reports were comprehensive; however, one cannot say the same for reliability. The data indicates that in 2013 the investors and shareholders were disappointed that information about higher levels of NPLs was not disclosed to them during their meetings with the bank. According to African Bank (2015), some investors and shareholders stopped rolling over their shares once they realised the financial state of the bank in the 2012/13 financial year and upon realising the operational risks and challenges faced by the bank.

VBS Themes

The areas of concern identified in these themes are discussed below with reference to VBS annual reports from 2014 to 2018 and Motau Investigative Report (2018).

Theme A: Lack of leadership in governance

Governance: The board of directors of the bank recognised governance principles as set out in King code III of corporate governance. However, there is no evidence indicating how the board and bank management practically executed internal audits and continuous activities that ensure effective corporate governance, risk management, and compliance.

Theme B: Lack of ethical leadership and poor consequence management

Code of conduct: There was no code of conduct in place. Bank's management used the bank's financial resources to pay off certain individuals for their silence and not to report unlawful transactions. Instead, management appeared to have been rewarded for facilitating unlawful transactions. In most instances, management and the board were encouraged to ignore the unlawful conduct of the CEO and CFO. The unlawful conduct extended to the involvement of the chairperson of the board.

Code of ethics: There was no code of ethics in place and no ethical guidance for the rest of the organisation. Staff and management up to the level of CEO and the board were not guided on matters of ethics and what is the desired culture of the organisation.

Lack of consequence management: Management deliberately overlooked discrepancies and integrity between the published financial statements and the actual financial state of the bank. Senior management and the board were expected to take action against those involved in wrongdoing as part of enforcing good governance and conduct in the organisation, instead, all the wrongdoing was concealed, and no action was taken.

Leadership unethical culture: There was no ethical leadership tone set by the senior management and the board to provide guidance and direction on the ethical culture of the organisation. Senior management allowed serious deviations from procedures such as failure to use the bank's operating systems and instead, they used manual recordings with no adequate audit trail. Banks management created fraudulent suspense accounts that reflected non-existent deposits.

Theme C: Collapsed internal risk controls

Responsibility: The available data indicated that the bank had structures with clear roles and responsibilities to identify risks as required. It appears that the appointed risk management and staff failed to adhere to and perform according to the defined roles and responsibilities. The is no evidence indicating that management took the responsibility of ensuring that the bank had an internal audit, instead the bank outsourced the responsibility of internal auditing to external auditors. This indicates the lack of seriousness for internal controls by management.

Internal risk controls: There is no evidence indicating that management ensured that the risk control activities are effectively carried out. This is illustrated by the fact that management outsourced this function to perform independent and objective assurance and to add value to the bank's operations. Management failed to coordinate, facilitate, and monitor the consistent effective execution of defence activities established in the first line of defence risk review. This can be attributed to the fact that there is no evidence indicating that internal audit structures existed in the bank. It appears that the CFO and the CRO colluded with the lead audit partner of KPMG to conceal the un-reconcilable financial accounts of the bank.

Audit: There is no evidence indicating the existence of internal audit structures in the bank. This resulted in the bank accepting the external auditor's report indicating that the audit report for 2017 and its financial performance and cash flows were according to IFRS and met the requirements of the Mutual Banks Act. This was not correct since the lead audit partner was aware that the books were not reconciling yet concealed this information. It appears that the external auditors may have overlooked and failed to report fraudulent activities that were taking place at the bank.

According to available data, the bank withheld the auditor's necessary information that would have assisted auditors to complete the audit. Junior audit staff members were unable to obtain the bank's information such as a general ledger with recorded bank accounts to use for audit purposes. Furthermore, when the junior auditors presented these and other audit problems they have identified in the audit, these issues were brushed aside and never addressed.

Reports: Reports appeared to have lacked transparency and integrity; this is demonstrated by non-disclosure by management of some identified risks.

Theme D: Ineffective leadership structures

Accountability: It appears that the bank had the required risk committees in place to report to the board and ensure accountability by both management and staff. However, evidence from the data indicates that the structures became ineffective and inactive, and subsequently, staff and management were not held accountable. This ineffectiveness opened a loophole for decisions such as approving staggered small amounts below the mutual bank's threshold resulting in lack of visibility and accountability to the banking industry regulator (SARB). During these transactions management failed to take any accountability for their actions, instead they rewarded themselves with payments.

Oversight: Management was expected to oversee transactions that were taking place at the bank, but it appears that management participated in colluding with staff to create fictitious transactions to reflect on the bank's financial reports. There is no evidence of the flow of information across organisational structures. It appears that the CEO and CFO made all decisions on their own with no input from the board.

No processes were in place that assessed the quality of operating system performance over time, management was responsible for overseeing the integrity of data, and in this case, it appears that VBS management failed to provide oversight.

Theme E: Non-compliance with regulatory requirements

Irregular transactions: Very large loan amounts were given to certain individuals without requisite approvals. Large amounts of loans in terms of contract finance and overdraft facilities were given to individuals without obtaining proper credit approval. The data indicates that risk committees responsible for making lending decisions did not convene frequently, and large loans amount were approved under the sole authority of the CEO, CFO, and the chair of the board in staggered small amounts that would not require approval of the Reserve Bank.

It appears that the bank started operating beyond its operating license limitations and abandoned its operational strategy of relying on small retail deposits and burial societies. The bank adopted a new strategy of obtaining very large, short-term deposits from municipalities as well as adopting non-conservative lending practices that attracted far more ambitious and potentially lucrative markets to give loans. However, this strategy was not consistent with the regulations that govern mutual banks. To maintain these irregular transactions, the senior management of the bank associated themselves with politically connected individuals to pressurise municipalities into investing with the mutual bank.

Theme F: Irregular financial management

Fraud: The bank's management and members of the board engaged in irregular financial conduct and paid bribes to buy people's silence and ignore the fraudulent activities that were taking place at the bank. The bank's management colluded on how to manipulate the banking system to create (suspense accounts) fraudulent transactions/ deposits that did not exist.

Theme G: Non-inclusive stakeholder relations

Stakeholders' non-inclusivity: There is no evidence indicating that the bank solicited feedback from stakeholders such as customers, industry regulators, and other affected parties for risk identification. The bank did not have integrated reports, subsequently; key stakeholders were left in the dark about the operations of the bank.

