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EMPLOYEE SHARE-OWNERSHIP PLANS IN THE MINING INDUSTRY– A NEW APPROACH TO ESOPS

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A research report submitted to the Faculty of Engineering and the Built Environment, University of the Witwatersrand, Johannesburg, in partial fulfilment of the requirements for the degree of Master of Science in Engineering

Johannesburg 2016

DECLARATION

I declare that this research report is my own, unaided work. It is being submitted for the Degree of Master of Science in Engineering to the University of the Witwatersrand, Johannesburg. It has not been submitted before for any degree or examination to any other University.

Signed:

Makatane Kagisho Jacob Diale

_____ day of _____2016

ABSTRACT

Empowerment of previously disadvantaged groups has been applied in many countries, in order to achieve specific political, economic and social outcomes. Group preferences and preferential policies are common in developed and developing countries under various names. They have been mostly implemented in countries where a specific ethnic, religious, or gender group has been discriminated against historically.

An ESOP is an empowerment tool that can be adapted and designed to achieve the goals of companies, employees and governments. An ESOP is an instrument used to enable employee ownership in private and public companies. Internationally the application of ESOPs have taken various architectures highly dependent on individual company and country circumstances.

SA has a long and well documented history of racial discrimination and economic exclusion. Poverty, unemployment and inequality continue to bedevil the South African economy. Transformation in the mining industry is given effect in the Mining Charter which is governed under section 100 of the Minerals and Resources Development Act. The Charter is buttressed by a key set of pillars. These pillars are supplemented by the codes of good practice as well as the housing and living conditions standards.

These pillars include reporting; ownership; housing and living conditions; procurement and enterprise development; employment equity; human resource development; mine community development; sustainable development and growth and beneficiation. This report focusses on the ownership pillar of the Charter.

The mining industry has completed a number of empowerment deals post implementation of the Mining Charter. The impacts of most BEE deals have not been broad-based; and have mostly benefitted only a few HDSA entrepreneurs. The value and number of transactions have coincided with the rise and fall of the JSE, making the deals expensive – due to elevated stock prices in favourable market conditions.

ESOPs enable extensive employee ownership; and have the ability to foster a sense of individual enterprise that fuels productivity in companies that have imbued a culture of ownership amongst their employees. ESOPs generally contribute positively to company performance; and they provide a stable and dynamic working environment, when administered effectively. ESOPs cannot be implemented in isolation; but they require a combination of factors to make them successful.

ESOPs generally contribute positively to company performance; and they provide a stable and dynamic working environment, when administered effectively. Effective ESOPs require a combination of elements for success: these comprise of financial incentives, employee-involvement mechanisms and the instilling of an ownership culture.

Anglo American was used as a proxy for the industry due to its size and diversity. ESOPs that have been implemented have failed to meet stakeholders' expectations. These ESOPs are inconsistent, complicated and mostly opaque to employees; whilst delivering modest returns to employees.

This report proposes the application of a new ESOP framework that is to be considered in amending existing ESOPs or in the crafting of new programmes. Existing ESOPs are assessed against this proposed framework in this report. The proposed ESOP framework is supported by a set of key principles, essential to the success of the framework.

The performance of ESOPs in Anglo American varied when assessed against the framework. With the exception of Envision, Anglo American's ESOPs have delivered very modest financial benefits to employees. They have not achieved their intended purpose, of empowering employees and aligning company performance with individual employee performance. When assessed against the other pillars of the framework, KIO and AAP did not perform satisfactorily.

DEDICATION

This research report is dedicated to my family, for the ongoing support that has been afforded to me over the years. It is also dedicated to Anglo American and the School of Mining Engineering at the University of the Witwatersrand – for offering me the opportunity to complete this research.

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TABLE OF CONTENTS

DECLARATION **i**

ABSTRACT **ii**

DEDICATION **v**

ACKNOWLEDGEMENTS **vi**

LIST OF FIGURES **xiii**

LIST OF TABLES **xvi**

LIST OF SYMBOLS/ACRONYMS **xvii**

1INTRODUCTION 1

1.1 Background and Motivation 2

1.2 Relevance and Importance of the Topic 3

1.3 Problem Statement 4

1.4 Objectives 4

1.5 Methodology 4

1.6 Report structure 5

2LITERATURE REVIEW 6

2.1 Empowerment of historically disadvantaged groups internationally 6

2.1.1 Empowerment Policies in the Soviet Union 7

2.1.1.1 ESOPs in the Soviet Union 8

2.1.2 Preferential Policies in India 8

2.1.2.1 ESOPs in India 9

2.1.3 Employment Equity in Canada 9

2.1.3.1 ESOPs in Canada 9

2.1.4 Empowerment in Malaysia 10

2.1.4.1 ESOPs in Malaysia 11

2.1.5 Empowerment in the United States of America 11

2.1.5.1 ESOPs in the USA 12

2.1.6 Group Preferences in Sri Lanka 12

2.1.6.1 ESOP in Sri Lanka 13

2.1.7 Summary 14

2.2 SA's Historical context 14

2.3 Empowerment of HDSA's 15

2.4 Current economic status of South Africans 17

2.5 Broad-Based Black Economic Empowerment Sector Charters 19

2.6 Empowerment in the Mining Industry 22

2.6.1 Policy Framework 22

2.6.2 Scoring Principles 23

2.7 Empowerment deals in the Mining Industry 25

2.7.1 Chamber of Mines assessment of members' empowerment transactions in the industry 25

2.7.2 Transactions involving employee schemes and community trusts 29

2.7.3 Company transactions 30

2.7.4 Summary of benefits to beneficiaries 32

2.7.5 Assessment by The Department of Mineral Resources on the industry's performance in relation to the Charter 33

2.7.6 Summary 33

2.8 ESOPS 34

2.8.1 The need for ESOPs 35

2.8.2 How ESOPs are structured 36

2.8.3 Various ESOP models 37

2.8.3.1 Share Appreciation Rights 37

2.8.4 Characteristics of successful ESOPs 42

2.8.5 Benefits of Establishing an ESOP 44

2.8.6 Criticism of ESOPs 45

2.8.7 Financing an ESOP 47

2.8.8 ESOPs in other parts of the world 47

2.8.9 Summary 48

2.9 Overview of ESOPs in South Africa 49

2.10 Summary 52

3ANGLO AMERICAN 53

3.1 Anglo American as a proxy for the mining industry 53

3.2 Anglo American’s BEE Transactions 60

3.3 AAP – Atlatsa / Bokoni 60

3.3.1 Structure Overview 60

3.4 AATC 63

3.4.1 Structure overview 63

3.5 De Beers 64

3.5.1 Structure overview 64

3.6 DTC SA Empowerment 65

3.7 Employee Share-Ownership Plans (ESOPs) 66

3.8 Summary 66

4. Anglo American’s assessments of current ESOPs 67

4.1 Performance assessment 67

4.2 Original objectives of the schemes 68

4.3 Summary 69

5ESTABLISHING A FRAMEWORK FOR A SUCCESSFUL ESOP 70

5.1 Principles underpinning the proposed framework 70

5.2 Proposed Framework 72

5.2.1 Meaningful economic participation 72

5.2.2 Instilling an ownership culture 73

5.2.3 Driving the business disciplines 73

5.2.4 Share price performance 73

5.2.5 Financial incentives 74

5.2.6 Aligned goals 74

5.2.7 Productivity gains 74

5.2.8 Engaged and responsive workforce 74

5.2.9 Regulatory compliance 75

5.3 Summary 75

6 ANALYSIS OF CURRENT ESOPS USING PROPOSED FRAMEWORK 77

6.1 KIO 77

6.1.1 Share performance and financial incentives 77

6.1.2 Meaningful economic participation 80

6.1.3 Instilling ownership culture and aligning goals 80

6.1.4 Productivity 80

6.1.5 Engaged and responsive workforce 81

6.1.6 Regulatory compliance 82

6.1.7 Summary 82

6.2 Anglo American Platinum 83

6.2.1 Share performance and financial incentives 84

6.2.2 Instilling an ownership culture and aligning goals with an engaged and responsive workforce 87

6.2.3 Meaningful economic participation 88

6.2.4 Productivity 88

6.2.5 Regulatory compliance 89

6.2.6 Summary of Kotula 90

6.3 Summary 90

7 CONCLUSION AND RECOMMENDATIONS 91

8 REFERENCING 94

9 APPENDICES 101

Appendix 1: Summarised HDSA ownership results 101

Appendix 2: Summary of Anglo American Platinum Atlatsa/Bokoni empowerment deal 102

Appendix 3: Anglo American Platinum Joint Ventures (JVs) 103

Appendix 4: Funding model for Anglo-Inyosi Coal 105

Appendix 5: Ponahalo-funding Structure 106

LIST OF FIGURES

Figure 1: Average annual household income by population group (Statistics South Africa, 2011) 18

Figure 2: Kernel Density curve of income distribution by group (Van De Berg, 2010) 19

Figure 3: A structure of the transformation policy framework for the mining industry (Department of Mineral Resources, 2015) 23

Figure 4: Portion of ownership of mining industry transferred to HDSA (Wu and Moodley, 2009) 27

Figure 5: Value of transactions in the mining sector (Wu and Moodley, 2009) 28

Figure 6: Resources 20 index (Financial Times, 2016) 29

Figure 7: BEE transactions involving employees and communities (Wu and Moodley, 2009) 30

Figure 8: Meaningful economic participation of HDSA (Chamber of Mines South Africa, 2015) 32

Figure 9: Anglo American's economic contribution to SA (Genesis Analytics and PwC, 2013) 54

Figure 10: Anglo American’s capital expenditure (Genesis Analytics and PwC, 2013) 55

Figure 11: Mining-production revenue (Genesis Analytics and PwC, 2013) 56

Figure 12: Distribution of AA's economic impact (Genesis Analytics and PwC, 2013) 57

Figure 13: Local sales and exports (Genesis Analytics and PwC, 2013) 58

Figure 14: Tax revenues paid by AA (Genesis Analytics and PwC, 2013) 59

Figure 15: AAP BEE deal structure 61

Figure 16: Atlatsa/Bokoni structure (Anglo American Corporate Finance , 2013) .. 61

Figure 17: De Beers' structure (Anglo American Corporate Finance , 2013) 64

Figure 18: DTC structure (Anglo American Corporate Finance , 2013) 65

Figure 19: Proposed ESOP framework 76

Figure 20: KIO's share price (Kumba Iron Ore Limited, 2015) 78

Figure 21: KIO's earnings-dividend 78

Figure 22: KIO's dividend flow graph 79

Figure 23: KIO's productivity 81

Figure 24: Summary of KIO Iron Ore's performance evaluated against proposed framework 83

Figure 25: Anglo American Platinum dividend comparison 85

Figure 26: Anglo American Platinum share price (Anglo American Platinum Limited, 2015).....86

Figure 27: AAP earnings – dividend chart 87

Figure 28: Precious Metals Sector Productivity (Goldman Sachs, 2012).....88

Figure 29: AAP labour productivity profile (Anglo American Platinum Limited, 2008-2015). 89

Figure 30: Summary of AAP performance evaluated against proposed framework 90

LIST OF TABLES

Table 1: Transformation sector charters (Department of Trade and Industry, 2016) 21

Table 2: Scoring principles for the elements of the charter (Department of Mineral Resources, 2015) 24

Table 3: Top 10 contributors and vendors to BEE transactions (Wu and Moodley, 2009) 31

Table 4: Advantages and Disadvantages of Share Appreciation Plans (Hunt, 2013). 38

Table 5: Advantages and Disadvantages of Share Performance Plans (Hunt, 2013). 39

Table 6: Advantages and Disadvantages of Forfeitable Share Plans (Hunt, 2013). 40

Table 7: Advantages and Disadvantages of Forfeitable Share Plans (Hunt, 2013). 41

Table 8: Summary of ESOPs in SA (Motswenyane, 2009). 50

Table 9: AA business unit ESOPs (Anglo American Corporate Finance , 2013) ...66

Table 10: KIO's annual financial results (Kumba Iron Ore Limited, 2006-2015) 77

Table 11: AAP annual financial result (Anglo American Platinum Limited, 2008-2014) 84

LIST OF SYMBOLS/ACRONYMS

AAP:	Anglo American Platinum
AASAF:	Anglo American South Africa Finance
AATC:	Anglo American Thermal Coal
AEMFC:	African Exploration Mining and Finance Company
AIC:	Anglo-Inyosi Coal
AMCU:	Association of Mineworkers and Construction Union
ANC:	African National Congress
ARM:	African Rainbow Minerals
ASAC:	Anglo South Africa Capital
ASSA:	Anglo American South Africa
BEE:	Black Economic Empowerment
BBSEE:	Broad-Based Socio-Economic Empowerment
BBBEE:	Broad-Based Black Economic Empowerment Amendment Act
DBCM:	De Beers Consolidated Mines
DBGS:	De Beers Group Services
DBSA:	De Beers South Africa
DMR:	Department of Mineral Resources
DTI:	Department of Trade and Industry
DT:	Development Trust
DTC SA:	Diamond Trading Company of South Africa
ESO:	Employee Stock Options
ESOP:	Employee share-ownership plan
FDI:	Foreign Direct Investment
GSS:	Global Shared Services
HDSA:	Historically Disadvantaged South Africans
IDC:	Industrial Development Corporation
IT:	Information Technology
JSE:	Johannesburg Stock Exchange
JV:	Joint Ventures
KIO:	Kumba Iron Ore
LLRT:	Lefa La Rona Trust
LSA:	Labour Sending Areas
LSA NPC:	Labour Sending Area Non-profit Company
MPRDA:	Mineral and Petroleum Resources Development Act
NEC:	National Executive Council

NUM:	National Union of Mineworkers
NVF:	Notional Vendor Funding
PAYE:	Pay as You Earn
PWC:	PricewaterhouseCoopers
RB Plat:	Royal Bafokeng Platinum Limited
RBH:	Royal Bafokeng Holdings
RBS:	Royal Bank of Scotland
SA:	South Africa
SAB:	South African Breweries
SIOC:	Sishen Iron Ore Company
SPV:	Special Purpose Vehicle
USA:	United States of America

1 INTRODUCTION

Historically, black South Africans have been excluded from the mainstream economy; and this has resulted in skewed distribution patterns of wealth and participation in the South African (SA) economy. Through various legislative instruments, the SA government has endeavoured to reconstruct the economy to better reflect South African society, and to eradicate some of SA's social ills.

Poverty, unemployment and inequality continue to bedevil the country; and as such, the mining industry continues to be a politically charged industry, which is seen by many as being capable of addressing SA's developmental goals. Consequently, the SA government is implementing policies to transfer mining assets to Historically Disadvantaged South Africans (HDSAs). The government has sought to achieve these objectives through the introduction of the Mining Charter.

The Mining Charter stems from the Mineral and Petroleum Resources Development Act of 2002 (MPRDA), where it states in section 2(c) that the objectives of the Act are to *"promote equitable access to the nation's mineral and petroleum resources – to all the people of South Africa".* It further states in 2(d), that some of the objectives are to *"substantially and meaningfully expand opportunities for historically disadvantaged persons, including women, to enter the mineral and petroleum industries, and to benefit from the exploitation of the nation's mineral and petroleum resources"* (Government Gazette vol.448, 2002).

The Act further states in Chapter 3, that: *"the Minister must ensure the sustainable development of South Africa's mineral and petroleum resources within a framework of national environment policy, norms and standards, while promoting economic and social development"* (Government Gazette vol.448, 2002).

1.1 Background and Motivation

In September 2010, the South African government published a Revised Broad-Based Socio-economic Empowerment Charter (BBSEE) for the Mining Industry. The revised Charter sought to give clarity to ambiguities existing in the original Charter, whilst providing more specific targets than its predecessor. With the 2014 review of the performance of mining companies with respect to the different elements of the Mining Charter, there has been a great deal of uncertainty in the mining industry with regard to how companies have performed (Anglo American Corporate Finance , 2013).

The revised charter calls for *"effective ownership"* of mining companies by HDSAs. This is defined in the revised Charter as *"the meaningful participation of HDSAs in the ownership, voting rights, economic interest and management control of mining entities"* (Department of Mineral Resources, 2010).

The regulator and mining companies disagree on performance. Government and the industry produce different performance results; with government intimating that industry is overstating their performance, and the industry pointing to government's inability to recognise good performance (Anglo American Corporate Finance , 2013).

The mining industry is of the view that the interpretation afforded by the DMR, that Black Economic Empowerment (BEE) deals completed after 2004, which resulted in participants disposing their assets, should result in renewed BEE deals is flawed. This has resulted in the DMR finding certain companies not having complied with the ownership aspects, due to the current reduced black ownership (Mthimkhulu, 2015).

The industry is of the view that those deals completed with empowered entities should be included in the ownership calculation as it represents HDSA ownership. It further ads that the Charter does not require the industry to maintain 26% ownership

once it has been achieved. The chamber believes the exclusion of past deals results in a material misrepresentation of HDSA participation (Mthimkhulu, 2015).

This report will investigate the different models used by companies for compliance with the ownership aspect of the Charter. The specific focus of this study will be on the different Employee Share Ownership Plans (ESOPs) adopted and the performance of this particular instrument.

These ESOPs will be evaluated against a new proposed framework that commandeers the virtues of a successful ESOP in the South African context. Anglo American is used as a case study and proxy for the industry; because it is the largest and most diversified company, with four (4) business units in SA, namely coal, platinum, iron ore and diamonds.

1.2 Relevance and Importance of the Topic

Over the past decade the mining industry has faced significant challenges relating to policy uncertainty, labour unrest and escalating costs. Most recently, the Association of Mineworkers and Construction Union (AMCU) engaged in a 5-months' strike. The strike has demonstrated the publicly perceived charge of an ongoing trust deficit that exists between business, labour and government.

It is important to investigate the reasons behind these events, especially because mining companies have instated ESOPs – with the expectation that this would achieve the aims envisaged in the Mining Charter. It is also important to investigate this topic because of the evolving minerals policy and regulatory environment.

The effectiveness of mining policy needs to be reviewed to assist in further policy development and implementation. Hence, there needs to be an understanding of the reasons behind the successes or failures of the current Mining Charter requirements and identification of opportunities to improve on development polices.

1.3 Problem Statement

The Mining Charter was developed to transform the socio-economic landscape of the mining industry in SA. In principle, most mining companies have expressed broad support for the objectives of the Charter and the outcomes it seeks to achieve. However, there have been disagreements between the regulator and the mining industry with regard to the performance of companies in aspiring to achieve the objectives of the Charter (Anglo American Corporate Finance , 2013).

The effectiveness of initiatives by mining companies to both comply with Charter requirements and improve the socio-economic conditions of HDSA's have received mixed reviews. ESOPs instituted by mining companies do not seem to be meeting the expectations of all the important stakeholders, mainly employees, the companies themselves and the regulator (Anglo American Corporate Finance , 2013).

1.4 Objectives

The objective of the study is to propose a framework to be used by mining companies when establishing ESOPs. The framework is underpinned by key fundamental pillars and will encapsulate the main virtues of successful ESOPs applied in a South African context. This report will evaluate the efficacy of current ESOPs in Anglo American; and test them against this proposed framework.

1.5 Methodology

The methodology applied in completing this report, in order to address the objectives of the study was as follows:

- Utilise historical and current government literature;
- Utilise data from the mining companies; and
- Utilising information collected from desktop studies.

This report has utilised Anglo American data. Anglo American can be considered as a proxy for the industry, due to its dominance in the local industry. The report used current and historical policy documents. Generic literature on ESOPs was also used. The report also used publicly available data from company annual reports and research reports discussing this issue.

1.6 Report structure

Chapter 1 introduces the scope of the study; and it provides the reasons for conducting this research. Chapter 2 provides a literature review on the empowerment of previously disadvantaged groups in other countries and application of ESOPs in those profiled countries. Chapter 2 also provides socio-political and socio-economic conditions that necessitated the empowerment of HDSAs. Furthermore, the chapter provides a review of ESOPs and the different associated models.

Chapter 3 focuses on Anglo American and the company's contribution to SA and the mining industry. Furthermore, the structure of Anglo American's empowerment deals in SA is analysed in Chapter 3. Chapter 4 provides an analysis of Anglo American's ESOPs.

Chapter 5 proposes a new approach to ESOPs in the mining industry. A set of principles is afforded that underpins the proposed framework. Chapter 6 analyses Anglo American's ESOPs against this framework. Chapter 7 contains the conclusion and recommendations of the report.

2 LITERATURE REVIEW

2.1 Empowerment of historically disadvantaged groups internationally

The empowerment of previously disadvantaged groups is a common practice internationally; and goes by various names in different countries. The tools and policy instruments adopted to achieve empowerment goals vary from country to country. Common names of empowerment philosophies include compensatory discrimination; preferential policies; positive action; and affirmative discrimination (Martin, 2001).

In his empirical study, Sowell (2004) studied how preferential policies have been implemented throughout history in various countries. He found that empowerment policies in some countries have included preferences for minority groups in society, whilst others were structured to favour majorities.

In other countries these policies where aimed at various classes in those communities. These group preferences have been applied in countries, such as India, Britain, Sri-Lanka, Nigeria, Malaysia, Indonesia, Israel, China, Australia, Brazil, Fiji, Canada, Pakistan, New Zealand, the United States of America (USA) and the Soviet Union, as well as its successive States (Sowell, 2004). There are a number of empowerment instruments that can be adopted depending on the nature of exclusion and envisaged outcome.

An ESOP is an empowerment tool that can be adapted and designed to achieve the goals of companies, employees and governments. An ESOP is an instrument used to enable employee ownership in private and public companies. Internationally the application of ESOPs have taken various architectures highly dependent on individual company and country circumstances (Gates and Saghir, 1995).

ESOPs are implemented for a variety of reasons, including broadening ownership, enhancing company performance, and facilitating privatization in previously state owned entities and carrying other reform measure as well as raising money for corporate purposes (Gates and Saghir, 1995).

2.1.1 Empowerment Policies in the Soviet Union

The Soviet Union was a large multi-ethnic state with an assembly of territories with diverse interests. It was the first state in the old European architecture to face strong nationalism and responded with the systematic promotion of its ethnic minorities. Martin (2001) provided a comprehensive assessment of the manifestation of group preferences in the large diverse national republics and territories scattered across the Soviet empire.

The majority of Soviet nationalities were regarded as culturally backward, compared to the Russians, Ukrainians, Georgians, Armenians, Jews and Germans; who were grouped as western nationalities. The Union was essentially divided into two regions, the East and the West (Martin, 2001).

The East had a problem of low literate, uneducated nationals; and so empowerment policies were skewed toward education and hiring of citizens from the East. In the West, literate and educated nationals were abundant, with the policy focusing on language, and establishing the national language as the official state language. *"Economic equalisation"*, which referred to the redistribution of economic power, through preferential policies in education and hiring of the local population was preferred (Martin, 2001).

2.1.1.1 ESOPs in the Soviet Union

ESOPs have been used in the former Soviet Union for empowering employees utilising previously state owned entities. ESOPs became a popular empowerment tool because they ensured workers benefited from the privatization programme that ensued post the collapse of the Soviet Union (Gates and Saghir, 1995).

2.1.2 Preferential Policies in India

India has a large and diverse population, with over a billion people living within its borders. The country has 6 main ethnic groups, 52 major tribes, 6 major religions, and 6400 castes and sub-castes – with 18 major languages and 1 600 minor languages and dialects (Castellino and Redondo, 2006). India has long history with preferential policies for targeted groups beginning under British colonial rule. India's constitution espouses policies designed to assist disadvantaged segments of its population (Sowell, 2004).

In 1950, the first amendment to the constitution enshrined preferential policies and programmes for deprived peoples, untouchables, Scheduled Castes and Tribes (Castellino and Redondo, 2006). There are different policies that predominated; those aimed at national minorities viewed as less fortunate and policies in the various states in India that target local groups. Tribal groupings that fell outside the social mainstream were also included (Sowell, 2004).

Sowell (2004) describes how these policies were implemented with the objective of raising the socio-economic conditions of these groups through what was termed *"positive discrimination".* These preferential policies were given effect in preferential hiring, admissions in institutions of higher learning and parliamentary representation amongst others. All of these were designed to overcome historical discriminatory patterns.

2.1.2.1 ESOPs in India

The use of ESOPs in India is common with varying design practices. Most of the ESOPs have been implemented in the Information Technology (IT) sector accounting for 61% of all ESOPs. This practice is particular tor the IT sector due to recruitment patterns in this sector and the need to retain highly skilled and globally mobile employees. ESOPs have been used as a retention tool in these companies (Pathak and Saraswathy, 2011).

2.1.3 Employment Equity in Canada

Renowned scholar Loney (1998) examined how preferential hiring policies placed race and gender at the centre of Canadian politics. There were various groupings that were beneficiaries of preferential policies in Canada. They had a specific concern for those who were said to have experienced double discrimination, notably women of colour. Aboriginal (First Nation) Canadians have also been the target of employment equity legislation aimed at addressing the historical injustices that Aboriginal's have suffered (Loney, 1998).

2.1.3.1 ESOPs in Canada

ESOPs have been widely used in Canada with some dating back 40 years. These ESOPs started out in the public sector as a means of rewarding employees for their efforts, then later expanded to all employers. Some organisations in Canada have used ESOPs post the financial crisis in 2008 as a job saving mechanism. Examples of such organisations include Algoma Steel, Spruce Falls and Canadian Airlines (ESOP Association Canada, 2015).

The Toronto Stock Exchange conducted a study that compared the performance of companies with ESOPs and those without ESOPs. The study found that companies with ESOPs had a 123% profit growth over 5 years, 95% higher net profit margin, 24% higher productivity, 92.3% higher return on equity and a 65.5% higher return on capital (ESOP Association Canada, 2015).

2.1.4 Empowerment in Malaysia

Malaysia has a population of approximately 23 million people; and it is considered to be one of the most prosperous countries in Southeast Asia. As many as 50% of the population are Malays; 24% are Chinese; and 7% are Indian. In 1948, the population of colonial Malaysia was 45% Chinese, 43% Malay, and 10% Indian. Apart from the 3 groups that exist in Malaysia there are other indigenous peoples, who together make up the Bumiputeras or the *"sons of the soil"* (Sowell, 2004).

As early as 2500 BC, technologically advanced groupings migrated to Malaysia from China. These groups of seafarers and farmers encountered and forced the indigenous populations into the hills and jungles. In later years, the Chinese predominated in the urban areas and mining districts; whilst the largest numbers of Indians were found in rubber areas (known for its production of natural rubber) mainly located on the West coast. Malays mostly lived in the in the Northern region, outside towns in rural areas (Castellino and Redondo, 2006).

Under British rule, Malaysia instituted policies in favour of the Malay population, whilst utilising cheap Indian labour to work in the peninsula. The Chinese were left to govern themselves; and utilised their entrepreneurial skills to get ahead. Chinese businesses flourished after the British rule; whilst the economic fortunes of the Malays languished. (Castellino and Redondo, 2006).

Sowell (2004) found that although Malays were more privileged than the Chinese, through rising incomes in the Chinese population, they managed to earn more than double the average income of Malays. This produced resentment, which precipitated demands from the Malay populous for preferential policies. At this time under British rule, the Malays already enjoyed preferential treatment; with other groups facing strong restrictions on land ownership and Malay children provided with free education. Despite these policies, the Chinese continued to outperform the other ethnic groups.

With the exclusion of Singapore (due to their high Chinese population) and other territories, Malaya became Malaysia. Policies included the political hegemony of the Malays. This was achieved by constitutional guarantees and by positively weighting votes in rural areas, where the Malay population mostly predominated (Sowell, 2004).

The Malays wanted to preserve and maintain this preferential treatment for themselves, and for other indigenous peoples, whilst the Chinese demanded equal treatment for all citizens. The inter-ethnic strife was resolved, when Malaysia expelled Singapore in 1965, because of Singapore's high Chinese population, leaving Malaysia with a comfortable Malay majority (Sowell, 2004).

According to Sowell (2004), new economic policies emanated where preferences that existed under government employment were extended to the private sector. The policy also prescribed that 30% of all corporate shares should be transferred to the Malay population, during which time they owned no more than 2% of the country's corporate equity.

2.1.4.1 ESOPs in Malaysia

The use of ESOPs in Malaysia are not as popular as Employee Stock Options (ESOs). Many publicly traded companies use this tool for employee compensation and incentives packages (Bacha et al., 2009).

2.1.5 Empowerment in the United States of America

Anderson (2004), has studied the history of affirmative action in the USA. He describes how many States in the 1880s promulgated various discriminatory laws based on race. These States established segregated schools, hospitals, jails and homes for the impoverished, elderly, deaf – and even for the blind.

Preferential policies and practices in the USA have been described as correction, the forestalling of discrimination, or as promoting diversity. Group preferences evolved out of laws initially seeking to ban discrimination against individuals (Sowell, 2004). Anderson (2004) found that group preferences had been part of American national policy for more than 40 years.

Companies in the USA are required to have affirmative action plans that ensure equal employment opportunities. If companies do not abide by their policy, the government may bar them from making contracts. Public institutions and universities must have preferential policies, including those private institutions that accept grants (Sowell, 2004).

2.1.5.1 ESOPs in the USA

The USA has implement the most number of ESOPs within companies operating in that country since the first ESOP was created in 1956 (Gates and Saghir, 1995). In 2011 The National Center for Employee Ownership found that 11,300 ESOPs existed in the USA which covered 13.3 million employees who collectively held approximately $900 billion in assets (Rodgers, 2011).

The study also found that companies employing ESOPs in the USA experienced faster growth rates in sales, employment and productivity. These companies also have higher compensation for employees, higher employee retirement assets and lower staff turnover (Rodgers, 2011).

2.1.6 Group Preferences in Sri Lanka

In Sri Lanka, simmering discontent and ethnic tensions had resulted in a full scale civil war, which subsequently divided the island-state. Sri Lanka has seen the two largest ethnic groups, the Sinhala (74%), who dominate State institutions and the army, and the Tamil minority (13%), who have resorted to guerrilla warfare, engaging in a vicious civil war. The minority Muslim population is mostly ignored in the face of this ongoing feud (Castellino and Redondo, 2006).

Historically, the Tamils were located in the northern part of the state, characterised by a dry climate and devoid of natural endowments. The Sinhalese were located in the more prosperous region with high rainfall and fertile ground. The Tamils readily took advantage of the education opportunities provided for by the missionary schools established (Sowell, 2004).

The Tamil minority was more favourably represented in universities, in the professions and in businesses than the Sinhalese majority. In 1956, the government instituted *"Sinhala only"* as the official language. Declining prospects, both in education and employment, led to the Tamils protesting, resulting in lethal riots in subsequent years. Ultimately, a civil war broke out between the two ethnic groups (Sowell, 2004).

Sri Lanka has enshrined minority rights in the country's Constitution and legal system, from the autonomy of regimes and negotiations with the Tamils, to the reservation of seats in political and governance structures and public institutions (Castellino and Redondo, 2006).

2.1.6.1 ESOP in Sri Lanka

ESOPs have been used in Sri Lanka in both the private and public sector. In the public sector these have been used in programmes that have been termed the *"peoplisation programmes"* aimed at transferring ownership of state enterprises into the hands of employees. In the private sector ESOPs have been used to expand employee ownership with the intended purpose of increasing profitability through greater employee satisfaction (Pushpakumara et al., 2009).

Pushpakumara et al. (2009) studied the profitability of listed companies in Sri Lanka that have applied ESOPs. They found that ESOPs where not a significant determinant of profitability in those listed companies. One reason cited for this conclusion was the lack of significant share allocations afforded to employees with

most shares not afforded voting rights and used as a compensation tool for employees.

2.1.7 Summary

Empowerment of previously disadvantaged groups has been applied in many countries, in order to achieve specific political, economic and social outcomes. Group preferences and preferential policies are common in developed and developing countries under various names. They have been mostly implemented in countries where a specific ethnic, religious, or gender group has been discriminated against historically.

These preferential policies have manifested in employment equity, ownership of land, protected representation in education and parliament in these countries. In most of the profiled countries ESOPs have been used as an empowerment tool for the collective benefit of employees, employers and governments.

South Africa has its own history of discrimination and economic exclusion based on race. Section 2.2 - 2.7 will focus on empowerment in the South African context, from a broader economic perspective to a more specific focus of empowerment in the mining industry. Section 2.8 will discuss ESOPs in terms of their formulation, structure and application with the advantages and disadvantages of each model. The various plans adopted by companies in the South African economy will be profiled.

2.2 SA's Historical context

SA has a long and well documented history of racial discrimination and economic exclusion. SA's modern economy has largely been developed on the back of the mining industry, with foreign capital turning what was largely an agricultural economy into a thriving mining center (Nattrass and Seekings, 2010).

By 1910, gold mining on the Witwatersrand had transformed SA's economy into an industrializing economy, anchored by a strong mineral exporting sector. During that time, there existed a set of discriminatory policies and institutions, which sought to protect the incomes of mostly white workers, whilst depressing the wages paid to unskilled, black employees (Nattrass and Seekings, 2010).

Assessing the history of SA's modern economy, Natrass and Seekings (2010) provided an analysis of how the SA economy experienced significant change throughout the twentieth century. These racially based discriminatory and coercive strategies they found, excluded unskilled black workers from the institutional framework that fostered economic prosperity.

These interventions not only ensured high levels of inequality in the short term; but they also shaped SA's growth path, such that high levels of inequality persisted over time. SA's economic growth model ensured that a minority enjoyed disproportionate benefits; whilst the rest of the population enjoyed very little and some had no benefits at all. Despite a growing economy, poverty and chronic unemployment persisted into the second half of the century (Nattrass and Seekings, 2010).

2.3 Empowerment of HDSA's

Apartheid denied the majority of South Africans the opportunity to amass capital in any form, such as land, finance, skills, education and social networks. The need to promote the drafting of redressing policies was necessitated by the enduring legacy of this system (Sharma, 2012).

South Africa's level of income distribution and racial inequality is high and persistent. South Africa is rated as an upper-middle income country (in terms of GDP per capita and economic structure), however its social indicators such as life expectancy, infant mortality and quality of education are closer to those of lower-middle countries. This is indicative of the levels of inequality within South African society (Van Der Berg, 2010).

Empowerment and the pursuit of equality in the South African context gets its tenants from the South African Constitution. Section 9 (2) of the constitution states, *"equality includes the full and equal enjoyment of all rights and freedoms. To promote the achievement of equality, legislative and other measures designed to protect or advance persons, or categories of persons, disadvantaged by unfair discrimination may be taken"* (Constitutional Assembly, 1996).

Post the power sharing arrangement in 1994 the South African government began to formulate their BEE intentions. These intentions found expression in legislative, regulatory and policy measures by 2000. At this stage, none of the discussions were involved with BEE ownership and investments (Cargill, 2010).

Much of the discussions were focussed on employment based affirmative action, skills training and business development as measures for black empowerment. The formulation of the BEE strategy began under the auspices of the Department of Trade and Industry in 2003 (DTI) (Cargill, 2010).

There were a number of BEE deals that were conducted at this time which many critics believed only benefitted the political and economic elite. BEE investors garnered a reputation for opportunistic rent seeking and unproductive investment behaviour without an interest in long term value creation (Cargill, 2010).

Another important criticism levelled against BEE deals at this time was the choice of empowerment partners. Consortiums involved in these transactions often involved trade unions, various social groupings and a few politically connected individuals (Cargill, 2010).

After the strategy was adopted by various stakeholders, parliament soon agreed to the BEE Act. The various state entities where compelled to formulate and implement code and sector charters. The codes sought to mitigate some of the unwanted occurrences from the first round of BEE transactions (Cargill, 2010).

Section 2.4 will delve into the socio-economic conditions of South Africans. It will depict the wealth profile of the different race groups in SA.

2.4 Current economic status of South Africans

Currently, wealth distribution in SA is skewed toward minority groups; whilst the majority of the population enjoy modest incomes. Figure 1 below, depicts the variance in average annual household income in the different ethnic groups. The average annual income in Black households was R60, 613 in 2011, significantly less than coloured-headed households at R112, 172. Indian households had the second highest annual income at R251, 541 in 2011.

White-headed households had the highest average household income at R365, 134 per annum. The average increase in the annual household income for black Africans was R38, 091 from 2001-2011; for the Coloured community, it was R60, 732; for the Indian/Asian community, it was R148, 935; and for the White community, it was R171, 314 (Statistics South Africa, 2011). This indicates growing racial inequality and further exacerbation the aforementioned economic exclusion. This requires more effective policy instruments tailored for redress.

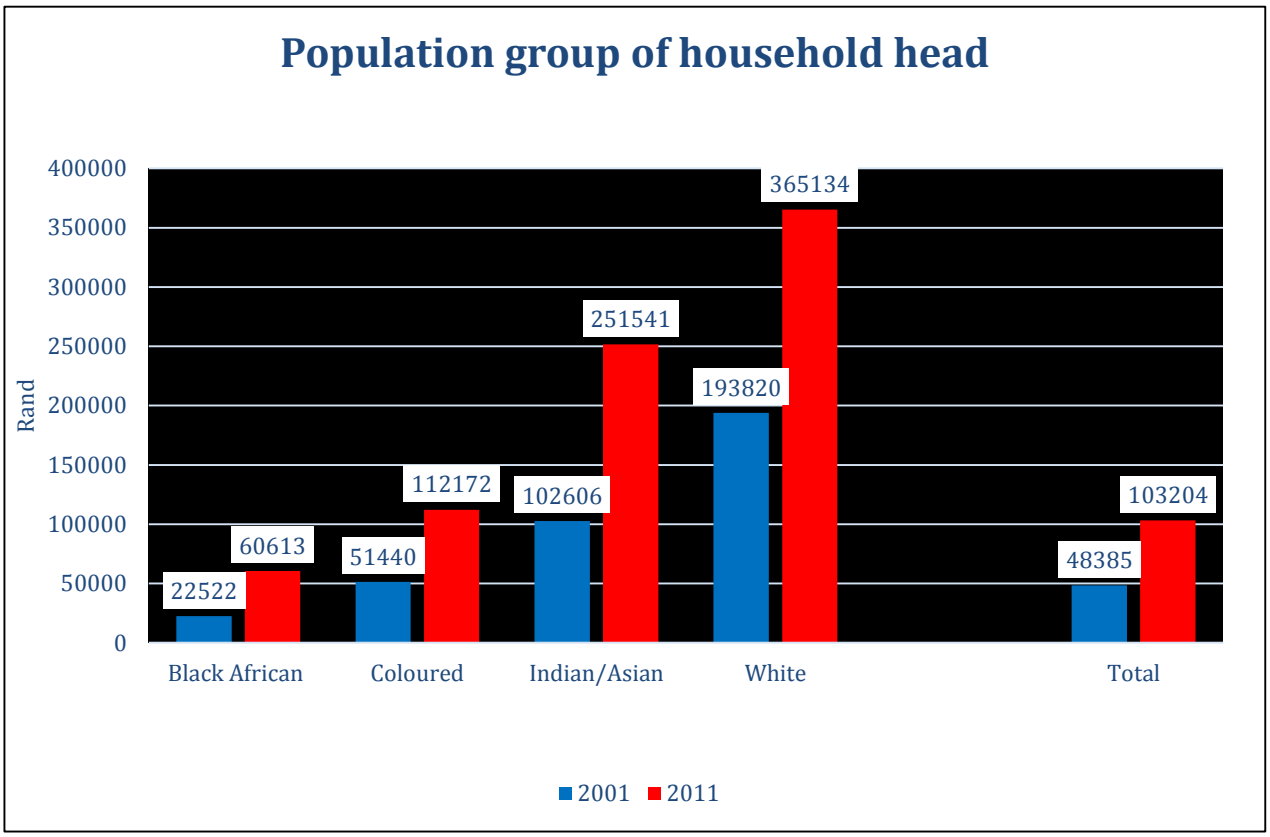


Figure 1: Average annual household income by population group (Statistics South Africa, 2011)

The kernel density curve of income distribution by race portrayed in Figure 2 below depicts how white incomes far exceed those of blacks and consequently lie to the right, with coloureds and Indians taking intermediate positions (Van De Berg, 2010).