The statements lacked integrity; therefore, reports did not allow key stakeholders to assess the true reflection of the bank. The reports lacked integrity and legitimacy towards interest, reasonable needs, and expectations of the stakeholders. The reports lacked integrity and relevance towards the risk disclosure to stakeholders.

Findings on the three lines of defence

The three lines of defence model is a framework that has been accepted in the financial sector as an effective tool for operational risk management. The three lines of defence model matrix for the banks are indicated in Table 5 below to provide an overview of how the banks adhered to the model which is one of the frameworks that has been adopted and used in various business sectors to address operational risks (Luburić, 2017).

The table indicates the line of defence and the type of control that the bank had for each line of defence. Furthermore, the table outlines the areas where the type of control was applied or/and effective or the control was not applied or/and not effective. The table is populated as per the statements drawn from African Bank and VBS reports.

Below is the guide for reading and interpreting the table.

Not applied - the identified type of control was not available/applied at the bank.

Applied - the identified type of controls was available/applied.

Not effective – even though the controls were available/applied, they were not effective.

Effective – indicates that controls were available/applied and effective as indicated in the table.

Table 5. Three lines of defence model matrix

AFRICAN BANK				VBS	
Lines of Defence	**Type of Control**	**Applied and Effective**	**Not Applied/ Not Effective**	**Applied and Effective**	**Not Applied/ Not Effective**
First Line	Management Controls	**Applied:** The bank had a specialist that was responsible for credit risks specifically within the credit department (African Bank, 2015).	**Not effective:** The CRO was not qualified to take up risk management responsibilities (Myburgh, 2016).	**Applied:** The bank had structures with clear roles and responsibilities as well as qualified managers to identify risks (VBS, 2018).	**Not applied**
			Not applied: No evidence of how the bank identified, assessed, responded to, and monitored the risks.	**Not applied**	**Not applied**
	Internal Controls	**Not applied**	**Not applied:** No risk management policy and procedures were identified at ABIL.	**Applied:** The board approved a risk management framework that the bank should operate. The framework demarcated risk limits, delegation, and levels of authority that were further incorporated within a comprehensive operational procedure.	**Not effective:** Risk committees that were to make lending decisions rarely convened, and large loans amount were approved on the sole authority of the CEO, CFO, and the chair of the board.

AFRICAN BANK					VBS	
Lines of Defence	**Type of Control**	**Applied and Effective**	**Not Applied/ Not Effective**		**Applied and Effective**	**Not Applied/ Not Effective**
First Line	Internal control measures (continued)	**Not applied**	**Not applied:** In 2012, management failed to adopt a more conservative write-off policy, for loan accounts that received no payments for more than 12 months.		**Not applied**	**Not effective:** Statements of accounts were manually generated instead of using the bank's central operation systems. The contract finance book was on excel spread sheets rather than the bank's operation system, meaning that no automatic reports could be generated to identify loans and other facilities that were not serviced by the borrowers.
Second Line	Financial Controller	**Applied:** Given that the bank was fined by the National Credit Regulator (NCR) for allegations of reckless landing in the Dundee branch, the branch systems were changed from the Phoenix system to the Gazelle system to reduce	**Not effective**: The credit underwriting model of the bank was not forward-looking as it assessed affordability and did not factor in any potential economic or business external environment changes.		**Not applied**	**Not effective:** Financial records were misrepresented to mislead the Prudential Authority into believing that the bank was performing well.

		the challenges if they cannot eliminate them.				

AFRICAN BANK					VBS	
Lines of Defence	**Type of Control**	**Applied and Effective**	**Not Applied/ Not Effective**		**Applied and Effective**	**Not Applied/ Not Effective**
Second Line	Security	**Applied:** African Bank implemented biometric systems for segregation of access to documents and other preventative actions.	**Not effective**: Staff did not entirely comply with the supervisory and risk control measures of the bank. Management continued to allow authorisation of unsecured second loans to customers who had outstanding amounts on their previous loans and failed to write off those loans that had fallen behind in repayments for over 12 months.		**Not applied**	**Not applied**
	Risk Management	**Applied** The bank kept the operational risk capital floor at 12 % as per the Basic Indicator Approach (BIA) standards. This was consistent with Capital Bank as one of the unsecured lending competitors.	**Not effective:** The bank had poor detection of early warning signs of operational risks.		**Not applied**	**Not applied:** There is no identified risk guidance and risk management training that could have served as a centre of excellence for specified risks in the organisation.

AFRICAN BANK					VBS	
Lines of Defence	**Type of Control**	**Applied and Effective**	**Not Applied/ Not Effective**		**Applied and Effective**	**Not Applied/ Not Effective**
Third Line	Compliance	**Applied:** ABIL had a compliance committee. The bank's complaints (especially of reckless lending) would be escalated to a legal unit within the compliance department to be attended to.	**Not effective:** The bank's accounting practice did not comply with the requirements of IAS39 regarding the cash flow to accounts that had reached duplum status. These accounts should have been discounted to the original effective rate, instead the bank discounted them to zero which was against industry practice.		**Not applied**	**Not applied**
	Internal Audit	**Applied:** The audit committee communicated the results of the audit reviews by preparing reports that included recommendations for notifications of management practices, fiscal policies, and accounting procedures as justified by audit findings.	**Not effective:** African Bank Internal audit failed to flag the financial difficulties that the bank was going through until the independent auditor raised concerns regarding the decline in the bank book and the risks associated with it.		**Applied:** The bank's Risk and Audit committees met quarterly to review and assess the risk levels of the bank in line with the committee's charter and terms of reference. The audit committee communicated the results of the audit reviews by preparing reports and	**Not applied:** VBS did not have an internal audit function. The bank appointed KPMG to carry out the functions of the internal audit.

					financial statements for approval by the board of directors.	