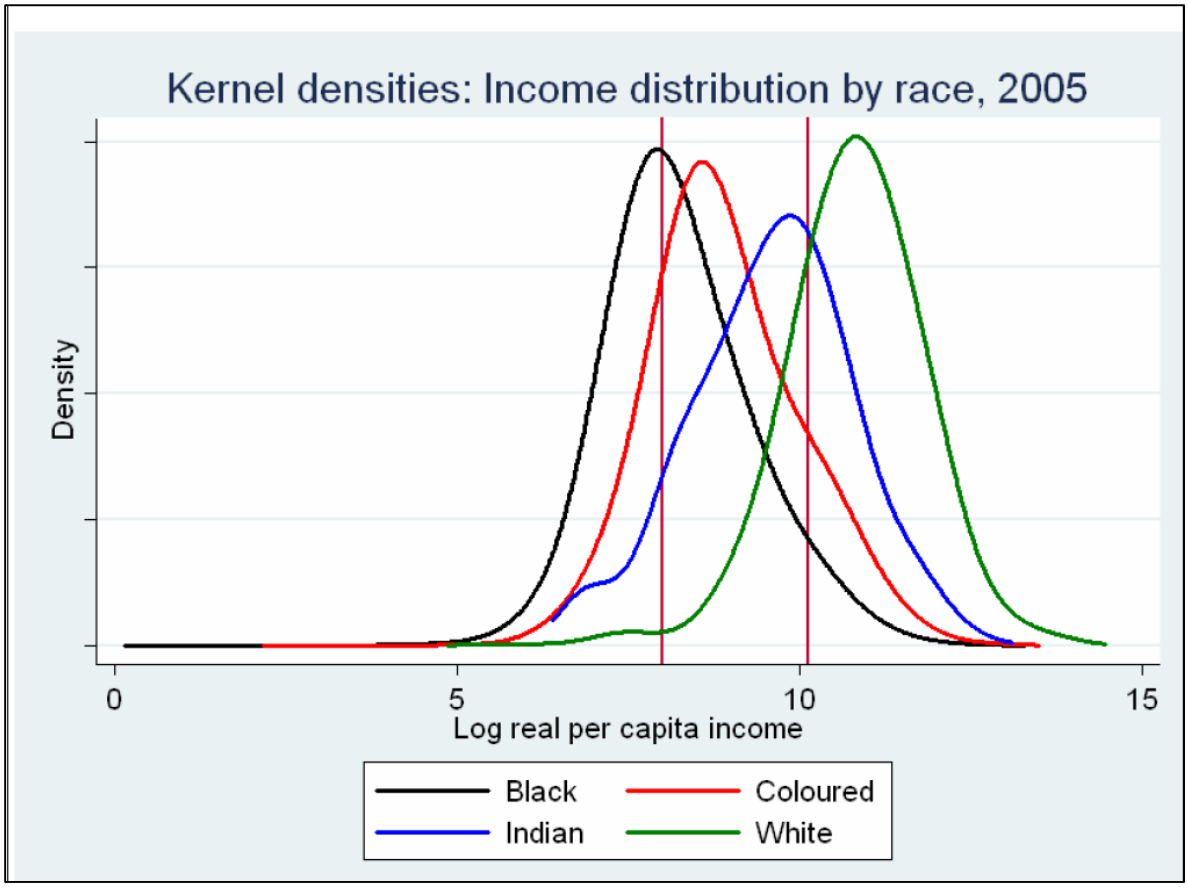


Figure 2: Kernel Density curve of income distribution by group (Van De Berg, 2010)

South Africa still struggles with income inequality. The average annual income of white South Africans is significantly higher than that of other groups in the country. The income disparity is most significant between white South Africans and black Africans. Section 2.5 outlines some of the policy instruments used to achieve redress in the broader economy.

2.5 Broad-Based Black Economic Empowerment Sector Charters

The Broad-Based Black Economic Empowerment (BBBEE) Amendment Act, is used as the policy instrument governing transformation in the broader SA economy. The Act defines broad-based black economic empowerment as the economic empowerment of all black people. The definition singles out the empowerment of women, workers, youth, people with disabilities and people living in rural areas. The strategies outlined to achieve this include, but are not limited to:

- Increased management, ownership and enterprise control of productive assets;
- ownership and management of enterprises and productive assets by communities, workers, co-operatives and other collective enterprises;
- human resource and skills development of black people;
- equitable representation in different levels in the workforce;
- preferential procurement; and
- investment in black owned enterprises (Parliament of the Republic of South Africa, 2013)

The DTI in 2007 introduced the Codes of Good Practice, in terms of which a number of transformation sector charters were introduced (Department of Trade and Industry, 2016). The charters are outline in Table 1 below.

Table 1: Transformation sector charters (Department of Trade and Industry, 2016)

Sector Charters	Effective Date	Highlights
Agri-BEE Charter	28 December 2012	Charter supports land reform by setting equity and land ownership targets. Recognition given for long-term leases under enterprise development and socio-economic development elements. Greenfield ventures, job creation and beneficiation of primary products, and support industrialisation, highly recognised
Financial Sector Charter	26 November 2012	Transformation guidelines for the financial sector. 8 pillars in Financial Sector Charter. Extra element, known as Access to Financial Services, aims to facilitate access to finance for black people and black-owned enterprises.
(ICT) Charter	6 June 2012	30% black ownership to be achieved by entities in the sector. 5% Net Profit After Tax to be spend on enterprise development initiatives. 1.5% of Net Profit After Tax on Socio Economic Development Initiatives
Property Sector Charter	1 June 2012	Charter introduced targets such as measurements for Economic Development used for investment for properties in underdeveloped areas and thus reduce service inequalities and the limited tradability of properties in these areas.
Chartered Accountancy Sector Code	10 May 2011	Chartered Accountancy Profession to increase the number of black people, particularly black women entering the profession.
Integrated Transport Sector Codes	21 August 2009	Comprises eight (8) sub-sectors, which seek to boost one of South Africa's largest infrastructure and Gross Domestic Product (GDP) contributors. Aims to fast-track the implementation of efficient transportation, freight and logistics sectors within the economy. 35% black-ownership target, within a period of five (5) years.
Forest Sector Code	12 June 2009	30% BEE ownership. It further seeks to encourage and support entities to undertake BEE-compliant procurement and job creation initiatives in the sector.
Construction Sector Code	5 June 2009	Advancement of transformation and BEE in the procurement of construction programmes and services. 30% black ownership in the industry over the next 10 years.
Tourism Sector Code	22 May 2009	Seeks to ensure that a significant number of enterprises doing business in the tourism industry are not excluded

Section 2.6 below outlines the empowerment governance framework in the mining industry.

2.6 Empowerment in the Mining Industry

2.6.1 Policy Framework

The mining industries policy framework is governed by the Constitution of South Africa and the MPRDA. The Mining Charter is provided for in terms of section 100 of the MPRDA as instrument for transformation in the industry (Department of Mineral Resources, 2015).

Transformation in terms of the Charter is buttressed by a key set of identified pillars. These pillars are supplemented by the codes of good practice as well as the housing and living conditions standards as per section 100 of the MPRDA. Figure 3 below summarises the framework (Department of Mineral Resources, 2015).

The Charter pillars include reporting; ownership; housing and living conditions; procurement and enterprise development; employment equity; human resource development; mine community development; sustainable development and growth and beneficiation (Department of Mineral Resources, 2015). For compliance with the Charter companies are measured against these pillars.

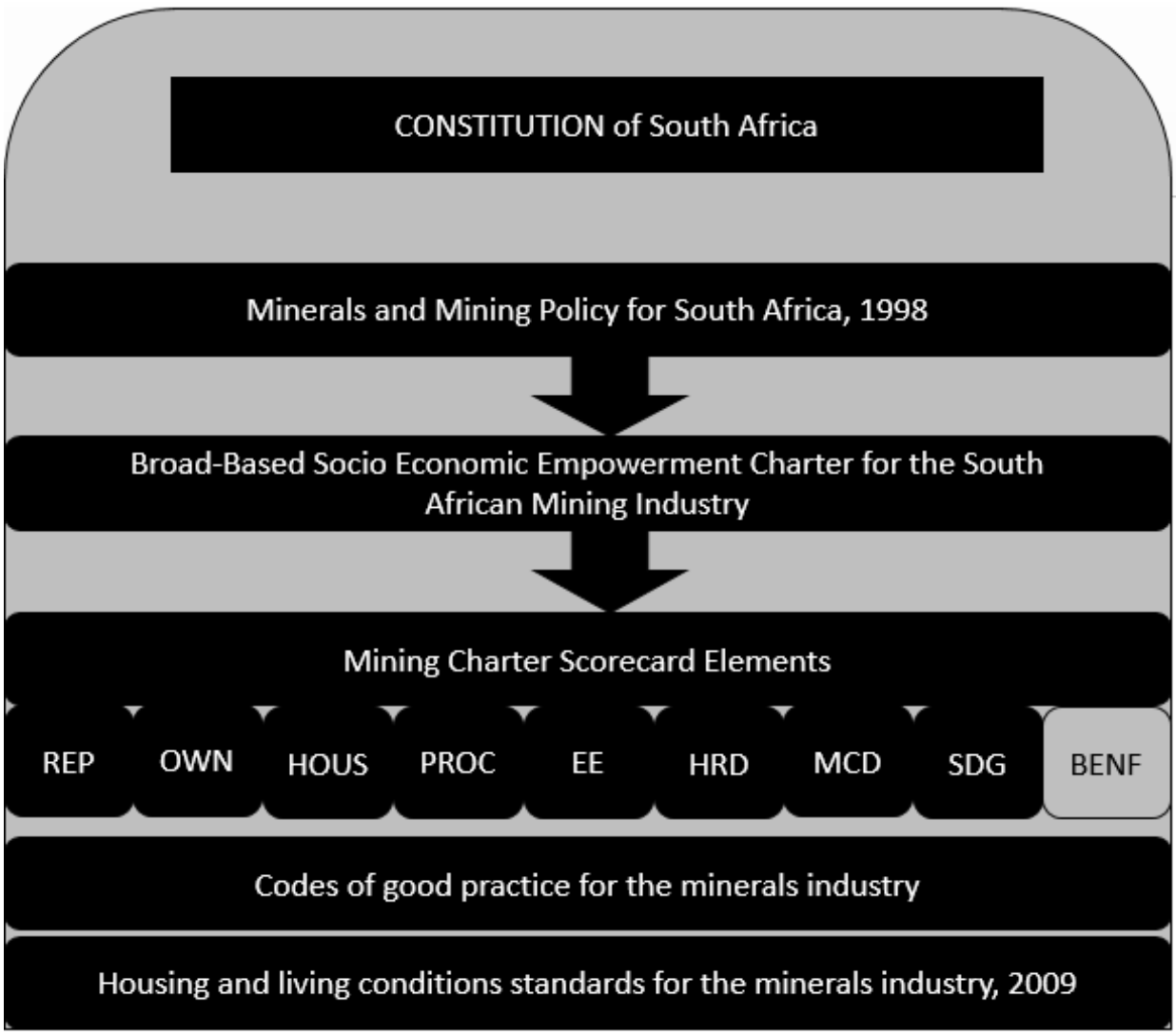


Figure 3: A structure of the transformation policy framework for the mining industry (Department of Mineral Resources, 2015)

2.6.2 Scoring Principles

Table 2 below sets out the performance measures prescribed by the Charter. These measures include targets and compliance dates.

Table 2: Scoring principles for the elements of the charter (Department of Mineral Resources, 2015)

Element	**Scoring Principle**
Reporting	Percentage of companies that have reported on the Charter requirements
Ownership	**Category 1:** Equal or greater than 26% HDSA but does without all three identifiable beneficiaries i.e. Entrepreneurs, ESOPS & Communities. **Category 2:** Equal or greater than 26% HDSA without trickle cash flow to HDSA. **Category 2+:** Equal or greater than 26% HDSA ownership, broad-based, reported trickle cash flow to HDSA. **Category 3:** HDSA ownership below 26%.
Housing and Living Conditions	100% conversion of hostels using the following measures: One person per room by 2014. Conversion of hostels into family units by 2014.
Procurement and Enterprise Development	Percentage expenditure from BEE entities by 2014: Capital goods = 40%, Services = 70%, Consumables = 50% and 0.5% of annual spend on procurement from multinational suppliers
Employment Equity	HDSA representation: Top Management = 40%, Senior Management = 40%, Middle Management = 40%, Junior Management = 40% and Core Skills = 40% by 2014
Human Resource Development	Payroll expenditure on training 2014 target was 5% of total annual payroll (excluding mandatory skills development levies) to be spent on HRD
Mine Community Development	Implementation of mine community project commitments by December 2014
Sustainable Development	Percentage implementation of the tripartite plan on mine health and safety, 2014 targets were Environment Management Plans = 100%, Tripartite Action Plan = 100% and Percentage of samples in South African facilities = 100%
Beneficiation	Contribution of a mining company towards beneficiation (this measure is effective from 2012)

2.7 Empowerment deals in the Mining Industry

2.7.1 Chamber of Mines assessment of members' empowerment transactions in the industry

Current empowerment policies are said to encourage redistribution rather than productive ownership. Where this productive ownership has occurred has not been by way of policy design, but by chance with inequitable benefit distribution. Sustainability of shareholding has been extremely difficult, due to high debt levels of empowerment partners who are also restricted from trading shares (Cargill, 2010).

Meaningful economic participation in relation to HDSA beneficiaries has four key attributes as described in the Charter which include (Department of Mineral Resources, 2010):

- Identifiable HDSA beneficiaries in the form of BEE entrepreneurs, workers and communities;
- Cash flow to BEE partners throughout the term of the investment and the ability of BEE entities to leverage equity to facilitate sustainable growth of the BEE entities;
- HDSA participants should have full shareholder rights including participation at general meetings and exercising voting rights;
- And lastly that ownership shall vest within the agreed timeframes.

The Chamber of Mines has recently released a report, which attempted to demonstrate the economic empowerment of HDSAs in the mining industry, in line with requirements of the Charter. The report aggregated overall company performance (members of the Chamber of Mines) based on the DMR's submissions, as at 31 December 2014. According to the report:

- Chamber of Mines members have reached 38% of meaningful economic participation by HDSAs, significantly higher than the 26% required by the Charter;

- Numerous commodity groups have all achieved, or surpassed, ownership targets for HDSA as outlined in the Charter: Coal achieved the highest ownership percentage at 47.2%; whilst Platinum-Group Metals (PGMs); manganese, iron ore chrome and gold where all above 27.2% with the exception of diamonds at 26%
- 63% of the HDSA population that has benefited are BEE entrepreneurs, with communities and employees at 22% and 15% respectively.

Figure 4 depicts the ownership patterns according to the commodity segment, and the beneficiary category. From Figure 4, it is clear that the majority of beneficiaries from the deals completed are BEE entrepreneurs. This has attracted criticism with regard to the structure of the deals, in that they benefit only a few individuals, rather than a larger pool.

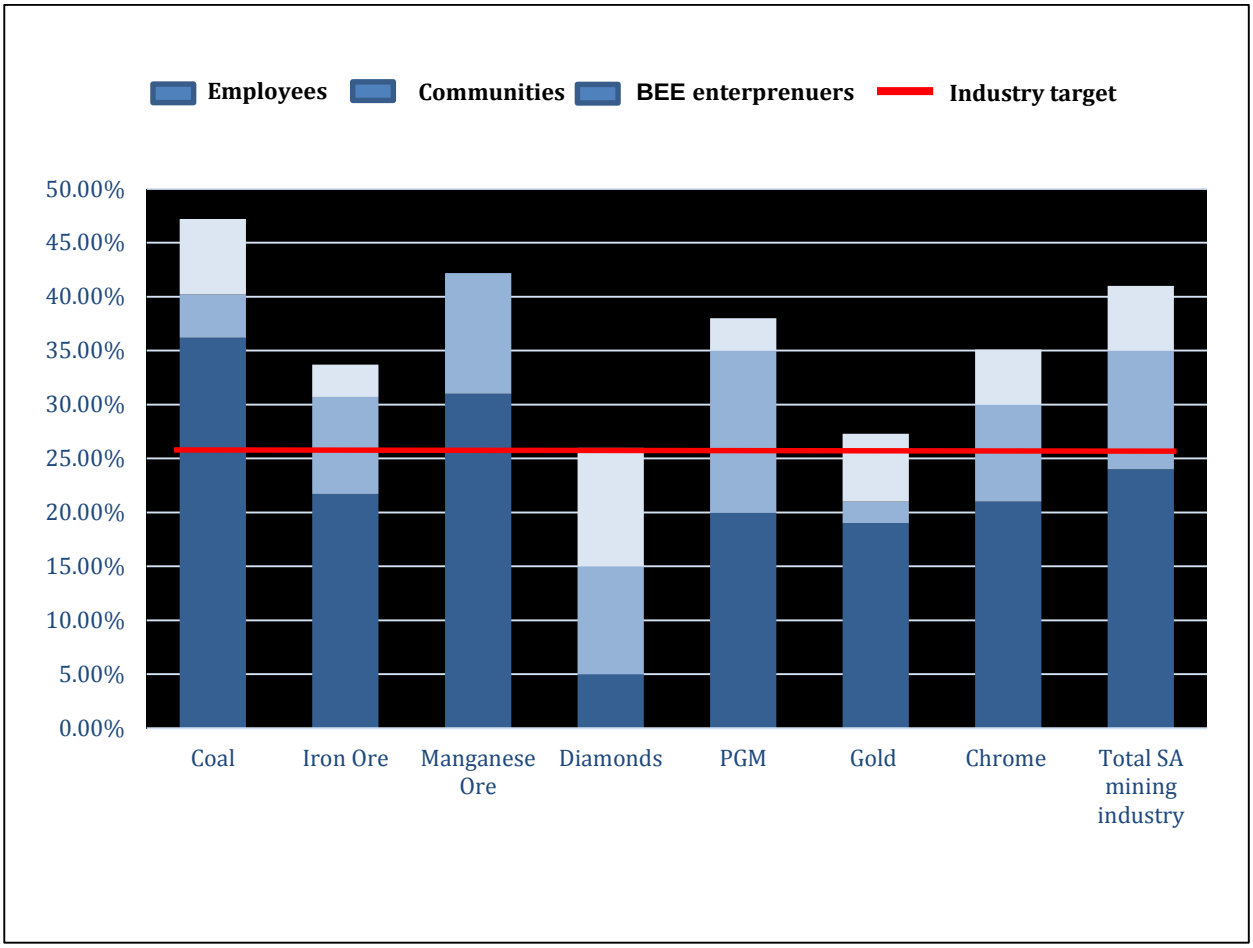


Figure 4: Portion of ownership of mining industry transferred to HDSA (Wu and Moodley, 2009)

When assessing the total value of reported empowerment transactions from 2004-2008, the mining industry had its highest transactions in 2007 not only in value but also in volume terms. More than R40 billion in transaction value was amassed underlined by 34 transactions. Figure 5 below depicts the transaction value through this period (Wu and Moodley, 2009).

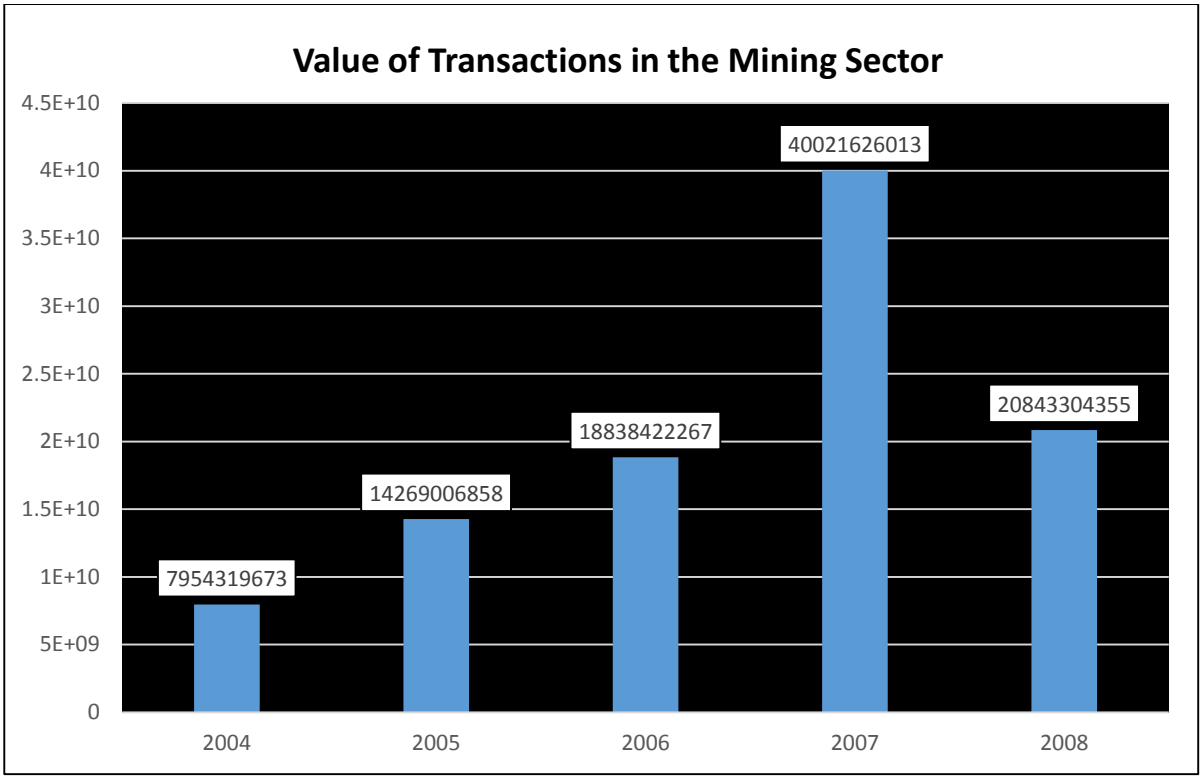


Figure 5: Value of transactions in the mining sector (Wu and Moodley, 2009)

Figure 6 below depicts the increase in value of the Johannesburg Stock Exchange (JSE's) resources index from 2005 reaching a peak in mid-2008, then declining in the latter part of 2008. This trend in the Resource 20, which denotes the performance of mining companies on the JSE is similar to the trend denoted in figure 5 (Wu and Moodley, 2009).

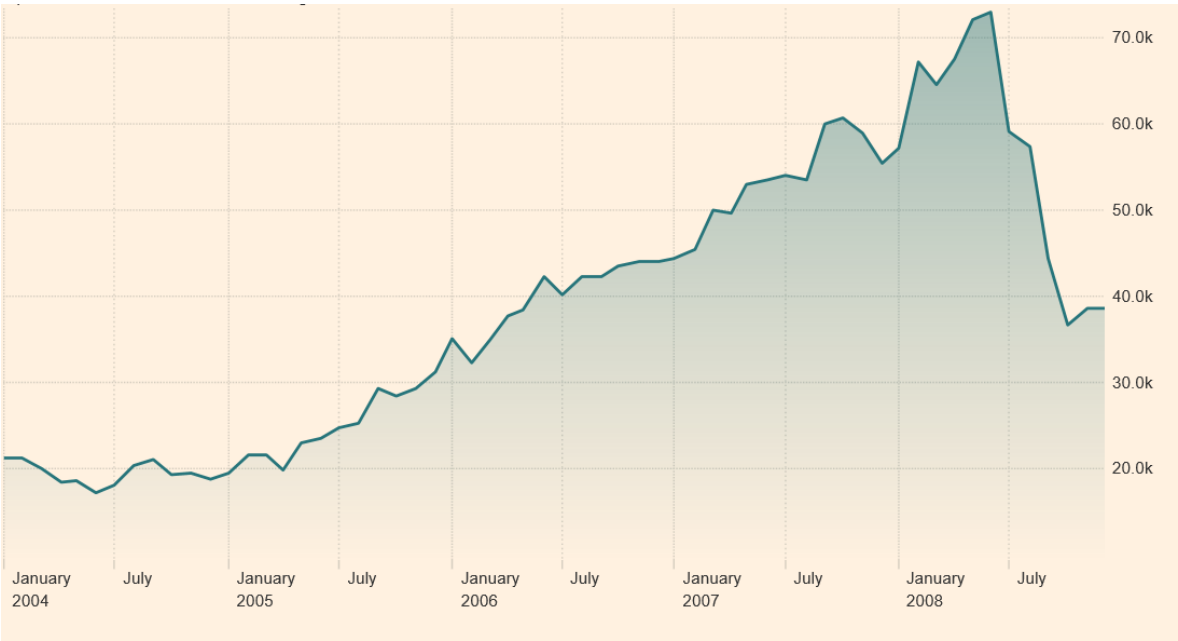


Figure 6: Resources 20 index (Financial Times, 2016)

2.7.2 Transactions involving employee schemes and community trusts

From 2004-2008, only 7% of the mining sector transactions during that time involved ESOPs; and only 10% involved community-ownership schemes, as shown in Figure 7 below. Lack of meaningful participation from employees in the schemes, is indicative of the popular models for ownership transactions that have been adopted in the industry. These transactions were not broad based resulting in limited benefits for employees and other stakeholders (Wu and Moodley, 2009).

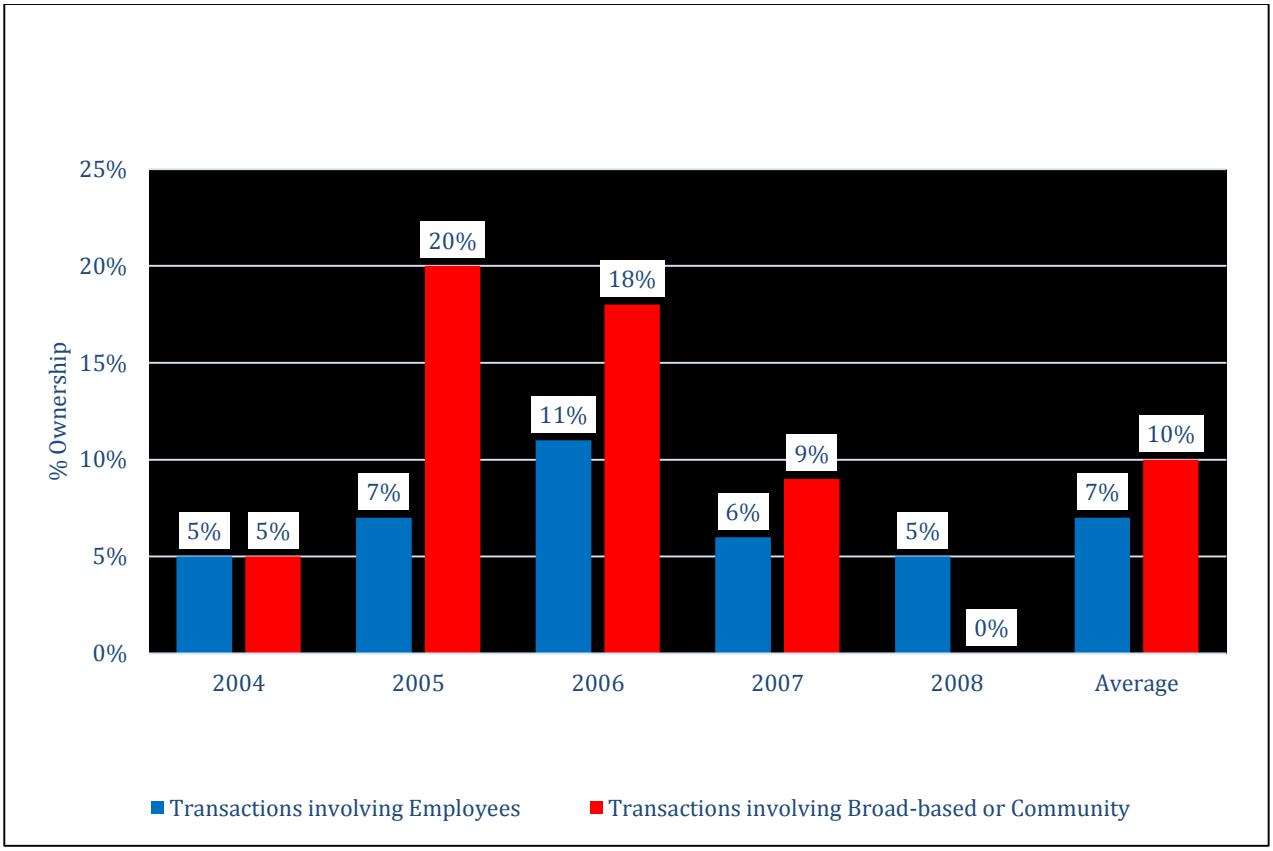


Figure 7: BEE transactions involving employees and communities (Wu and Moodley, 2009)

2.7.3 Company transactions

Table 3 below represents some of the notable empowerment transactions conducted in the mining industry over the past decade. Wu and Moodley (2009) found that Anglo American and its subsidiaries completed the largest number of empowerment deals in the industry, with 10 reported transactions with a combined value of approximately R28 billion as at December 2009.

In their analysis, Impala Platinum followed the list of mining companies corporates with 8 empowerment deals valued at R19.3 billion, with most of the empowerment transaction value emanating from the Royal Bafokeng Nation's acquisition of its 13% stake in Impala Platinum – valued at R10.6 billion.

Table 3: Top 10 contributors and vendors to BEE transactions (Wu and Moodley, 2009)

Rank	Contributing entity/ Vendors	Total Value of Transactions (Rand)	Total Number of BEE Transactions
1	Anglo American Group of Companies (including Anglogold Ashanti, Anglo Platinum and Scaw	28,103,448,800	10
2	Impala Platinum	19,363,000,000	8
3	Kumba Iron Ore (KIO)	9,200,000,000	2
4	Northam	6,250,000,000	2
5	Xstrata	5,370,000,000	3
6	Arcellor Mittal	4,200,000,000	1
7	Harmony Gold	3,573,314,660	3
8	Aquarius Platinum	2,722,526,000	4
9	De Beers	2,000,000,000	4
10	Sasol	1,855,000,000	1

2.7.4 Summary of benefits to beneficiaries

The Chamber of Mines asserts that over the 12-year period that the Mining Charter has been in effect, a minimum of R47 billion in dividends has accrued to HDSA participants (BEE entrepreneurs, employees and communities), which in their analysis was found to represents 19.6% of the dividends paid over the same period by Chamber of Mines members (Chamber of Mines South Africa, 2015). Figure 8 provides a breakdown of the transactions and the accrued benefits.

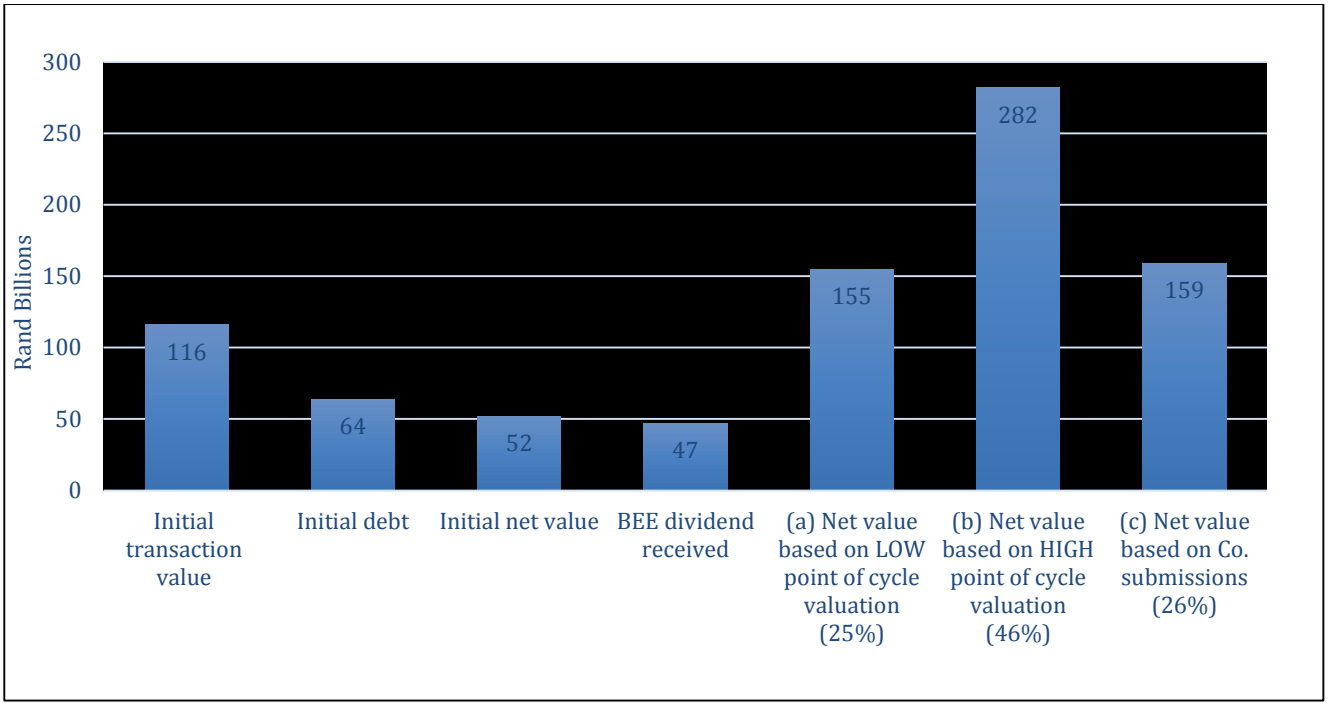


Figure 8: Meaningful economic participation of HDSA (Chamber of Mines South Africa, 2015)

At the lowest point of the commodity cycle, the net value of the transactions was R155 billion according to the Chamber of Mines; whilst at the high point of the cycle, the value of the transactions totalled R282 billion. These two points were highly dependent on company share price performance.

The initial transaction value of all empowerment deals, of members in the Chamber of Mines was R116 billion with an initial debt of R64 billion. The completed transactions have generated significant returns for participants with a net value of R159 billion (Chamber of Mines South Africa, 2015). For a complete breakdown of

the BEE transactions that have taken place in the various commodity groupings, see Appendix 1.

2.7.5 Assessment by The Department of Mineral Resources on the industry's performance in relation to the Charter

The assessment conducted by the department in 2009 outline weaknesses in company performance as per the Charter requirements in relation to HDSAs. This included a conspicuous lack of transfer of ownership, access to funding, indebtedness, limited flow of dividends to HDSAs to service loan agreements, onerous transaction conditions and financially cumbersome deal structures. According to the assessment, BEE ownership was concentrated in a few black beneficiaries. In 2009 aggregated ownership was at 9% against a target of 15% (Department of Mineral Resources, 2015).

The 2014 assessment of the Charter concluded that although mining companies have reported to the department to have met or exceeded the 26% HDSA ownership target, meaningful economic participation by beneficiaries remains elusive. The assessment further concluded that the number of broad based empowerment transactions involving both communities and ESOPs were low. Results from the department's assessment also found limited impact in terms of beneficiaries realising economic benefits (Department of Mineral Resources, 2015).

2.7.6 Summary

The impacts of most BEE deals have not been broad-based; with 63% of transactions from Chamber of Mines members benefitting BEE entrepreneurs with communities and employees at 22% and 15%. The value and number of transactions have coincided with the rise and fall of the JSE, making the deals expensive – due to elevated stock prices in favourable market conditions. Results from the Department of Mineral Resources assessment found limited impact in terms of beneficiaries realising economic benefits.

One of Anglo American's well known former CEO's Clem Sunter has said that one of the solutions to the current endemic problems in the mining industry is for greater participation by employees in companies. This can achieved through the use of ESOPs to ensure income inequality is reduced in South Africa, he added (Visser, 2004).

Sunter, who was one of the original proponents of the idea is of the opinion that ESOPs have never been adequately explored. He regards the implementation of ESOPs as a fairer way of implementing BEE as it relates to ownership of capital. As an experienced previous executive in Anglo American, Sunter believes ESOPs are a better alternative to the BEE deals that have been completed, often making a few well connected black individuals wealthy, whilst not being sure of the value ad these individuals make to the company as passive investors. Often their knowledge of the industry in which they participate is limited (Sunter, 2012).

With this background in mind, Section 2.8 will focus on ESOPs.

2.8 ESOPS

Traditionally the relationship between company owners, management and labour has been fractious and at times dysfunctional. This dynamic has made labour relations challenging, and not geared toward making organizations reach their full potential. ESOPs establishes unity of interests between management and labour, owners and employees (Rosen et al., 2005).

Today's business environment is characterised by fast changing technological advancements and requires a workforce that is engaged and responsive, qualities that are too often stifled in traditional organisations. *"The organisation that permits participation ultimately produces individuals who are responsible to participate"* (Beirne, 2006).

2.8.1 The need for ESOPs

Postlethwaite et al. (2005) have found that those companies that have embedded ESOPs in their business model, have performed better than those have not through productivity gains, higher innovation, superior customer loyalty, and improved talent management.

As Postlethwaite et al. (2005) established, this is mainly because those ESOPs that have prospered combine three critical factors that ensured the success of the scheme. These comprise financial incentives, employee-involvement mechanisms, and the instilling of a culture of ownership.

Most companies with employee share-ownership schemes already possess these attributes as single entities. The best results are achieved through the combination of all 3 virtues. Where the company is completely owned by employees these attributes exist (Postlethwaite et al., 2005).

When analysing the failures of some ESOPs, Postlethwaite et al. (2005) found how some employers make the mistake of simply assessing their business and the sector, reviewing their best practice, and concluding that the secret is simply employee-share ownership and good communication. They would then emulate that part which they thought was the most important, or just the part that they admire. However, as a growing number of businesses have discovered, it is the whole package that works best.