AFRICAN BANK					VBS	
Lines of Defence	**Type of Control**	**Applied and Effective**	**Not Applied/ Not Effective**		**Applied and Effective**	**Not Applied/ Not Effective**
Third Line	External Audit	**Applied** Deloitte gave an unqualified audit opinion to ABIL for the 2013 financial year. Additionally, Deloitte indicated to the bank in 2013 that unless the bank increases its impairment provisioning significantly, the firm would be left with no choice but to modify its audit opinion to the effect that the advances were overstated during the 2012/13 financial year. For a number of years, Deloitte had advised	**Not applied**		**Applied:** The bank's risk and audit committees met quarterly to review and assess the risk levels of the bank in line with the committee's charter and terms of reference. The audit committee communicated the results of the audit reviews by preparing reports and financial statements for approval by the board of directors.	**Not applied:** VBS did not have an internal audit function. The bank appointed KPMG to carry out the functions of the internal audit.

		management and the board of directors that the adopted practice of reducing the effective interest rates of NPL portfolios, which were in duplum to 0%, did not comply with the IAS39. Furthermore, Deloitte had advised that the management's impairment event of CD4 should be CD1 as CD4 was not prudent.				

AFRICAN BANK					**VBS**	
Lines of Defence	**Type of Control**	**Applied and Effective**	**Not Applied/ Not Effective**		**Applied and Effective**	**Not Applied/ Not Effective**
Third Line	Regulator	**Applied:** The Governor of the South African Reserve Bank (SARB) placed the bank under curatorship in 2014. The concerns leading to this decision were the bank's liquidity, impairment,	**Not applied**		**Applied:** The Governor of the South African Reserve Bank (SARB) placed the bank under curatorship in March 2018 and eventually liquidated the bank in November 2018.	**Not applied**

		provisioning policy, rapid credit worth as well as the need for a strategic rethink of the bank's business model.				

Source: Own Formulation

The table above outlines all the types of controls within the three lines of defence. More importantly, at the first level, the table explains whether the controls were applied, and secondly, it explains the effectiveness of each of the controls that were outlined. This was crucial in demonstrating what controls were in place in each of the banks and the level of effectiveness thereof.

In both banks, two types of controls were identified in the **first line of defence**; these include management control and internal controls as indicated in the above table. For the African Bank management controls were applied, however, the risk controls were not effective. This was because African Bank did not have a qualified CRO to ensure that risk management controls were in place and effective (Myburgh, 2016). The internal controls were not in place and not identified in the analysed documents. Thus, internal controls were not applied.

In the case of VBS, management controls were applied and effective. The bank had risk management structures with clear roles and responsibilities as well as qualified managers (VBS, 2016). In terms of internal controls, these were applied but were not effective. The board approved the risk management frameworks that demarcated risk limits and levels of authority. However, these risk frameworks were not implemented since the committees that were to implement the framework rarely convened (Motau, 2018).

The **second line of defence** consists of four (4) types of controls, i.e. financial control, security, risk management and quality were assessed for both banks. For African Bank, financial controls were applied but were not effective. The bank's credit underwriting model was not forward-looking and did not factor in any potential economic and external environmental changes (Myburgh, 2016). On the other hand, VBS bank's financial controls were not applied.

In terms of security, African Bank applied security controls but they were not effective. The African Bank staff did not comply with the security controls put in place, and management continued to allow the authorisation of further loans to already over-indebted customers (Myburgh, 2016). VBS on the other hand did not have any security controls that were identified when analysing data.

Risk management controls were applied at African Bank by keeping the operational risk capital floor at 12%, which is consistent with other unsecured lending banks such as Capitec (African Bank, 2015); however, these controls were not effective. Management did not ensure the effective detection of early warning signs of operational risks (Myburgh, 2016). VBS on the other hand did not apply any risk management controls.

Lastly, quality control was not applied at both banks.

The **third line of defence** focused on four (4) types of control, namely compliance, internal audit, external audit and regulator. In terms of compliance, African Bank had a compliance team whilst VBS did not. African Bank's compliance team would escalate bank's complaints to legal services for attention (Myburgh, 2016). However, the bank was still not compliant with accounting requirements, which further landed the bank in trouble.

Internal audit controls were applied at African Bank; however, these controls were not effective as the bank's internal audit failed to flag the financial difficulties faced by the bank until the independent auditor raised concerns regarding the decline in the bank book and the risks associated with it (Myburgh, 2016). VBS on the other hand did not apply any internal audit controls.

In terms of external audits, both African Bank and VBS applied this risk control. African Bank's external auditor was Deloitte, the external auditor advised the board and management regularly and advised the bank's management on the debt impairment issues that the bank faced (Myburgh, 2016). Similarly, VBS's external auditor was KPMG (VBS, 2016). Even though the audit partner was colluding with the bank's management, the audit committee met quarterly and communicated the audit reviews to the board of directors (Motau, 2018).

Finally, the South African Reserve Bank placed both banks under curatorship at different times. African Bank was placed under curatorship in 2014 while VBS was placed under curatorship in 2018. Fortunately for African Bank, the bank could be saved by splitting it into bad bank and good bank, which later managed to become financially viable until now (African Bank, 2015). VBS, on the other hand, was later liquidated in November 2018 (VBS, 2018), and many customers lost their money with the collapse of the bank.

All the above findings are discussed in the following chapter. Each finding is discussed following a compare and contrast approach, with an explanation provided for both African Bank and VBS.

CHAPTER 5: DISCUSSION OF FINDINGS

5.1. Introduction

This chapter discusses the findings of the study in line with the research objectives and literature review. As highlighted in the preceding chapters, the purpose of the study was to analyse the contributing factors to the failures of VBS and African Bank and the impact it had on their key stakeholders. The objectives were to (i) evaluate African Bank and VBS Bank's operational risk management process and controls, (ii) evaluate the role of ethical failures at African Bank and VBS, as well as (iii) assess how African Bank and VBS failures affected their stakeholders.

5.2. Discussion of the findings

5.2.1. Lack of leadership commitment to governance

This theme highlights the issues that are relevant to the lack of leadership commitment to governance at both banks (Myburgh, 2016; Motau, 2018). According to IoDSA (2016, p.20), corporate governance is *"the exercise of ethical and effective leadership by the governing body towards the achievement of ethical culture, good performance, effective control, and legitimacy".*

Both banks embraced the governance principles as set out in the King Code of good corporate governance to ensure that an ethical foundation exists and promotes responsibility, accountability, fairness, and transparency in the banks. Furthermore, both banks did not practically execute internal audits and continuous activities that ensure effective corporate governance, risk management, and compliance (Myburgh, 2016).

When the African Bank started providing financial assistance to the Ellerines retail business, the board of directors were conflicted and failed to make decisions that were focused only on African Bank, thus breaching their fiduciary duties to the bank (Myburgh, 2016). On the other hand, the executive management of VBS encouraged the board of directors to turn a blind eye towards the unlawful conduct of the CEO, CFO, and chairperson of the board (Motau, 2016).

Therefore, both banks embraced the King Code of good governance principles, and both failed to execute internal audits. There were contrasting approaches about the effectiveness of the two companies' board of directors. The African Bank board failed to make effective decisions and the VBS board of directors completely neglected their responsibilities.

5.2.2. Lack of ethical leadership and poor consequence management

Basel Committee on Banking Supervision (2011) argues that establishing policies such as a code of conduct and ethics policy that sets clear expectations of ethical values and integrity will enable and ensure that employees know and understand their roles and responsibilities as well as their authority to act in an event where risks occur. Furthermore, principle 2 of King code IV highlights the need for the governing body to govern organisational ethics in a way that supports the establishment of ethical culture (IoDSA, 2016).

Both banks did not indicate the availability of the code of conduct in their institution. In the case of African bank, the unavailability of the code of conduct led to the inability of executive management to take any decisive consequence management. This practice continued even after being warned about the liquidity crisis the bank was heading for (African Bank, 2015). In the case of VBS, the unavailability of the code of conduct led to the executive management using the bank's financial resources to pay off certain individuals within the bank to silence them so that they do not report unlawful transactions that took place (Motau, 2016).

Similarly, both banks did not have an indication of the code of ethics in place or ethical guidance. The banks staff and management up to the level of CEO and the board were not guided on matters of ethics and the desired culture of the organisation (Myburgh, 2016; Motau, 2018). This is inconsistent with principle 2 of King IV (IoDSA, 2016) stated above. This inconsistency is displayed in management's failure to take meaningful actions and commitments that would raise ethical standards in both banks (Ogbo, Okechukwu, and Ukpere, 2013).

According to Green (1989), every organisation has an ethical responsibility, its record and perception of its ethics can affect the reputation of the organisation, which will determine the long-term success or failure of that organisation. While African Bank senior management was expected to carry out their responsibilities to take action against those involved in wrongdoing as part of enforcing good governance and conduct in the organisation, no action was taken (Myburgh, 2016) This lack of consequence management resulted in a culture of deliberate non-compliance by the bank staff, knowing that there will be no action taken against them.

Similarly, VBS management deliberately overlooked discrepancies and integrity between the published financial statements and the actual financial state of the bank (Motau, 2018). The bank's senior management and the board were expected to take action against those involved in wrongdoing as part of enforcing good governance and conduct in the organisation, instead, all the wrongdoing was concealed, and no action was taken.

Both banks did not take ethical issues seriously, as they did not have clear ethical guidelines in place. Both banks failed to enforce good governance and conduct in their organisations.

According to Khang (2005), the key component to achieving the best ethical organisations is the leadership that is made visible through its actions and commitment to ethical practices, as well as setting the moral tone from the top and translating ethical principles into the behaviour that is expected from every person acting on behalf of the organisation. It is clear from the findings that both banks failed to govern organisational ethics in a way that supports ethical culture establishment in the banks. Unlike African Bank, VBS's leadership intentionally ignored practising good business ethics and lost their moral compass to ensure good ethical culture at the bank.

5.2.3. Weak internal risk controls

Internal controls should provide for the safeguarding of assets, and proper recording of transactions as well as the effective and efficient running of the banks (BCBC, 2011). Internal controls are essential in ensuring that the organisation can meet its strategic objectives (IoDSA, 2016). According to Anderson and Eubanks (2013), effective control systems should consist of a controlled environment, risk assessments, control activities, information and communication as well as monitoring and assurance components.

For a *control environment*, management and the board are charged with taking lead in establishing a strong and sound risk management and corporate culture that is guided by strong risk management throughout the organisation amongst other components (BCBS, 2011). The findings indicated that both banks failed to establish a strong and sound control environment where risk management and corporate governance culture could be embedded at all levels of the organisation. In the case of the African Bank, the bank appointed an unqualified Chief Risk Office who held the position for over 10 years. This is contrary to the banking industry norm of appointing well-qualified and experienced people to occupy this position (Donnelly, 2016).

In the case of VBS, even though the bank had governance structures, these structures were ineffective to the extent that they never convened any meetings. The CEO, CFO, and board chairperson took all decisions exclusively (Motau, 2018). Some of the decisions that were taken by the above mentioned small group of people were not in the interest of achieving the bank's objectives, instead, they served the individual objectives of this small group and resulted in looting (Motau, 2016).

The board of directors for both banks failed to establish a strong and sound risk management and corporate culture that is guided by strong risk management throughout the organisation among other components.

Anderson and Eubanks (2013) highlight that the effective *risk assessment* process assists the organisation to determine potential risks, controls needed, and how the risk should be managed to mitigate the potential negative impact on the organisation's operation. In addition, *risk assessment* involves the identification, measurement, and analysis of risks that may arise because of controllable/uncontrollable activities.

Both African Bank and VBS had risk management committees whose role was to assist the board in ensuring the quality, integrity and reliability of risk management processes at both banks (Myburgh, 2016; Motau, 2018). At African Bank, there was no consistency in risk assessment measures. This is displayed in the failure to write off non-performing loans on time. Consequently, this left the bank exposed to various risks in the long term that eventually led to the near collapse of the African Bank (Myburgh, 2016).

On the other hand, VBS risk management structures were ineffective, management instead misrepresented the true state of the bank in its financial statement and annual report (Motau, 2018). This misrepresentation prevented stakeholders from determining the true state of risk levels in the bank.

BCBS (2011) emphasises the importance of having strong *control activities* that provide reasonable assurance and ensures that the bank has efficient and effective operations, reliable financial reports, and compliance with applicable regulations and laws governing them. The findings indicate that both African Bank and VBS failed to comply with international standards of accounting practices. VBS failed to comply with the requirements of the bank's audit team, African Bank adopted a relaxed bad debt write-off policy in 2012 (Myburgh, 2016). Moreover, African Bank adopted a debt impairment point of CD4, which was way above the industry standards for a nonsecure lending space (Myburgh, 2016). This led to the bank having an unmanageable credit book, which became the most contributing factor to the bank's near collapse (Myburgh, 2016).