An employee's ability and opportunity to contribute to decision making, supplemented by meaningful financial incentives, is that which creates a conducive environment for employees to disseminate information about process failures and improvement opportunities. Companies with successful ESOPs create mechanisms for employees' contributions to be heard, and timeously acted upon. This is in contrast to a working environment that is bureaucratically centralised in its structure and working culture (Postlethwaite et al., 2005).

Postlethwaite et al. (2005) discovered a strong negative relationship between a company's ability to innovate and a centralised bureaucratic organisation. This facilitates adverse behaviours and attitudes amongst employees; stifling new ideas and innovation as well as resisting suggested improvement methods from management.

Those companies that offered broad based ESOPs far outperformed these companies. From their study, Kruse concluded that while broad based ESOPs are not a guarantee for improved performance and employee attitude, it does help on average to improve productivity, profitability, organizational commitment and other employee attitudes (Rosen et al., 2005).

2.8.2 How ESOPs are structured

A company can create a trust fund for employees, which would serve as a holding structure for an ESOP. The company would then have the option of either subsidising the trust with funds to purchase shares, or contribute shares directly to the plan. The company could also provide guarantees allowing the trust to borrow money to purchase shares. A combination of all three can also be adopted (The National Center for Employee Ownership, Undated). Employers can also afford shares directly to employees.

Usually, employees are exempt from paying taxes on their contributions until they receive the shares or proceeds from the ESOP; but when they sell, they are then liable for taxation; alternatively, this may be the case when they leave the company or retire. Once this has occurred, the employee has the option to either sell the shares on the market, sell them back to the company, or alternatively to keep the shares (The National Center for Employee Ownership, Undated).

2.8.3 Various ESOP models

ESOPs vary in architecture depending on the desired outcome. Success measures such as productivity improvements, increased dividend flows, an engaged and responsive labour force, lower operating costs, higher quality returns are but some of these measures (Hunt, 2013). The different variations are detailed below.

2.8.3.1 Share Appreciation Rights

One of the more common structures used are share appreciation rights. These rights give employees the option to cash out, or get payment in shares or a combination or both on any appreciation in share value of the concerned entity.

If a specific entity has a share value of R100 per share at the inception of the scheme, and a value of R800 during the vesting period, employees are entitled to R700 in cash or R700 worth of shares. These shares are accounted for in employee remuneration as gross income in the year where the scheme matures (Hunt, 2013). Table 4 below contains some of the advantages and disadvantages of this type of scheme.

Table 4: Advantages and Disadvantages of Share Appreciation Plans (Hunt, 2013).

Advantages	Disadvantages
They work well in rising markets	The plan does not work well in in depreciating market
When cash settled share dilution in the company is minimized	Share ownership is diluted when settled using shares
Assist in retaining the right staff, whilst ensuring that those exiting the company do so without those incentives	Continued disaggregation of shareholders makes the scheme difficult to administer when settled using shares
Easy to administer when cash settled	
Is administratively easy especially if cash settled	
Rights settled using equity ensures better management of profit and loss outcomes	

2.8.3.2 Share Performance Plans

These shares are linked to overall company performance and are used to incentivize employee productivity and align employer and employee objectives. These shares are conditional on the company meeting specified share performance targets.

If the share price of a company is R100 per share at the date of inception, and appreciates to R800 per share at maturity, employees are entitled to the specified number of shares at R800 per share. Similar to share appreciation schemes, performance shares are treated as gross income and subjected to Pay as You Earn (PAYE) (Hunt, 2013). Table 5 stipulates some of the advantages and disadvantages of share performance plans.

Table 5: Advantages and Disadvantages of Share Performance Plans (Hunt, 2013).

Advantages	Disadvantages
Performance plans work well in appreciating and depreciating markets	Free share allocation creates dilution effect
The scheme imposes performance criteria on beneficiaries	Beneficiaries may become disillusioned if performance criteria is arduous
The scheme is easy to implement	Implementation becomes complex with increasing shareholder base
Profit and loss metrics' are easily managed	

2.8.3.3 Forfeitable Share Plans

Forfeitable share incentive plans are plans structured to afford employees free shares on condition that they comply with specific company provisions. In the event where these conditions are contravened, the shares revert back to the company or special purpose vehicle chosen.

Conditions imposed on this scheme may be performance related or employment period related. Beneficiaries of the scheme receive dividends and profit from share appreciation. These structures may also be structured such that they are cash settled at maturity performance, shares are treated as gross income and subjected to PAYE (Hunt, 2013). Table 6 contains some of the advantages and disadvantages of this plan.

Table 6: Advantages and Disadvantages of Forfeitable Share Plans (Hunt, 2013).

Advantages	Disadvantages
Performance plans work well in appreciating and depreciating markets	Free share allocation creates dilution effect
The plan is flexible and provides a capability impose performance criteria	Beneficiaries may become disillusioned if performance criteria is arduous
Profit and loss metrics' are easily managed	Implementation becomes complex with increasing shareholder base

2.8.3.4 Deferred Annual Bonus Plans

These plans include the deferral of beneficiaries' annual bonus payments towards purchasing shares. Most of these plans have been used as successful retention strategies performance shares are treated as gross income and subjected to PAYE (Hunt, 2013). Table 7 contains some of the advantages and disadvantages of this plan.

Table 7: Advantages and Disadvantages of Forfeitable Share Plans (Hunt, 2013).

Advantages	Disadvantages
The plan has good retention elements	Participation rates from employees tends to be low
Ideal for investors for employee purchased shares	May become disincentive if performance conditions too arduous
Performance conditions may be imposed on the plan	Gross employee earnings may be significantly increased if bonuses increased to facilitate deferral
Provides ability to manage short and long term performance	

2.8.3.5 Broad-based share ownership plan

Broad based share incentive plans are commonly implemented to attract and retain specific qualifying individuals to the company. The plan not only assist in aligning the financial interests of the company but also can be used to meet specific regulatory requirements. To qualify as a broad-based share incentive plan in terms of the income tax Act, the plan must comply with the following requirements:

- Participants must directly purchase shares in the company
- Employees may only be restricted from selling shares for 5 years
- The combine market value of the shares may not exceed R50, 000 (Hunt, 2013).

2.8.4 Characteristics of successful ESOPs

Successful ESOPs are buttressed by a shared mind-set, which is anchored by 3 fundamental pillars. The first of these pillars is equity, the second is culture, making people feel and think like owners, and the third is a common understanding of key business disciplines and a common commitment to pursuing those (Rosen et al., 2005).

2.8.4.1 Equity Ownership

Entities that afford organizations capital traditionally own those businesses, whilst management is accountable to these owners. If the company does not succeed, the capital providers carry all the risk in the business, whilst claiming all the earnings and returns if the entity succeeds. These capital providers are concerned with the success and prosperity of the organization (Rosen et al., 2005).

The challenge these owners face is pursuing profits and growth with a workforce that is not aligned with the goals and aspirations of the organisation. Companies have tried addressing this challenge with other tools such as performance reviews, motivational speeches and team building exercises in hopes that employees will inspired to perform better. Employees are incentivized with bonuses, salary increases, promotions with the expectation and employees will align with company objectives (Rosen et al., 2005).

The confrontational relations between labour and management has created an environment where strike and lockout are used as tools to advance individual interests. These interactions are supported by the premise that collective labour is willing to disadvantage the company in order to further their own individual goals (Rosen et al., 2005).

The principle underlying ESOPs is that employees are incentivised through ownership to pursue long term success of the business. The ability to garner support for the ESOP when it comes to equity is dependent on the amount of equity the organization provides. Insubstantial and intermittent share offerings will unlikely make recipients recalculate their economic interests (Rosen et al., 2005).

2.8.4.2 Ownership Culture

Organizational culture has transformed over time, previously characterized by a command and control ethos where employees did as they were told. Employees of these organizations were part of a rigid hierarchy where individuals could not contribute to decisions made. The rigid structures was further accentuated by dress code, hours worked, freedom to come to and go, pay and bonuses, parking spaces and other indications of power and status (Rosen et al., 2005).

To establish an ownership culture organizations need to eliminate the ‘us’ versus ‘them’ mentality that has plagued many organizations. An approach that could be used to mitigate this behavioural framework is to constantly communicate with staff. This entails sharing information about the organization relating to its operations including much of the financial data to which investors and analysts are traditionally privy to and that senior managers use to run the business (Rosen et al., 2005).

Employees need to get a sense that are aware of operational financials that managers use to make decisions. A second approach would be source the opinions of employees when making important decisions. This does not in any way advocate for people voting on everything and making every decision. This approach seeks to engender a sense of collective decision making on those decisions that affect the whole company (Rosen et al., 2005).

2.8.4.3 Business Discipline

In organizations that have successfully implemented ESOPs, employees are concerned with, and drive the business disciplines that help their company do well. Employees are taught their companies' key business disciplines. These successful organizations are staffed with employees who understand how to contribute to improving performance and how to measure the results. Employees in these organizations are engaged and have managed to successfully embed the principle of driving business discipline by doing the following:

- Identifying critical performance metrics;
- Outlining performance objectives and targets;
- Sharing ideas on how to improved performance;
- Continuously monitoring and tracking those critical performance metrics;
- Celebrating and rewarding wins (Rosen et al., 2005).

2.8.5 Benefits of Establishing an ESOP

ESOPs can be used as a vehicle to facilitate the sale of the shares over a period of time, whilst ensuring employees still retain the capability to sell their shares to other employees when parting ways with the company. Apart from incentivising the desired behaviours by employees in an organisation, ESOPs can form part of an employee's company benefit package (Voison and Volaw, 2007).

Effective ESOPs create a working culture where an employee's individual enterprise is stimulated which ultimately leads to improved productivity. Employees in these organisations, because they are empowered as owners of the business, tend to be more entrepreneurial when solving problems. They possess more creative ideas for solving problems in the organization. Consequently, these employees take ownership of their decisions and exercise more discretion when carrying out tasks (Postlethwaite et al., 2005).

According to Postlethwaite et al. (2005), these factors foster an environment where employees are motivated and empowered to act in the best interests of the organization – via a collective voice.

Gamble et al (2001) studied the correlation between job satisfaction and improved company performance. Employees that were beneficiaries of ESOPs were found to have a higher job satisfaction which resulted in improved company performance. The study also investigated the employment setting of these companies. Working conditions in these organisations where characterised by the following:

- Suitable working conditions
- Ability of employees to participate in the decision making process
- Employees displayed an intimate knowledge and understanding of company's key business drivers
- Employers and employees were aligned in their goals (Gamble et al., 2001)

There are common traits found in companies that encourage ESOPs. These companies are more innovative and stable, with a staff turnover that is lower than companies without ESOPs. Companies with effective ESOPs poses faster employment growth and higher rates of survival (Rosen et al., 2005).

2.8.6 Criticism of ESOPs

Transforming employees into owners reduces the overall company costs. This in part is due to the fact that as employees become more aligned to company owners, the overall company cost is reduced through productivity gains and improved company performance. However, this may create corporate governance failures as the line of separation between ownership and control becomes blurred (Mitchell et al., 2005).

Abdullah (2006) studied the implementation of ESOP and its effect on corporate governance. He found that the application of ESOPs are not associated with a return on assets, however he did find a negative correlation between the use of ESOPs and corporate governance.

Some of the strongest weaknesses of ESOPs is the lack of excitement generated within the company at the different levels. Those charged with the responsibility of implementing ESOPs in companies, often treat ESOPs as just another benefit or financial tool. These include company owners, human resource practitioners and finance professionals (Rosen et al., 2005).

Managers, often responsible for business execution are not encouraged to run the business differently. Employees are not educated and informed about what is meant to be an owner, and are neither expected to change their approach to their jobs. Due to the erroneous application of ESOPs, companies are unable to tap into the immense energy, intelligence and extra effort throughout the organization required to meet today's global business challenges (Rosen et al., 2005).

Criticism levelled at ESOPs include that they are highly dependent on tax breaks and favourable accounting treatment. Critics have claimed that ESOPs cannot, as independent structures, lead to improved company performance (Rosen et al., 2005).

Winther et al. (1997) concluded that ESOP implementation does not necessarily result in increased profits. They focused on 110 companies with the key areas of focus being on productivity and profitability. The results of the study was that ESOPs had little or no impact on profits, however the analysis highlighted increased productivity.

2.8.7 Financing an ESOP

In most cases ESOPs are funded by employers through structured loan facilities to the designated holding structure of the ESOP. The loans mostly have favourable repayment conditions in lieu of forgoing dividends used to repay the loan. When a company has a strong balance sheet, on occasion, ESOPs may be directly funded by the company and the debt owed by the holding structure settled outright (Voison and Volaw, 2007).

There are other common financing instruments used to finance ESOPs, such as bank loans where the employer acts as a guarantor. Other funding mechanisms include call-option agreements, where the holding structure may only purchase shares from those financial institutions that originally financed the purchase of the shares (Voison and Volaw, 2007).

2.8.8 ESOPs in other parts of the world

The USA has for many years led the way with regard to ESOPs with other countries following suit with application of these principles in their companies. The United Kingdom, through many of their large corporations have some kind of broad ownership plan, whilst in Ireland large energy companies offer ESOPs. Other European countries that offer similar arrangements include Spain and Italy, offering worker co-operatives in their important sectors (Rosen et al., 2005).

ESOPs have been used by other countries to privatize state owned entities, countries include Poland, Russia, Slovenia and Hungary. China's government has allowed employees to buy shares in enterprises it owns. ESOPs have been used in other countries such as Australia, Egypt, Jamaica and Kenya (Rosen et al., 2005).

Freeman and Knoll (2008) conducted an empirical study using 10 years of data from companies in the USA that have implemented ESOPs. Their study showed that the implementation of ESOPs led to an average increase in productivity and profitability that benefited both employees and employers. Their study found that ESOPs

accounted for $14 billion annually in equity contributions, plus $3 Billion attributable to increased job stability, as well as non-qualified benefits of greater work satisfaction and reduced stress (Freeman et al., 2008).

Jones et al. (2006) studied a large data set from publicly listed entities in Finland and concluded that the implementation of ESOPs in organisations improved company performance. Most companies in the UK have used ESOPs for the purpose of tax incentives as the main reason for implementing ESOPs (Robinson et al., 2005).

ESOPs have been implemented successfully by many international companies in many different sectors. Construction companies, banks, insurance companies, textile manufacturers, architectural firms, health care providers, hotels and resorts and many other industries have successfully employed ESOPs (Rosen et al., 2005).

2.8.9 Summary

In summary, ESOPs enable extensive employee ownership; and they have the ability to foster a sense of individual enterprise that fuels productivity in companies that have imbued a culture of ownership amongst their employees. ESOPs generally contribute positively to company performance; and they provide a stable and dynamic working environment, when administered effectively. ESOPs cannot be implemented in isolation; but they require a combination of factors to make them successful.

There are different ESOP structures and funding models that can be adopted depending on the desired outcome. Section 2.9 seeks to give a broad summary of ESOPs conducted in SA, and the different structures adopted.

2.9 Overview of ESOPs in South Africa

A number of companies have implemented ESOPs in their organisations. Table 8 below contains a summary of ESOPs across multiple companies operating in different industries and all adopting a company specific model.

Table 8: Summary of ESOPs in SA (Motswenyane, 2009).

ESOP Transactions				
COMPANY	DESCRIPTION	TERM	FUNDING RATE	DIVIDENDS
ABSA BANK	Employees part of BEE consortium (effective 1% stake in ABSA). General ESOP for all employees (not only HDSA) provided a further 1%	5 year vesting period 7 year lock in period	Maximum implied funding rate of 7.5% per year	No dividends earned until shares are acquired
AngloGold Ashanti	ESOP for employees Patterson grades A, B and C) – c.30, 000 employees, 91.5% HDSA. 1.4% of issued share capital dispersed to beneficiaries. 30 *"free shares"* and 90 *"loan shares"* at a 10% discount to the market value	7-year term with vesting in five annual tranches from year 3.	7% on loan shares	50% dividends for debt, net dividends to beneficiaries. 100% dividends from free shares
Discovery	2 models - targeted employees would receive free shares vesting at later date. Second, employee given options to purchase shares at pre-determined prices.	5 year vesting period	No funding cost.	No dividends to employees until shares are owned
Standard Bank & Liberty Life	ESOP for all non-management employees	10 year lock-in	8.5%	Dividends used for debt
Murray Roberts &	10% sold to trusts, general employees and HDSA managers. The broad-based trust, at least 200 shares each at R3, 200 per employee	Staggered vesting periods with 10 year lock in.	Interest free.	Dividends used to repay vendor funding

COMPANY	DESCRIPTION	TERM	FUNDING RATE	DIVIDENDS
Impala Platinum	c.3% to SA employees in Patterson A, B & C grades and any new employees who join within two years.	10 years	interest free capital	Dividend post expenses, taxes and debt repayment.
Medi-Clinic	Non-management employees, 4% stake in Medi-Clinic's 15% BEE transaction.	10 year lock in period	Not disclosed	20% div. For 10 years
Edcon	Employees were sole beneficiaries of 10.66%. option structured plan with periodic cash payments	Vesting period of 3 and 6 years	26% for shares vesting in 3 years and 12.3% for shares vesting in 6 years	Dividends used to settle share funding
FirstRand	3.5% through BEE transaction, Free shares to HDSA, at R6, 000 with remainder used to incentivize and retain targeted employees.	4-10 year vesting. 10 year lock-in	80% prime less dividends received	Dividends are used to service debt
Distell	Employees owned 45% of the 15% BEE deal. Employees not involved in separate ESOP but form part of consortium	8 – 10 years	Inflation plus 7% less dividends.	Dividends used to fund the vendor loan
Group 5	4.5% to ESOP comprised a management scheme (87%) and a broad-based scheme amounting to R2, 000 per employee.	2 – 4 years	None (interest rate was set equal to the dividend yield)	No dividends till debt settled
Mutual & Federal	2 components to ESOP – free shares and share options	4– 6 years vesting 5– 8 year lock-in	Interest free	Dividends on free shares

2.10 Summary

Chapter 2 provided a broad overview of empowerment applications around the world and the promotion of preferential policies aimed at historically disadvantaged groups. These groups have been previously discriminated against on the bases of their ethnicity, race, culture, language and various other descriptions. SA has a history of discrimination on the bases of race with policies aimed at economic exclusion of black South Africans.

The South African government has enacted a number of transformation policy instruments in an attempt to empower HDSAs. For the broader economy these are governed under the BBBEE Amendment Act, whilst in the mining industry these are governed under the MPRDA, given effect in the Mining Charter. The Charter has several pillars against which transformation is measured. This report focusses on the ownership aspects of Charter.

When applied correctly, ESOPs have proven advantageous to companies. The application of ESOPs in the mining industry will be investigated. Anglo American will be used as a proxy for the mining industry, with chapter 3 outlining the company's impact and presence in the industry.

3 ANGLO AMERICAN

3.1 Anglo American as a proxy for the mining industry

In 2013, Anglo American recognised the need to more accurately measure and articulate the company's economic and developmental impact in the South African economy and society as a whole. Assisted by PricewaterhouseCoopers (PwC) and Genesis Analytics, Anglo American produced a report quantifying its impact in the industry and the broader economy.

This was necessitated by the perception that mining companies were not contributing concomitant benefits to South African society in line with those reaped by the company itself from SA's mineral endowment. Figure 9 outlines the direct economic impact of Anglo American in the South African economy. The study found that Anglo American employs 82 000 people in South Africa, and that it had directly contributed R60 billion to the South African economy in 2012.