Meanwhile, at VBS the CFO, and CEO, colluded with the lead audit partner, and this created grounds for the CEO and CFO to disregard the requirements of the audit team. This collusion escalated to the concealing of unreconcilable financial accounts of the bank (Motau, 2016). Subsequently, the presented financial statements were overstated in the annual reports of the 2017 financial year.

According to Anderson and Eubanks (2013), a*udit, monitoring, and assurance* include the need to carry out internal audits and continuous activities that ensure effective corporate governance, risk management, and compliance are implemented. Both African Bank and VBS used the services of an external auditor to perform independent audits to provide an objective assurance that will add value to the bank's operations (Myburgh, 2016; Motau, 2016). Deloitte audited African Bank and KPMG VBS. Both banks failed to carry out internal audits and continuous activities that would have ensured effective corporate governance, risk management and compliance.

In the case of African Bank, the bank failed to act on the risk and compliance warnings presented in Deloitte's external audit report for the financial year 2013 (Myburgh, 2016). For several years, Deloitte had advised executive management and the board of directors, that the adopted practice of reducing the effective interest rates of NPL portfolios which were in duplum to 0% did not comply with the IAS39 (Myburgh, 2016).

On the other hand, VBS management failed to coordinate, facilitate, and monitor the effective execution of defence activities established in the first line of defence risk review. Furthermore, VBS accepted the external auditor's report indicating that the audit report for 2017 and its financial performance and cash flows were in line with IFRS and met the requirements of the Mutual Banks Act (VBS, 2016) while this was incorrect. This statement was incorrect given that the lead audit partner was aware of the books not reconciling, and instead opted to conceal this information (Motau, 2018). The findings of the study revealed that the external auditors may have overlooked and intentionally failed to report fraudulent activities that were taking place at the bank (Motau, 2018). Even though the audit committee existed, there is no evidence that the committee discharged its duties of ensuring the integrity of financial controls, integrated reporting as well as identifying and managing financial risks (Motau, 2018).

Even though external auditors were appointed as the designated auditors for both banks and had full independence when auditing the banks, it would have been beneficial to have an internal auditing function for adequate risk control measures. This would have enabled the implementation of internal audits and continuous activities that ensure effective corporate governance, risk management, and compliance are implemented. Perhaps the near collapse of the African Bank and the collapse of VBS could have been prevented.

5.2.4. Ineffective leadership structures

According to IoDSA (2016 p.49), *“the governing body should serve as the focal point and custodian of corporate governance in the organisation."* The board and management should exercise leadership in ensuring that there is oversight, monitoring of implementation and execution of risk management, as well as accountability for organisational performance using reporting and disclosure (IoDSA, 2016).

Both African Bank and VBS had the required risk committees in place for reporting to the board and ensuring accountability by both management and staff (Myburgh, 2016; Motau, 2018). However, these committees became ineffective, and subsequently, staff and management were not held accountable (Myburgh, 2016; Motau, 2018). In the case of African Bank, the board of directors and executive management allowed themselves to be dominated by the founding CEO of the bank who took most of the decisions (Myburgh, 2016). The CEO’s leadership was associated with unwillingness to take advice or align the bank’s impairments practices with the rest of the local banking industry (Myburgh, 2016). Thus, management could not take accountability for the decision made, even when the National Credit Regulator (NCR) made damning findings regarding reckless lending by the bank, management did not take any action or accountability (Myburgh, 2016).

Different from African Bank, VBS management intentionally took decisions to approve loan amounts below the threshold of the Mutual Banks to avoid accountability to the South African Reserve Bank (SARB), which is the financial sector regulator (Motau, 2018). During these transactions, management failed to take any accountability for their unethical actions, instead, they rewarded themselves with payments whilst the bank was sinking into a liquidity crisis (Motau, 2018).

Therefore, both banks failed to ensure that leadership structures are effective and members of the committees, the staff and management take accountability for organisational performance.

In terms of ensuring oversight, both banks had a board of directors that met regularly as indicated in the bank's annual reports (African Bank, 2015; VBS, 2016). It is stated that the board of ABIL (the holding company for the African Bank) was the same as the African bank. This resulted in a conflict of interest in terms of the director’s fiduciary duties (Myburgh, 2016). In addition, executive management supported the CEO’s decisions even though they did not agree with his views, they allowed themselves to be dominated by the CEO (Myburgh, 2016).

This made it impractical to ensure that the bank continues to remain a sound institution while being exposed to the risks of group companies. Moreover, it became difficult for the board to provide oversight as their views were not taken into consideration because of the domination of the CEO's views (Myburgh, 2016).

In the case of VBS, the executive management was expected to provide oversight for transactions that were taking place at the bank, it appears that management participated in colluding with staff to create fictitious transactions to reflect on the bank's financial reports (Motau, 2018). Similar to African Bank, the CEO and CFO made all decisions on their own with no input from the board (Motau, 2018).

Therefore, it can be concluded that both banks' executive management failed to execute their leadership responsibilities of providing accountability and oversight as well as monitoring the implementation and execution of risk management (IoDSA, 2016).

5.2.5. Non-compliance to regulatory requirements

Principle 13 of King code IV puts the responsibility on the governing body to govern compliance with applicable laws, codes, and standards that supports the organisation to be an ethical and good corporate citizen (IoDSA, 2016).

Both banks failed to comply with the set regulatory requirements. African Bank's accounting practice did not comply with the requirements of IAS39 regarding the cash flow to accounts that had reached the in duplum status (Myburgh, 2016). According to the accounting standards, these accounts should have been discounted to the original effective rate, instead the bank discounted them to zero (Myburgh, 2016). This was a deviation from the market practice relating to the definition of "default" and NPL write-offs. Therefore, the failures in the bank's risk frameworks resulted in non-compliance with the National Credit Regulator (NCR).

On the other hand, at VBS large loans in terms of contract finance and overdraft facilities were given to individuals without obtaining proper credit approval (Motau, 2018). The risk committees responsible for making lending decisions rarely convened, and large loan amounts were approved under the sole authority of the CEO, CFO, and the chair of the board (Motau, 2018). These transactions were carried out in staggered small amounts that would not require the approval of the Reserve Bank (Motau, 2018). According to the Companies Act section 45(3), (b), *"the board of directors may not authorise any financial assistance unless the board is satisfied that immediately after providing the financial assistance, the company would satisfy the liquidity and solvency test".* It is clear that in the case of VBS, there were blatant irregular activities.