The company accounted for approximately 2% of Gross Domestic Product (GDP); comprising wages and profits generated by the company. Apart from the direct impacts the company imparts in the economy, there were corollary indirect and induced impacts. The indirect impacts are those produced by the company's spending in the economy, thereby stimulating further spending by suppliers, contractors, etc. According to the study 126, 000 jobs and R41 billion were realised from these indirect impacts in 2012 (Genesis Analytics and PwC, 2013).

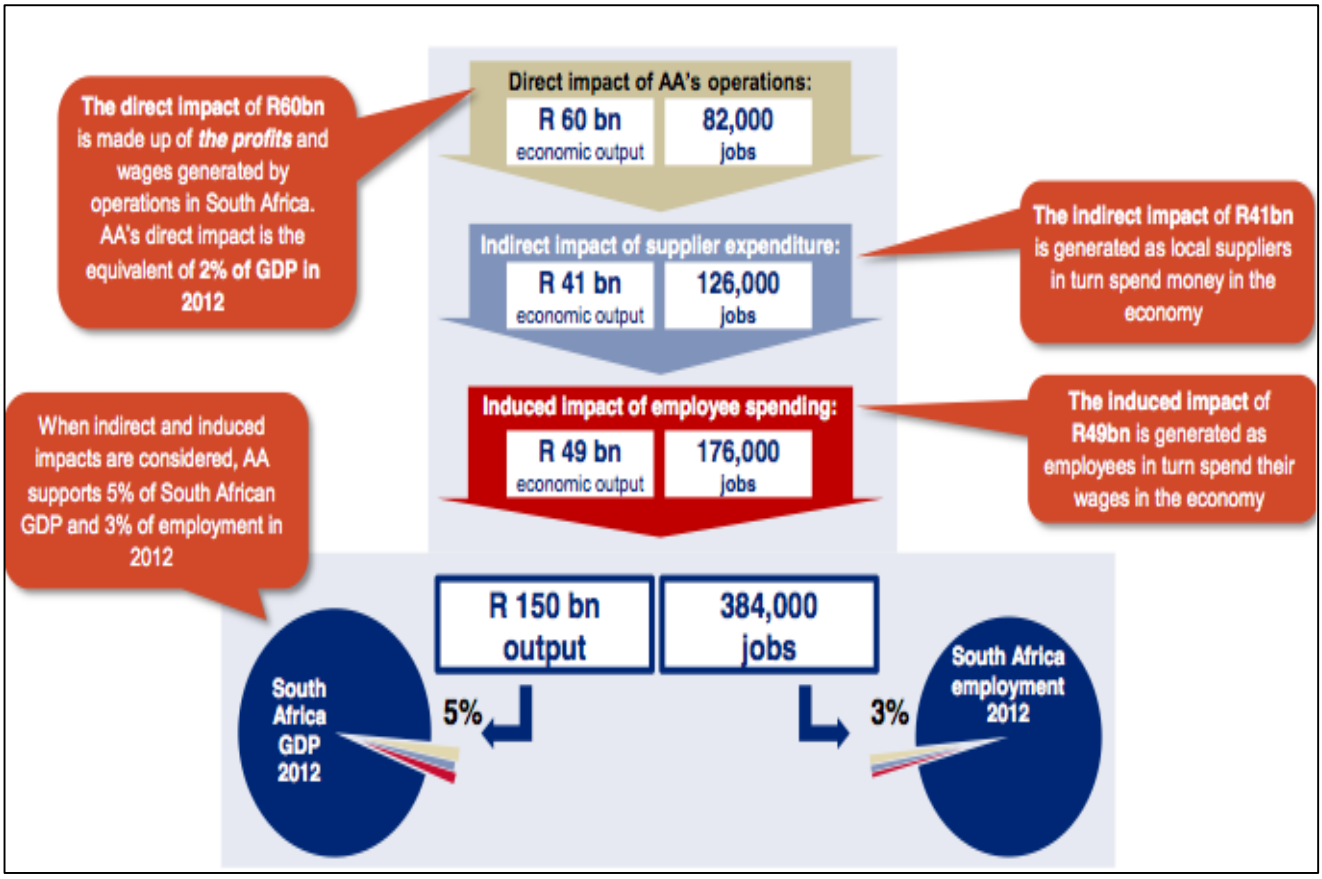


Figure 9: Anglo American's economic contribution to SA (Genesis Analytics and PwC, 2013)

The induced impacts are those produced by employees spending their money in the economy, which in turn produces jobs downstream. A total of 176, 000 jobs and R49 billion were the result of the induced impacts. In total, approximately 384 000 jobs and R150 billion resulted from Anglo American's existence in South Africa. This equated to 3% of employment and 5% of GDP (Genesis Analytics and PwC, 2013).

The mining industry, the study found, had a total capital expenditure of approximately R46.5 billion. Of this, Anglo American accounted for approximately 33% of the capital expenditure, as is depicted in Figure 10 below. Anglo American's capital expenditure, both in the form of expansionary and replacement capital, has increased from 2000-2012, as depicted in Figure 10, by an estimated eight jobs being created for every R1 million spent on capital expenditure.

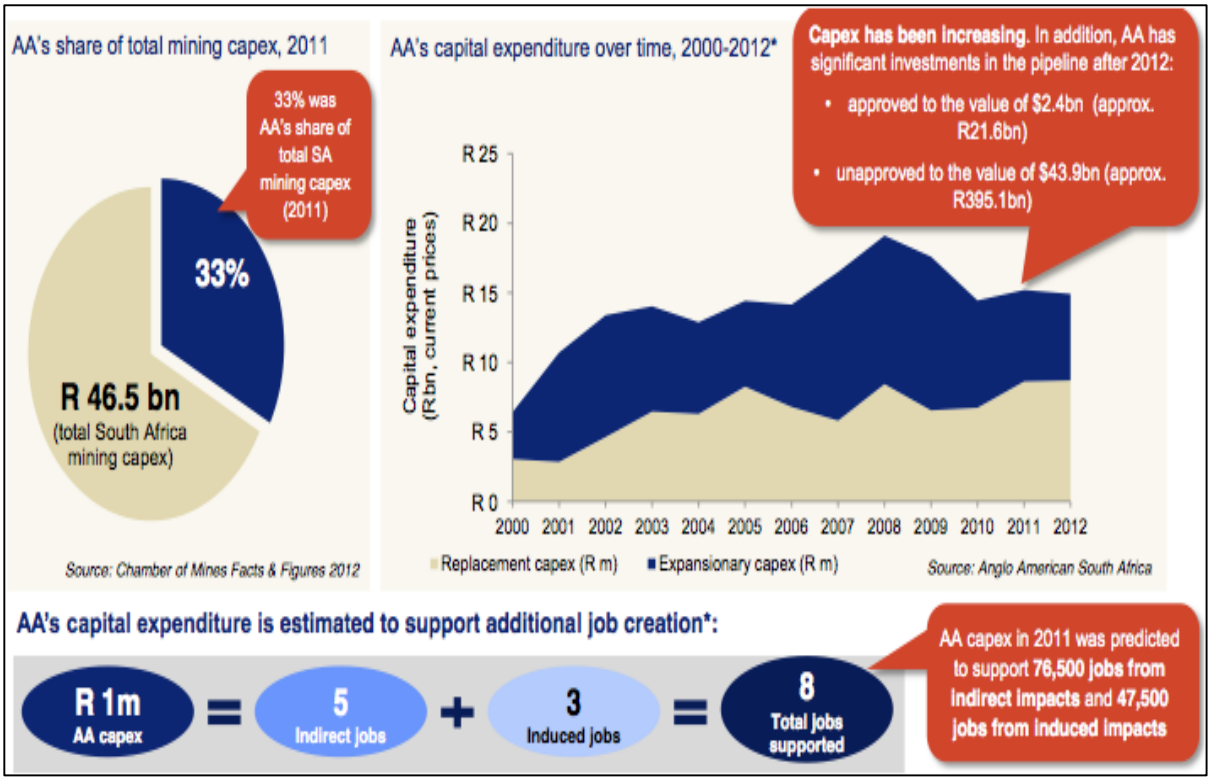


Figure 10: Anglo American's capital expenditure (Genesis Analytics and PwC, 2013)

In 2012, the mining industry's production revenue was approximately R372 billion, of which Anglo American accounted for approximately 32% of revenue, equating to R119 billion. When assessing the direct economic impact, in 2012, the mining industry contributed 9%; whilst Anglo American contributed 23% of the direct economic impact in the mining industry (Genesis Analytics and PwC, 2013).

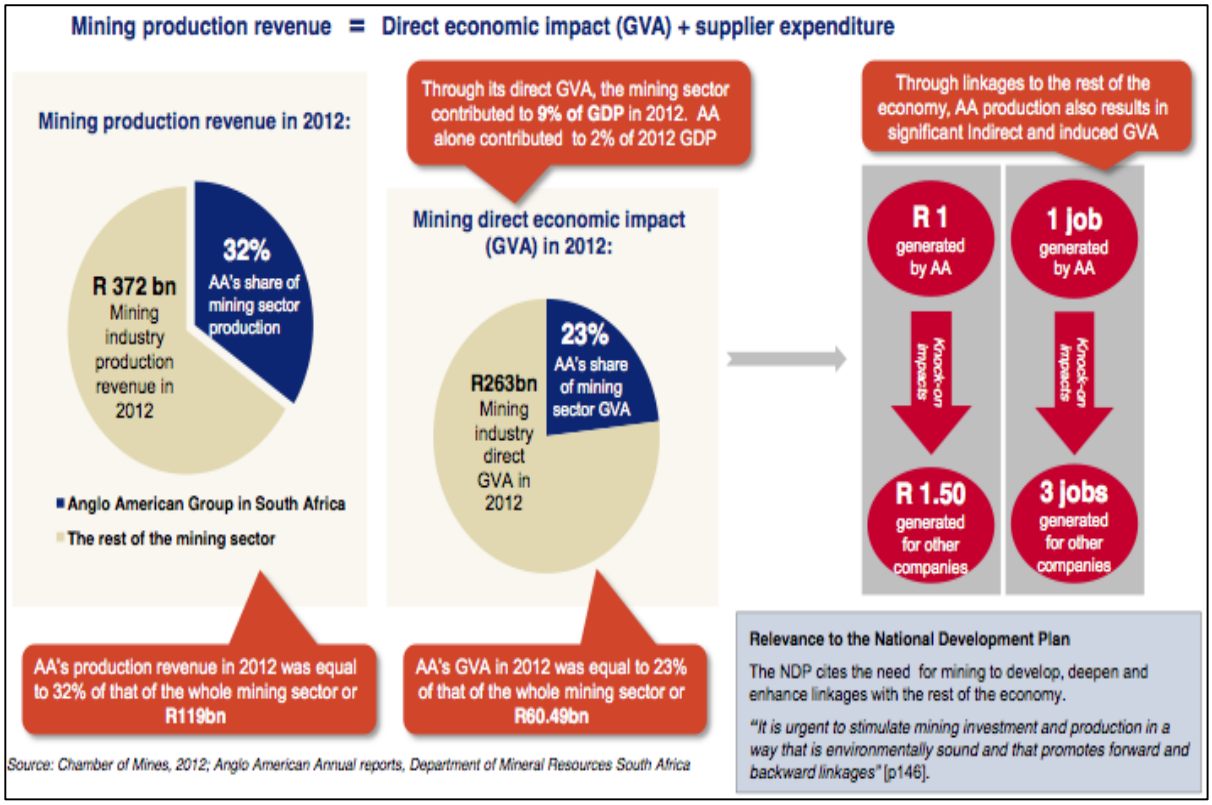


Figure 11: Mining-production revenue (Genesis Analytics and PwC, 2013)

The study also compared Anglo American's contribution to the economy with that of other sectors. It found that the direct impacts from the company were comparable to the direct impacts from the entire agricultural sector (R73 billion). It was also comparable to that of the utilities sector (R79 billion), and a little more than half the direct impacts of the entire construction sector. When indirect and induced benefits are included, Anglo American accounts for considerably more than any of the different sectors, as depicted in Figure 12.

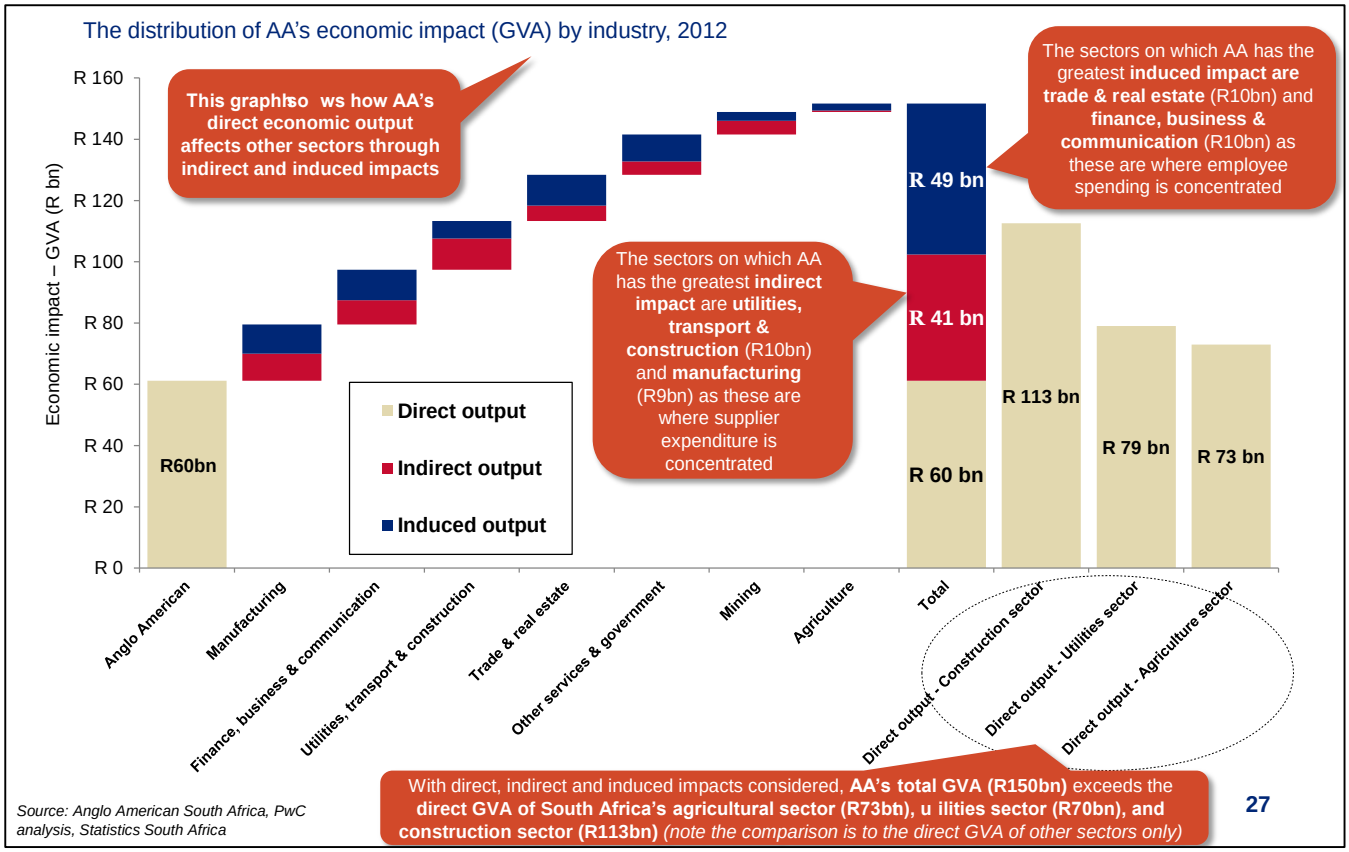


Figure 12: Distribution of AA's economic impact (Genesis Analytics and PwC, 2013)

Figure 13 depicts SA's balance of payments, together with the export revenue generated by Anglo American. Figures obtained from the South African Reserve Bank and Anglo American indicate that the company accounted for 12% of total South African exports, and approximately 41% of the total mining exports. Anglo American's coal division supplied 72% of its production for local use; whilst KIO supplied the local domestic markets full demand at prices well below the export rates (Genesis Analytics and PwC, 2013).

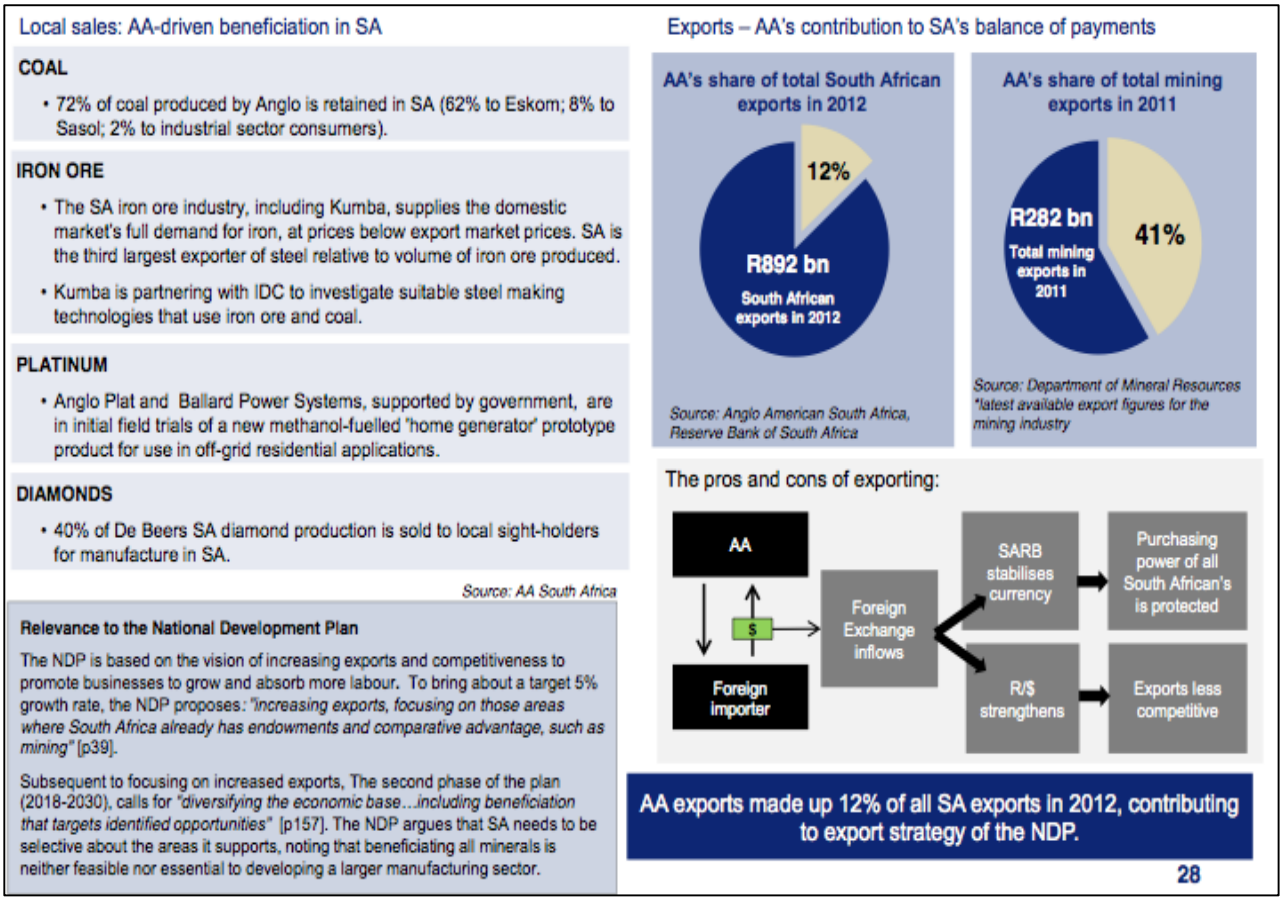


Figure 13: Local sales and exports (Genesis Analytics and PwC, 2013)

PwC and Genesis Analytics (2013) maintain that Anglo American accounted for approximately 3% of tax revenues in 2012, which equated to approximately R13.1 billion. According to their findings, this amounted to 42% of the total tax paid by the entire mining industry. This was equivalent to 68% of the public health expenditure, and 57% of the education department expenditure over the same period.