Therefore, it can be concluded that the board of directors and management of both banks failed to govern the banks into complying with applicable laws and standards that support the organisation to be an ethical and good corporate citizen.

5.2.6. Irregular financial management

In 2011, the NCR fined African Bank for adverse findings of reckless lending at their Dundee branch (African Bank, 2015). This was caused by the manipulation of bank IT and Phoenix systems to allow repeat customers to be granted new loans without settling existing loans. According to Myburgh (2016), bank operations were conducted recklessly by making loans to Ellerines's already financially overcommitted customers with no reasonable prospect of the loans being repaid. The findings of this study indicated that African Bank underestimated the financial implications of bad debts and impairment. The same can be said about the ignorance towards the cost of funding Ellerines, and the risk of the market losing confidence in the bank as well as funders failing to continue to support the bank (Myburgh 2016). Therefore, the bank acted recklessly in underestimating these financial issues.

VBS executive management and members of the board engaged in irregular financial conduct by paying bribes to buy people's silence and ignore the fraudulent activities that were taking place at the bank (Motau, 2018). The bank's executive management colluded in manipulating the banking system to create (suspense accounts) fraudulent transactions/ deposits that did not exist (Motau, 2018). According to Motau (2016), the CFO admitted to having committed fraud in the preparation of the 2017 financial statements, and the chairman of the board and CEO were aware of this manipulation. The aforementioned fraudulent activities misled the Registrar of SARB into believing that the bank was financially sound whereas its liabilities exceeded assets and the bank was hopelessly insolvent in 2017.

5.2.7. Stakeholder non-inclusivity

The King code of good corporate governance advocates for stakeholder inclusivity wherein the governing body should take into account the legitimate and reasonable needs, interests, and expectations of all material stakeholders (IoDSA, 2016).

Both banks had stakeholders; however, there is no clear evidence of how banks achieved stakeholder inclusivity. In addition, the banks produced reports annually. African Bank published integrated reports (African Bank, 2015), while VBS published annual reports (VBS, 2016). Both these reports lacked integrity and reliability (Myburgh, 2016; Motau, 2016).

African Bank investors and shareholders always believed the integrated reports published annually until 2013 when the information on higher levels of NPLs that was not disclosed to them during their meetings with the bank were published (Myburgh, 2016). This was the period when African Bank's financial challenges began to surface. According to Myburgh (2016), some investors and shareholders stopped rolling over their shares once they realised the poor financial state of the bank in the 2012/13 financial year (Myburgh, 2016). This indicates that the bank did not have transparent disclosures about its operations to the stakeholders. Therefore, African Bank failed to provide and publish credible financial and integrated reports required by stakeholders to make informed decisions based on the risk status at the bank (Myburgh, 2016).

VBS on the other hand did not have integrated reports and the financial statements on the annual reports were not credible (Motau, 2016). Subsequently, key stakeholders were left in the dark about the operations of the bank. According to IoDSA (2016), the inclusive stakeholder approach ensures that the interest and expectations of stakeholders are considered whilst decisions are taken in the best interest of an organisation. It was never going to be possible for VBS to achieve stakeholder inclusivity under the circumstances discussed above.

Thus, the bank's board failed to adopt a stakeholder inclusive approach that balances the stakeholder needs, interests, and expectations as well as the best interest of the organisation as outlined in proposition 1 of the study (IoDSA, 2016).

5.3. Conclusion

This chapter presented the findings of the study, which were gathered using qualitative methods using document analysis. These findings highlight the risk management structures at African Bank and VBS, as well as the ineffectiveness of their risk management structures. In some instances, internal control functions were non-existent, coupled with collusion at executive management and board level to facilitate irregular transactions.

CHAPTER 6: CONCLUSION AND RECOMMENDATIONS

6.1. Introduction

This chapter presents a summary of the findings. The chapter further acknowledges the limitations, highlights the contribution of the study and provides some recommendations to the banking industry and the body of knowledge.

6.2. Summary of findings

The study aimed to analyse the contributing factors to the failures of VBS and the African Bank and the impact it had on their key stakeholders. This was done by analysing the integrated and annual reports, as well as the investigative reports for both banks and extracting statements that related to the operational risk controls, ethical conduct, and stakeholder inclusivity at African Bank and VBS Mutual Bank as this study mainly focused on those areas.

The findings from these studies revealed that there were ineffective risk controls in both banks and some instances a total collapse in risk control structures. There is an indication that unethical business practices became embedded in some of the operational activities due to a lack of ethical leadership guidance. The overbearing behaviour and influence of CEOs of the banks led to an ineffective and submissive board of directors that followed directives of the executive management and subsequently resulted in non-accountability for management. The irregular conduct of doing business became a norm; an example is VBS's failure to comply with Mutual Banks Act and the acceptance of deposits from various municipalities (Motau, 2018). The study found that there were non-disclosure issues. Although the banks produced annual integrated reports and held meetings with major stakeholders, they failed to consult and disclose to stakeholders the major changes and decisions taken. In the case of the African Bank, this failure of disclosure caused some of the investors to pull out their investment in the bank (Myburgh, 2016).

The inability of the African Bank and VBS board of directors to execute risk management and compliance responsibilities indicates the bank's failure in ensuring that good corporate governance is maintained. This failure is evident in both banks as discussed in the findings chapter of this particular study. The wrongdoings at VBS were encouraged by the lack of consequence management, resulting in a culture of non-accountability for employees engaging in irregular activities. There are indications of deliberate intention by VBS executive management to conceal information and defraud the bank of its financial assets, which was later referred to as 'looting'. It is clear from the findings that the banks, particularly VBS's leadership intentionally ignored practising good business ethics and lost their moral compass to ensure good ethical culture at the bank. Motau (2018) attributes this to the lack of a code of conduct and code of ethics in the organisation.

The weak risk management structures exacerbated the lack of risk management controls. In the case of African Bank, the overbearing founding CEO resulted in an ineffective board of directors. At VBS, the executive management went as far as colluding with the auditing partner resulting in intentionally overstated financial statements. All these weaknesses ultimately eroded the effectiveness of risk management structures that were meant to provide oversight and enforce risk controls in these organisations. This lack of oversight is highlighted by the approval of loans at VBS without following the approval hierarchy (Motau, 2018).

It is evident that several operational activities at VBS were unethical, the African Bank case highlights a lack of internal controls and lack of accountability. This is important in illustrating that the contributing factors to the operational challenges ultimately experienced by both banks had different root causes. The contributing factors to the near collapse of the African Bank were weak controls, ineffective risk management structures, and a disempowered board due to the dominant influence of the CEO. VBS was affected by a lack of ethical leadership, intentional wrongdoing, and collusion in facilitating irregular transactions at the staff and management level including the board of directors. In the VBS case study, the senior auditing partner who was supposed to be the key risk management and control structure responsible for protecting both the organisation and key stakeholders further assisted this. The ultimate result of collapsing internal controls was the collapse of VBS as announced by the Governor of the Reserve Bank in 2018.

This study concludes that the circumstances at African bank and VBS could have been avoided had the organisations effectively implemented risk management controls, codes of conduct, ethical guidelines, and good corporate governance. All these failures were exacerbated by a lack of leadership guidance from the senior leadership structures of the organisation, which subsequently sets the tone for a distractive culture at multiple layers of the organisation.

6.3. Recommendations

Recommendations are made concerning the following areas:

6.3.1. To the banking industry:

The industry controlling structures should make a code of ethics compulsory for all industry participants, to drive an ethical culture in the entire industry.

The JSE should consistently enforce corrective measures for listed companies that transgress during their financial year for individual companies to be more responsible in their actions.

The banking industry should make it compulsory to produce integrated reports for any bank that requires licensing, operating license renewals, and access to capital funding.

6.3.2. To the banking industry regulator

The regulator should increase the number of inspections and tax incentives for organisations that meets regulatory requirements.

There should be financial relief penalties charged against organisations who bridge the regulations to financially compensate the affected vulnerable stakeholders such as the village communities in the case of mutual banks.

The regulator should not only focus on monetary fines but operating license suspension for non-compliant organisations.

The regulator should blacklist executives involved in irregular financial management from participating in future industry business dealings.

6.3.3. To the body of knowledge

To add to the data included in the available data at the time of data collection from both African Bank and VBS. The paper acknowledges that accessing internal information might be a challenge for future researchers on this topic; however, the availability of such data would further enrich the findings of future studies.

6.4. Limitations

Several limitations were encountered when conducting this study. These limitations include.

(i) Data collection was mainly based on secondary data, this included integrated annual reports and investigative reports on both African Bank and VBS bank. Subsequently, the limitations of using secondary data apply to the research and the analysis undertaken. This includes the fact that some organisations limit their disclosure for various reasons.

(ii) The study applied a deductive approach. If the study had been conducted inductively, more themes would have been explored and included in the study to bring further clarity on the events of both banks' failure.

6.5. Conclusion

This chapter presented an overview of the research and its findings. The findings revealed that the contributing factors to the near collapse of African Bank were due to weak internal controls, whereas VBS mutual bank collapsed because it lacked ethical leadership. These events had serious impacts on the banks stakeholders especially that of VBS bank as most stokvel groups and individuals lost their savings because of the bank being liquidated.

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8. LIST OF ANNEXURES

Annexure 1: King Code Principles on Corporate Governance

Principles	*Description*
Principle 1	The governing body should lead ethically and effectively
Principle 2	The governing body should govern the ethics of the organisation in a way that supports the establishment of an ethical culture.
Principle 3	The governing body should ensure that the organization is and seen to be a responsible corporate citizen.
Principle 4	The governing body should appreciate that the organisation's core purpose, its risks and opportunities, strategy, business model, performance, and sustainable development are all inseparable elements of the value creation process.
Principle 5	The governing body should ensure that reports issued by the organisation enable stakeholders to make informed assessments of the organisation's performance and it's short-, medium- and long-term prospects.
Principle 6	The governing body should serve as the focal point and custodian of corporate governance in the organisation.
Principle 7	The governing body should comprise the appropriate balance of knowledge, skills, experience, diversity, and independence for it to discharge its governance role and responsibilities objectively and effectively.
Principle 8	The governing body should ensure that its arrangements for delegation within its own structures promote independent judgment and assist with the balance of power and the effective discharge of its duties.
Principles 9	The governing body should ensure that the evaluation of its own performance and that of its

	committees, its chair, and its individual members, support continued improvement in its performance and effectiveness.
Principle 10	The governing body should ensure that the appointment of, and delegation to, management contributes to role clarity and the effective exercise of authority and responsibilities.
Principle 11	The governing body should govern risk in a way that supports the organisation in setting and achieving its strategic objectives.
Principle 12	The governing body should govern technology and information in a way that supports the organisation setting and achieving its strategic objectives.
Principle 13	The governing body should govern compliance with applicable laws and adopted, non-binding rules, codes and standards in a way that supports the organisation being ethical and a good corporate citizen.
Principle 14	The governing body should ensure that the organisation remunerates fairly, responsibly and transparently so as to promote the achievement of strategic objectives and positive outcomes in the short, medium and long term.
Principle 15	The governing body should ensure that assurance services and functions enable an effective control environment, and that these support the integrity of information for internal decision-making and of the organisation's external reports.
Principle 16	In the execution of its governance role and responsibilities, the governing body should adopt a stakeholder inclusive approach that balances the needs, interests and expectations of material stakeholders in the best interests of organisation over time.
Principle 17	The governing body of an institutional investor organisation should ensure that responsible investment is practiced by the organisation to promote the good governance and the creation of value by the companies which it invests.

Annexure 2: Basel Commission Fundamental Principles of Operational Risk Management.