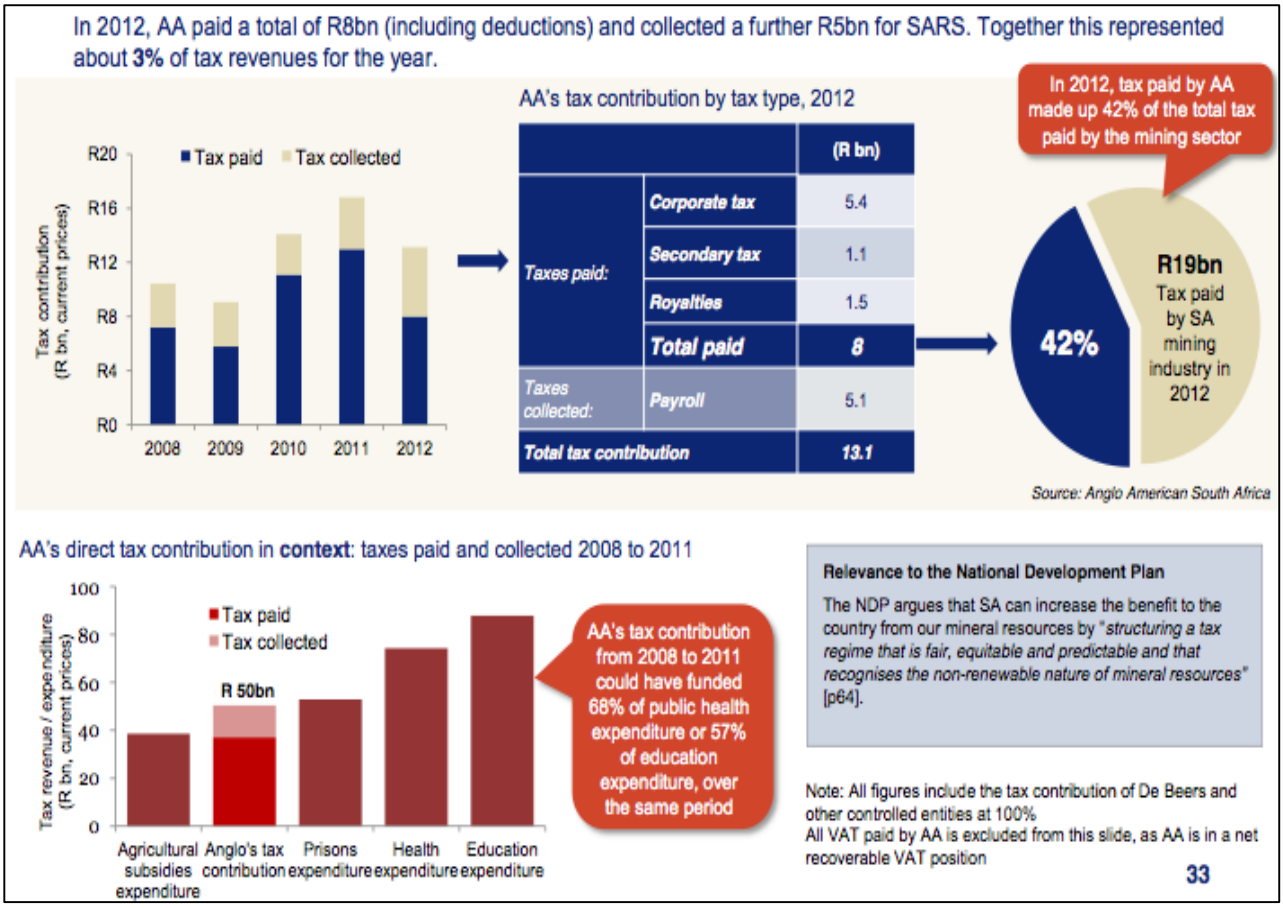


Figure 14: Tax revenues paid by AA (Genesis Analytics and PwC, 2013)

3.1.2 Summary

Anglo American remains an important player in the mining industry and the SA economy. Due its size, commodity mix, and significance in the mining industry, Anglo American can be used as a proxy for the industry. Section 3.3 provides a summary of the empowerment transactions completed by the company's various business units.

3.2 Anglo American's BEE Transactions

Anglo American in SA implemented a range of empowerment transactions in its various business units, in order to meet MPRDA and Mining Charter requirements. The group completed empowerment deals in KIO, Anglo American Platinum (AAP), Anglo American Thermal Coal (AATC) and De Beers, its diamond division (Anglo American Corporate Finance , 2013).

Typically, SA empowerment transactions were structured to lock in HDSA shareholders until 2014, to ensure that the 26% HDSA ownership in that year, as prescribed by the MPRDA and Mining Charter, was complied with. Anglo American adopted a hybrid methodology (e.g. measuring both equity and units of production transferred to HDSAs) (Anglo American Corporate Finance , 2013).

3.3 AAP – Atlatsa / Bokoni

3.3.1 Structure Overview

AAP, one of the biggest business units in the group, completed a number of empowerment deals with HDSA entrepreneurs, host communities and employees. One of the deals involved the Bokoni platinum mine in the Limpopo province (Anglo American Corporate Finance , 2013).

Figure 15 below depicts the structure of the deal. AAP disposed of 51% of Bokoni Platinum Mines (previously Lebowa Platinum Mines) to Atlatsa (a BEE company). AAP transferred its 100% interest in Bokoni Platinum Mines to a new wholly-owned subsidiary, Bokoni Platinum Holdings (previously Lebowa Holdco). Atlatsa (via Plateau) acquired a 51% share in Bokoni Platinum Holdings from AAP, with the remaining 49% being held by AAP. Bokoni Platinum Holdings owns 100% of Bokoni Platinum Mines and 100% of the projects Ga-Phasha, Boikgantsho and Kwanda. The financing structure is presented in Appendix 2 (Anglo American Corporate Finance , 2013).

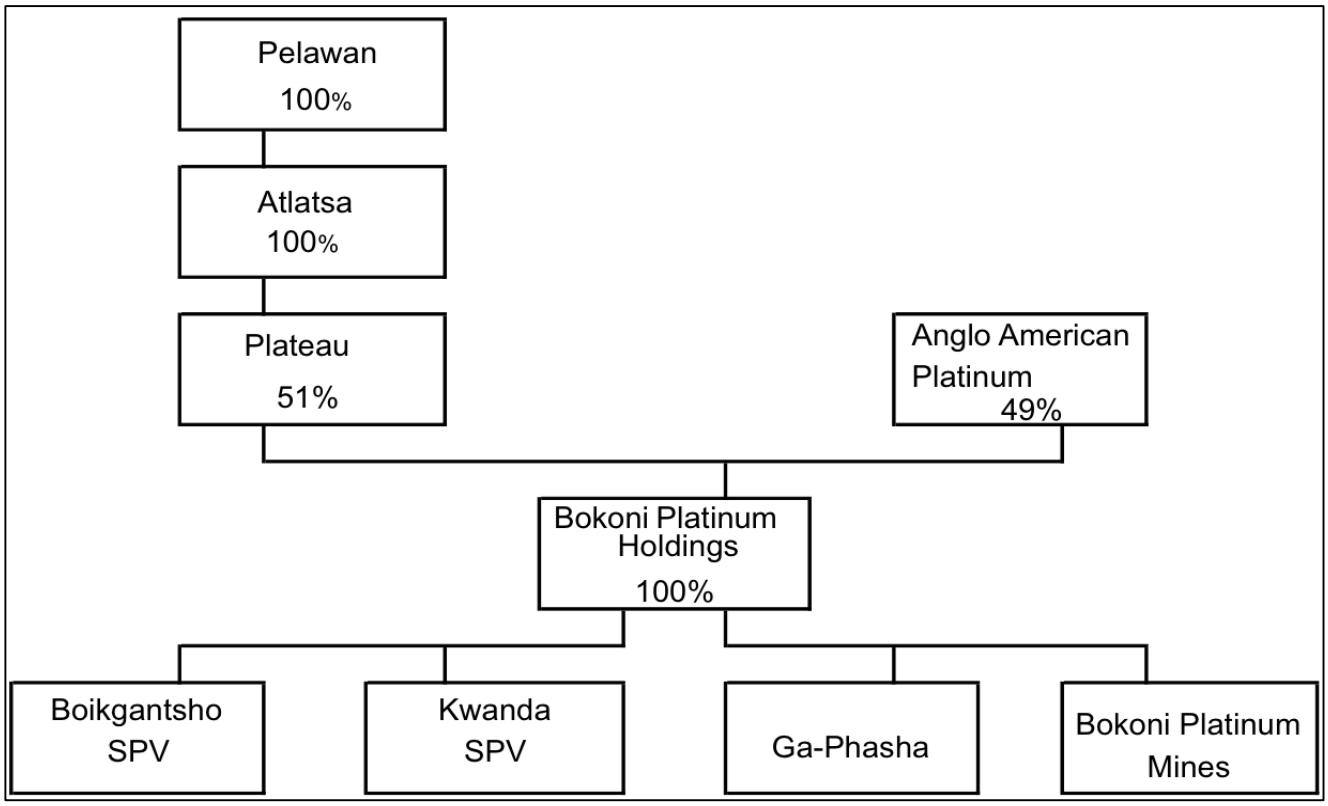


Figure 15: AAP BEE deal structure

3.3.2 Anglo American Platinum Community Empowerment

AAP completed an empowerment deal with host communities in Rustenburg, Amandelbult, Mogalakwena and Twickenham operations, as well as AAP's labour-sending areas (LSAs). The structure includes an umbrella trust called the Lefa La Rona Trust (LLRT), acting as a conduit and bank to the underlying development trusts (DT) in each of the four operational areas. The trust also acts as a non-profit company for the labour-sending areas (LSA NPC) (Anglo American Corporate Finance , 2013).

The LLRT was set up in November 2011 at the time when the AAP share price was R556/share. JSE and shareholder approval was obtained; and on 15 December 2011; 6, 290, 365 (2.33% of AAP market capitalisation) of AAP shares were issued to LLRT. (All the other AAP joint ventures (JV's) are outlined in Appendix 3) (Anglo American Corporate Finance , 2013).

The transaction involved AAP issuing new shares worth R3.5 billion to a trust for the benefit of the communities. AAP provided Notional Vendor Financing (NVF) for the whole transaction; hence no cash was required from AAP (except for an up-front donation of R629, 037 to the LLRT to subscribe for the shares). The NVF structure is in place for 10 years, after which a sufficient quantity of shares will be sold to repay the NVF; and the LLRT will retain the remainder.

A total of 60% of the ordinary AAP dividends on the shares were held back and used towards the repayment of the NVF. The remaining dividends (40%) were paid to the LLRT, which, in turn, distributed the funds to the DTs and LSA NPC according to the determined allocation splits (Anglo American Corporate Finance , 2013).

3.4 AATC

AATC, one of the smaller business units in the division, conducted an empowerment deal with HDSA partners. AATC is not a listed entity, compared to the other business units in the group; and it is wholly owned by Anglo American.

3.4.1 Structure overview

Anglo Inyosi Coal (AIC) is a venture entered into between Anglo South Africa Capital (ASAC) (representing AATC) and Inyosi (Pty) Ltd, as displayed in Figure 16. AIC's share capital is 73% owned by ASAC and 27% owned by Inyosi (Pty) Ltd. Inyosi (Pty) Ltd is 33% owned by Pamodzi Coal (Pty) Ltd; and 33% owned by Ndonsa Mining (Pty) Ltd (named Lithemba Consortium); 19% owned by WDB Investment Holdings (Pty) Ltd; and 15% owned by a Community Trust (Anglo American Corporate Finance , 2013).

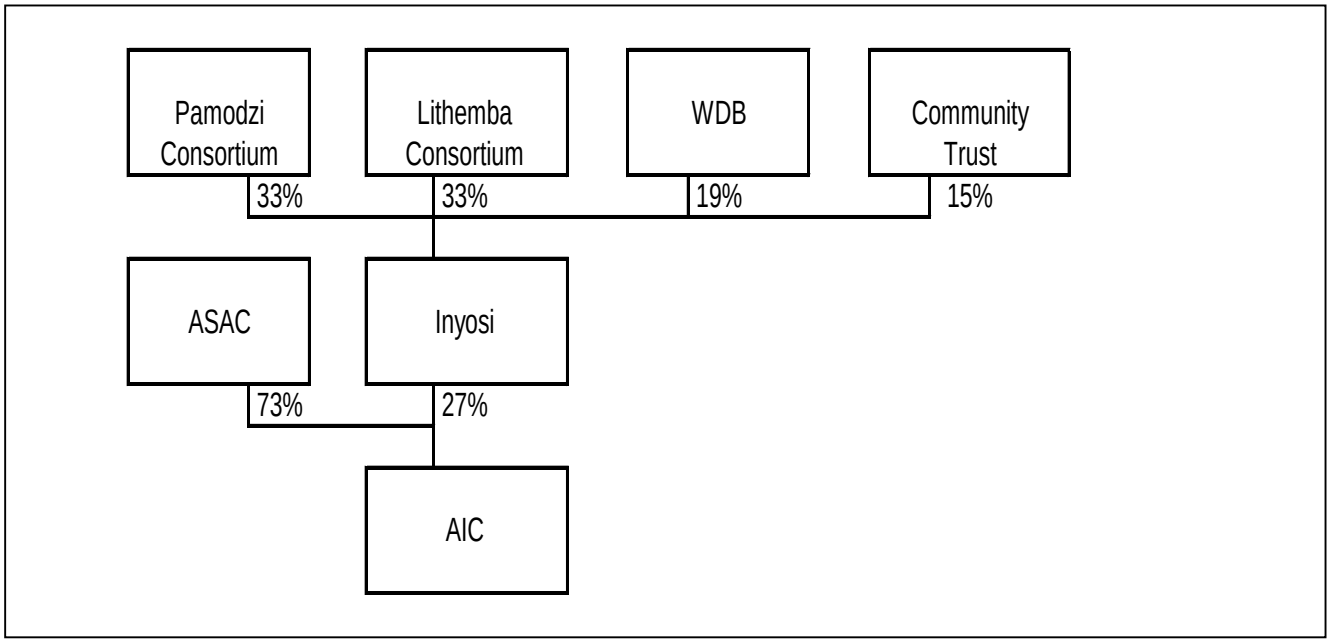


Figure 16: Anglo Inyosi Coal structure (Anglo American Corporate Finance , 2013)

AIC purchased assets from Anglo Operations Proprietary Limited (Anglo Coal division). The capital structure of the deal is described in Appendix 4.

3.5 De Beers

3.5.1 Structure overview

Figure 17 illustrates the De Beers empowerment structure. Several empowerment partners were co-opted into the consolidated holding company. Ponahalo purchased a 26% holding in De Beers Consolidated Mines (DBCM). The remaining 74% is owned by De Beers South Africa (DBSA).

The purchase price of R3.7 billion was funded with preference shares issued to Standard Bank, with maturity dates between 2009 and 2013. Of this amount, DBSA guaranteed R800 million. DBCM was funded with senior debt from the Royal Bank of Scotland (RBS); and it had a facility of R1.8 billion with Standard Bank. The equity contribution for the BEE shareholders was R10 million (Anglo American Corporate Finance , 2013). Appendix 5 illustrates the financing structure.

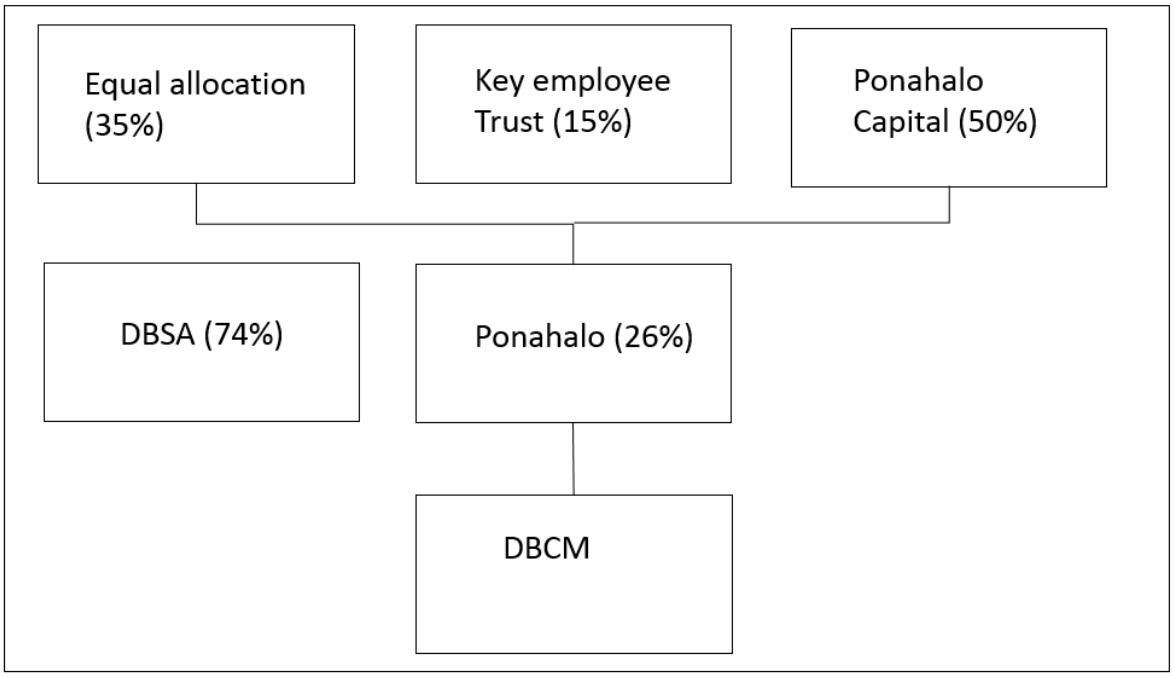


Figure 17: De Beers' structure (Anglo American Corporate Finance , 2013)

3.6 DTC SA Empowerment

As part of the 2008 diamond dealers' licence application, De Beers committed to empowering the Diamond Trading Company of South Africa (DTC SA) prior to the expiry of the licence in August 2013. It was envisaged that DBCM (26% BEE empowered) would acquire DTC SA from De Beers Group Services (DBGS), which is 100% held by DBSA. However, owing to the economic downturn in 2008/2009 and the subsequent strain on the DBCM balance sheet, DBCM has not been in a position to purchase DTC SA at a fair value. The group structure prior to the proposed transaction is illustrated in Figure 18 (Anglo American Corporate Finance , 2013)

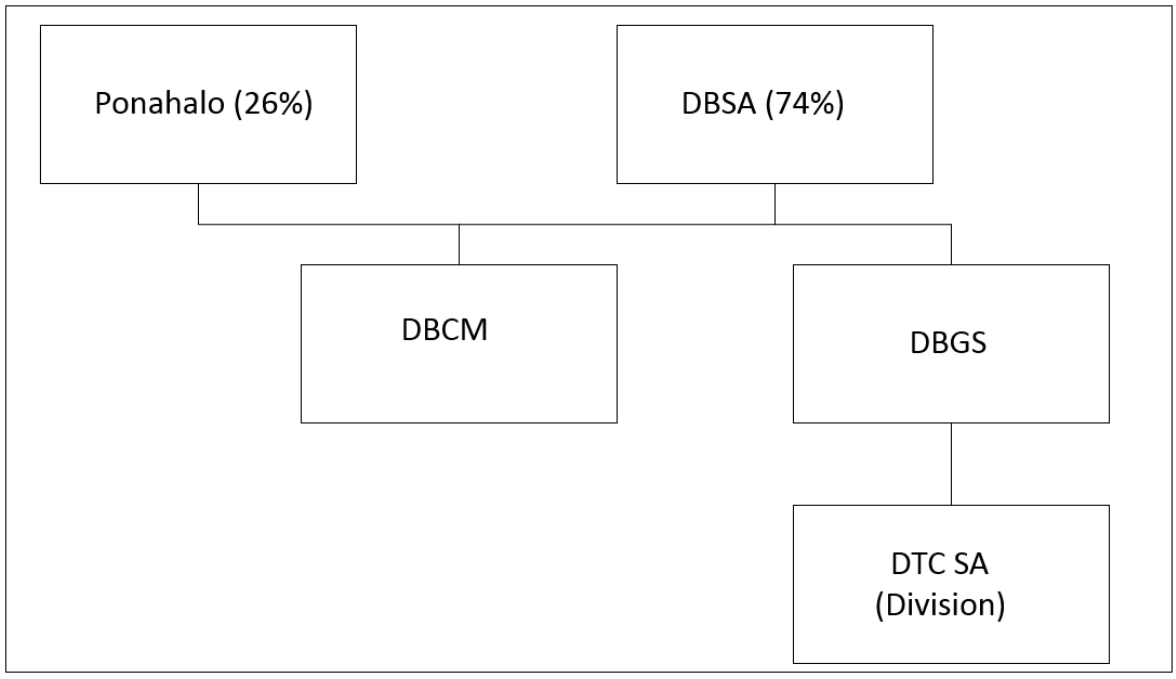


Figure 18: DTC structure (Anglo American Corporate Finance , 2013)

3.7 Employee Share-Ownership Plans (ESOPs)

All Anglo American business units in SA have ESOPs. The ESOPs for the different business units are outlined in Table 9 below. At inception, KIO's scheme was R8.7 billion, whilst the net equity value in 2012 was R5.2 billion (Anglo American Corporate Finance , 2013).