Principles	Description
Principle 1	The board of directors should take the lead in establishing a strong risk management culture. The board of directors and senior management should establish a corporate culture that is guided by strong risk management and that supports and provides appropriate standards and incentives for professional and responsible behaviour. In this regard, it is the responsibility of the board of directors to ensure that a strong operational risk management culture exists throughout the whole organisation.
Principle 2	Banks should develop, implement and maintain a Framework that is fully integrated into the bank's overall risk management processes. The Framework for operational risk management chosen by an individual bank will depend on a range of factors, including its nature, size, complexity, and risk profile.
Principle 3	The board of directors should establish, approve and periodically review the Framework. The board of directors should oversee senior management to ensure that the policies, processes, and systems are implemented effectively at all decision levels.
Principle 4	The board of directors should approve and review a risk appetite and tolerance statement for operational risk that articulates the nature, types, and levels of operational risk that the bank is willing to assume.
Principle 5	Senior management should develop for approval by the board of directors a clear, effective, and robust governance structure with well-defined, transparent, and consistent lines of responsibility. Senior management is responsible for consistently implementing and maintaining throughout the organisation policies, processes, and systems for managing operational risk in all

	of the bank's material products, activities, processes, and systems consistent with the risk appetite and tolerance.
Principle 6	Senior management should ensure the identification and assessment of the operational risk inherent in all material products, activities, processes, and systems to make sure the inherent risks and incentives are well understood.
Principle 7	Senior management should ensure that there is an approval process for all new products, activities, processes, and systems that fully assess operational risk.
Principle 8	Senior management should implement a process to regularly monitor operational risk profiles and material exposures to losses. Appropriate reporting mechanisms should be in place at the board, senior management, and business line levels that support proactive management of operational risk.
Principle 9	Banks should have a strong control environment that utilises policies, processes, and systems; appropriate internal controls; and appropriate risk mitigation and/or transfer strategies.
Principle 10	Banks should have business resiliency and continuity plans in place to ensure an ability to operate on an ongoing basis and limit losses in the event of severe business disruption.

Annexure 3: The board of directors, committee, and members

African Bank					VBS			
Committee Name	**Members**	**Qualifications**	**Position**		**Committee Name**	**Members**	**Qualifications**	**Position**
Board Members	**Mutle Constantine Mogase,**	BCom; Executive Development Programme and graduate Diploma in Corporate Governance)	**INED** **Chairperson**		Board Members	**Mr. Tshifhiwa Matodzi**	(BCom (Accounting), BCom (Hons), CASA))	**NED** Chairperson
	Nomalizo Berly Langa-Royds	(BA Law, LLB)	**INED**			**Mr. Wilson Muvhulawa**	(Certificate Institute of Bookeepers)	**NED**
	Adv. Mojankunyane Florence Gumbi	(BPrac, LLB, Certificate in Trial Advocacy)	**INED**			**Mr. Avhashoni Ramikosi**	(BCom (Accounting), BCompt Honours (Accounting), H.Dip Tax Law, H.Dip International Tax Law, CA(SA))	**INED**
	Robert John Symmonds	(BCom (Hons), Strategic Banking Programme, Executive Development Programme)	**INED**			**Mr. Nathaniel Mudau**	**NED** (Jnr Sec Teachers Certificate)	**NED**
	Nicholas Adams	BCom (Hons), CTA, ACMA	**INED**			**Mr. Paul Magula**	(BCom, BCom(Hons)(Financial Management), Master's in development finance.	**NED**
	Morris Mthombeni	(BPrac, LLB, B Juris, MBA	**INED**			**Mr. Manelisa Mavuso**	(Bachelor of Economics)	**INED**
						Mr. Mangalani Nevhuhulwi	(BCom (IT& Risk)	**INED**
	Leon Kirkinis (resigned Aug 2014)	No Qualifications stated	**ED**			**Mr. Mbulaheni Manwadu**	(BCom (Accounting), BCom (Hons) (Financial Management), ACMA)	**NED**

						Mr. Thilivhali Ramawa	(BCom (Accounting), CA (SA)	**INED**	

African Bank				VBS			
Committee Name	**Members**	**Qualifications**	**Position**	**Committee Name**	**Members**	**Qualifications**	**Position**
Board Members	**Nithia Nalliah** (resigned Mar 2015)	No Qualifications stated	**ED**	Board Members	**Mrs. Belinda Mapongwana**	(LLB, LLM, Bachelor of Social Science)	**INED**
	Toni Fourie - ED (resigned Feb 2014)	No Qualifications stated	**ED**		**Mr. Andile Ramavhunga**	(BCom (Accounting), BCom Honours (Accounting), CA (SA))	**ED**
	Tami Sokutu (resigned Feb 2014)	No Qualifications stated	**ED**		**Mr. Ernest Nesane**	(LLB, Attorney of the High Court)	**NED**
					Mr. W.H Meyer	(BCompt (Hons), B.PI, CA (SA))	**NED**
Audit Committee	**Robert John Symmonds**	(Bcomm (Hons), Strategic Banking Programme, Executive Development Programme)	**INED** Chairperson	Audit Committee	**Mr. Avhashoni Ramikosi**	(BCom (Accounting), BCompt Honours (Accounting), H.Dip Tax Law, H.Dip International Tax Law, CA(SA))	**INED Chairperson**
					Mrs. T Ramuedzisi	MPD, MBA, BSC (Honours) Computer Science, BSC (Computer Science and Mathematics)	**NED**

	African Bank			VBS			
Committee Name	**Members**	**Qualifications**	**Position**	**Committee Name**	**Members**	**Qualifications**	**Position**
Risk and Capital Management	**Nicholas Adams**	BComm (Hons), CTA, ACMA	**INED** Chairperson		**Mr. M Mnwadu**	BCom.Honours (Financial Management), BCom (Acc), ACMA	**NED** Chaiperson
	Adv. Mojankunyane Florence Gumbi	(BPrac, LLB, Certificate in Trial Advocacy)	**INED**		**Mr. P.A Ramikosi**	B.Com(Accounting), B.Compt Honours (Accounting), H.Dip Tax Law, H.Dip International Tax Law, CA (SA	**NED**
					Mr. B.I Mapongwana,	LLB, LLM, Bachelor of Social Science	**NED**
					Mr. E Nesane	LLB, Attorney of the High Court] (PIC Representative)	**NED**
					Mr. P.T Truter	B.Com (Accounting), B.Compt (Hons)	**NED**
					Mrs. T Ramuedzisi	MPD, MBA, BSC (Honours) Computer Science, BSC (Computer Science and Mathematics)	**ED**
Ethics and sustainability	Nomalizo Beryl Langa-Royds	(BA Law, LLB)	**INED**	Ethics committee did not exist at VBS			
	Mutle Constatine Mogase						