KIO's ESOP has outperformed all other business units in Anglo American. Disappointingly, both Anglo American South Africa and Anglo American Platinum's schemes have not performed well; and they have delivered less than satisfactory value for employees (Anglo American Corporate Finance , 2013).

Table 9: AA business unit ESOPs (Anglo American Corporate Finance , 2013)

Entity	ESOP	Number of employees	Scheme value at inception	Net equity value Dec 2012	Meaningful value
AAP	Kotula	46, 000	R1.5 billion	R0.5 billion	R7.5 billion
KIO	Envision	6, 000	R8.7 billion	R5.2 billion	R1.8 billion
Anglo American SA (AASA)	Siyaphambili	10, 000	R0.2 billion	R0.2 billion	R5.2 billion

3.8 Summary

Anglo American has concluded a number of empowerment deals through its various subsidiaries. It has done this by adopting diverse financing models and holding structures tailored for the unique needs of each company. Most of the significant empowerment deals have involved HDSA partners. Chapter 4 will provide a general assessment of these ESOPs and their performance. A framework of what a successful ESOP looks like will be developed, and these ESOPs assessed against that framework.

4. Anglo American's assessments of current ESOPs

4.1 Performance assessment

Anglo American conducted a study on the performance of current ESOPs employed in the different business units. These include:

- AAP: Kotula;
- KIO: Envision;
- AASA (AATC, Corporate Centre, Global Shared Services (GSS), Vergelegen): Syaphambili; and
- DBCM: Ponahalo (Anglo American South Africa, 2013).

According to the company, as they are currently structured, the ESOPs across the business units are not consistent in terms of both design and generated returns. In terms of the financial structure, the main categories include:

- Free shares (AASA, part of Kotula);
- Notionally vendor-funded shares (part of Kotula, Envision, Ponahalo); and
- Different vesting periods (3-5 years) (Anglo American South Africa, 2013).

After analysing the performance of the ESOP, the company found that the majority of ESOPs have not performed satisfactorily, in financial terms, with the exception of Envision.

- Kotula's benefits have been limited to minimal dividends and a small value that vested in relation to the free shares;
- Envision has delivered beyond expectation;
- The AASA scheme's benefits have been relatively modest; and
- The DBCM scheme has not yielded any anticipated benefits for employees (Anglo American South Africa, 2013).

According to Anglo American, the performance of the ESOPs have been driven mostly by the commodity cycles, where Envision benefited from the iron ore up-cycle; but Kotula and AASA suffered from general weakness in AAP's and Anglo American plc's share prices, respectively.

Due to the varying architectures and the various financial performances of the ESOPs in the group, Anglo American cannot show that its employees have meaningful and consistent long-term share-ownership in the company, because employees sell their shares, after vesting. This is accredited to the need for short-term financial needs, as opposed to long-term investment opportunities. Consequently, the employees do not experience any transparent long-term participation in the organisation (Anglo American South Africa, 2013).

4.2 Original objectives of the schemes

According to their findings, Anglo American believes some of the original objectives of the current ESOPs, such as wealth creation for employees, have not been met. This, in large part, is due to modest pay-outs for employees and the sale of shares by employees upon vesting, even in the case of high-performing schemes, such as Envision. The alignment of company performance with the individual performance of employees has not materialised.

The ESOPs do not, in all cases, meet the employees' needs. The day-to-day reality of employees' lives puts a stronger emphasis on the availability of cash than on active participation as a shareholder. The current notional vendor-funded structures are highly dependent on share price performance; whereas non-management employees have a far greater need for low-risk consistent cash income (Anglo American South Africa, 2013).

4.3 Summary

Anglo American has conducted a number of ESOPs in its various business units. The financial performance of the ESOPs has been inconsistent. Employees have not fully benefitted from current ESOPs, with structures that are complicated and opaque to employees. Chapter 5 seeks to propose a framework that encapsulates varying success factors of an ESOP, which can be used by mining companies when structuring new ESOPs or amending existing plans.

5 ESTABLISHING A FRAMEWORK FOR A SUCCESSFUL ESOP

5.1 Principles underpinning the proposed framework

The new proposed ESOP model has to take into account all that has been discussed with regard to the failures of current ESOP models in the industry, whilst providing mechanisms to alleviate these drawbacks. This is to ensure that ESOPs are instruments used by mining companies to foster all the virtues of an effective ESOP.

It is envisaged any ESOP formulated under the framework should apply to employees of that organisation so long as they remain employees. Once an employee leaves the organization, the provisions of the ESOP would be forfeited and gained by the employee who replaces the departing employee. This is a critical principle of the proposed ESOP framework as this would ensure that companies continue to comply with regulation and that their employees continue to benefit from the ESOP.

Similarly, employees that get promoted and fall within a higher bracket forfeit their benefits in the scheme. Any new employees that falls within the bracket becomes an automatic participant in the scheme. Beneficiaries of these ESOPs should be HDSAs that fall within the lower salary bands in the organisation. If there is a reduction in employee numbers, the benefits of that ESOP should be redistributed to the remaining employees. This is to avoid constant dilution of employee shareholding to external partners when employees leave the company.

The shares issued to employees must be placed in a holding structure, which is managed by representatives elected by the employees. Each representative union would have a nomination, based on the percentage share of those employees it represents in the category of workers that qualify. The trust must have full voting rights, preferable with a seat on the board of directors of the company through the trust.

The payment of annual dividends must also be balanced with the need to finance the sale of shares to employees. It is proposed that the vesting period of the shares be extended to allow for a more consistent and notable dividend flow to the employees. It is important to note that once the debt has been settled, employees would be entitled to 100% of the dividend flow.

Once vested, employees are allowed to sell their shares to qualifying employees within the organization. These are HDSA participants that fall within the specified salary bracket. There should be an obligation placed on the trust to maintain a certain amount of capital to ensure rights offers are followed through. This is to mitigate the risk of diluting shares and also to ensure continued empowerment.

To ensure that during times when companies are performing satisfactorily, due to rising commodity prices, or improved productivity gains, a sliding scale should be used, when determining what percentage should flow to the employees. During high commodity cycles dividends should be skewed towards debt repayment. During low cycle periods dividends paid should be skewed towards cash payments for employees.

The report does not propose separate dividend policies for employees and other ordinary shareholders. It is incumbent on the trust, upon receiving dividends from the company to institute this sliding scale.

It is not enough for companies to institute an ESOP without engaging employees on the meaning of the ESOP, and providing employees with financial literacy programs. These must be geared towards sensitising employees to the financial aspects of the business as new owners. This, with a view of aligning company interests with individual employee interests.

These aspects are equally important; and they need to be applied in concert, accompanied by constant engagement with the employees and the provision of an environment conducive to individual employee enterprise.

5.2 Proposed Framework

A successful ESOP must be buttressed by a set of key fundamental pillars if it is to meet the collective needs of critical stakeholders. In terms of an ESOP, these critical stakeholders include employers, employees and the government. This section will outline a proposed framework for companies to utilise when instituting a new ESOP or reviewing their old ESOPs. This framework as aforementioned will be underpinned by the set of principles outlined in section 5.1.

5.2.1 Meaningful economic participation

The first most important pillar is the equity stake in the company. If companies want to employ ESOPs successfully, they need to ensure that they afford a meaningful equity value toward the ESOP. The percentage depends on the dynamics of the business. In terms of the Mining Charter, the requirements are 26% HDSA participation.

Khan (2014) studied the effect of ESOPs on company profitability in the South African mining industry. The study was conducted on JSE listed companies. The study found that ESOP percentages for these companies ranged from 1.4%-3% of the total shares for of the company. His study also found that only 8 out of the 30 company's listed had ESOPs in place (Khan, 2014).

Short and Keasey (1999) contended that the effect of ESOP is not only dependent on the existence thereof, but highly dependent on the level of ownership. Their study depicted a positive relationship between ownership and performance at various percentages. In Anglo American the highest equity stake from broad based ESOPs is 3% from Envision.

5.2.2 Instilling an ownership culture

The second critical pillar to the framework is the ability of a company to instil an ownership culture within the business. Employees must have the ability and opportunity to contribute to decision making processes, accompanied by implementation of those business decisions. This must be enabled by mechanisms that allow for efficient dissemination of information and channels that enable employee participation in identifying process failures and improvement opportunities. These contributions should be heard, and timeously acted upon.

5.2.3 Driving the business disciplines

For successful ESOPs companies must ensure that employees are concerned with driving the business disciplines. These employees must understand how their individual performance contributes to overall performance improvement. An enabling environment where these employees identify critical performance metrics, are clear about the performance objectives and targets whilst continuously monitoring and tracking those metrics is needs to be created. Ideas about performance improvement must be shared between lower level employees and management.

5.2.4 Share price performance

A prerequisite for any successful ESOP is an improving share price. This is critical to the success of an ESOP in large part due to the fact that the repayment for the equity afforded by the company depends on dividend flow. Increasing share normally is indicative of improved company performance, and results in improved dividend payment which results in shorter vesting periods.

5.2.5 Financial incentives

Under the proposed framework, short term and long term financial incentives are critical to the success of the ESOP. The implementation of the ESOP must ensure that employees recalculate their economic interests. Meeting the short term needs of employees and protecting employee incentives from commodity cycles is an important feature of the ESOP under this new framework.

5.2.6 Aligned goals

Employers and employees must have aligned goals and objectives under the proposed framework. These objectives and goals centre on business sustainability, operational and financial performance. Other considerations include meeting stakeholder requirements and ensuring business risk is mitigated.

5.2.7 Productivity gains

Improved productivity is a measure of business efficiency. Application of an ESOP should ensure improved productivity from the workforce as this will indicate a positive collaborative relationship between management and lower level employees and an indication of employee sentiment.

5.2.8 Engaged and responsive workforce

A successful ESOP must result in an engaged and responsive workforce. Employees must be responsive to the needs of the organisation in a dynamic business environment. This has to be supported by effective employee involvement mechanisms. Strikes and lock-outs are not features of an engaged and responsive workforce.

5.2.9 Regulatory compliance

One of the more important pillars supporting an effective ESOP is the compliance with regulatory requirements. In terms of SA, mining companies must comply with requirements of the Charter.

5.3 Summary

Chapter 5 summarises a proposed framework that should utilised by employers when constituting an ESOP. The ESOP is underpinned by the set of principles specified. The framework comprises key pillars that should be considered when implementing an ESOP, with underlying programmes underpinning these key pillars. The framework is summarised in figure 19 below. ESOPs in Anglo American will be tested against this framework and their success assessed according to the framework.



Figure 19: Proposed ESOP framework

6 ANALYSIS OF CURRENT ESOPS USING PROPOSED FRAMEWORK

Anglo American has two listed companies in its stable, namely, AAP and KIO. This report provides an analysis of the performance of the ESOPs, as well as some of the key drivers behind this performance. The ESOPs will be evaluated using this new proposed framework laid out in Chapter 5.

6.1 KIO

Kumba Resources (now KIO), was unbundled in 2006, resulting in KIO owning 74% of the Sishen Iron Ore Company (SIOC). Exxaro Resources took up 20%; SIOC development SPV (Pty) Limited (3%); and employees through the ESOP, named Envision, owning the remaining (3%). The combined minority shareholding accounts for the 26% demanded by the Charter. The shares were meant to vest in years five, six and seven from the subscription date (Kumba Iron Ore Limited, 2006-2015).

6.1.1 Share performance and financial incentives

Table 10 below contains the parameters used for the analysis, with figures obtained from KIO's annual integrated financial report, from 2006-2014.

Table 10: KIO's annual financial results (Kumba Iron Ore Limited, 2006-2015)

Year	Total dividend (R million)	Earnings per share (R/share)	Dividend per share (R/share)	Dividend cashflows (R million)
2006	12	0.84	0.8	7
2007	98	9.85	7.5	11
2008	271	22.8	21	32.00
2009	189	21.88	14.6	59.00
2010	419	44.67	34.5	62.00
2011	587	53.11	44.2	127.00
2012	426	37.97	31.7	120.00
2013	144	48.08	40.04	83.00
2014	478	34.32	23.34	169.00

Figure 20 depicts KIO's share price performance from its initial listing in 2006 to 2014. The graph shows how the company experienced tremendous share price growth from listing until 2012; but this was followed by a precipitous fall in sub sequent years.

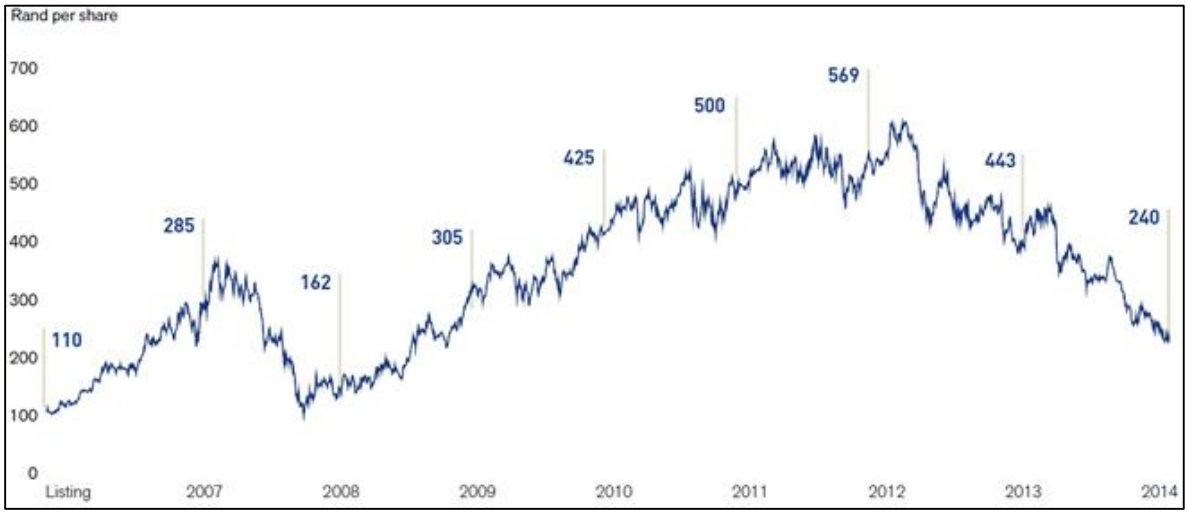


Figure 20: KIO's share price (Kumba Iron Ore Limited, 2015)

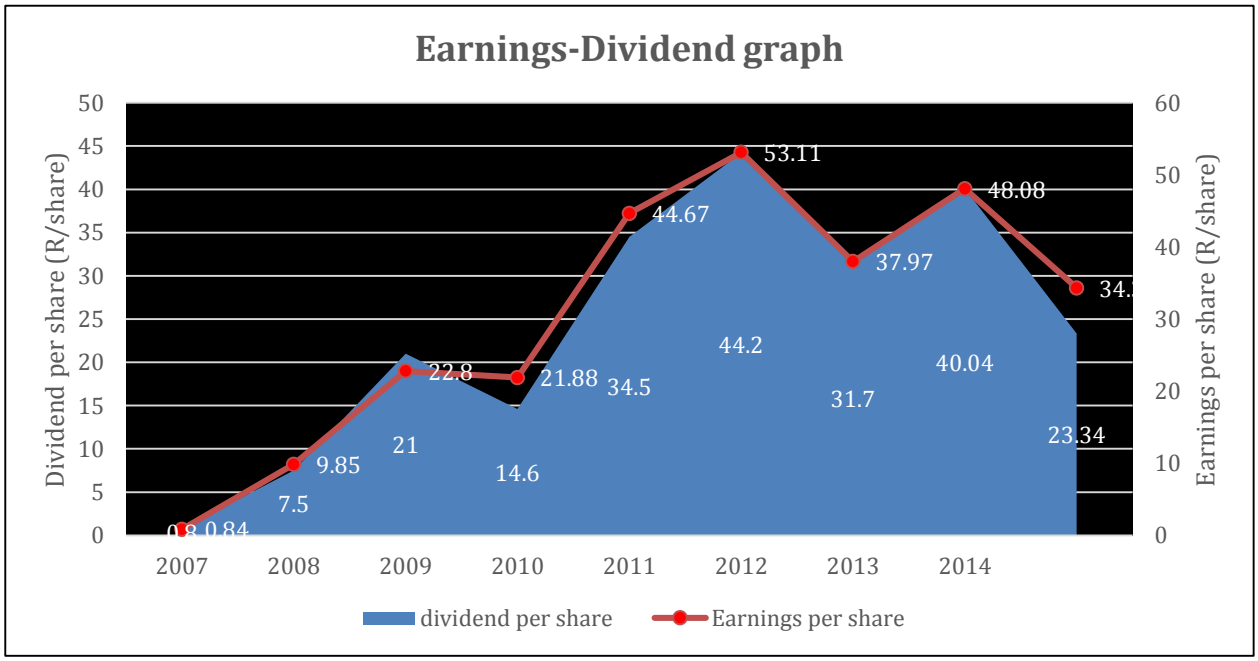


Figure 21: KIO's earnings-dividend

There is a direct relationship between a company's share price, earnings per share, and dividends per share. Higher earnings are accompanied by a higher share price and increased dividends.

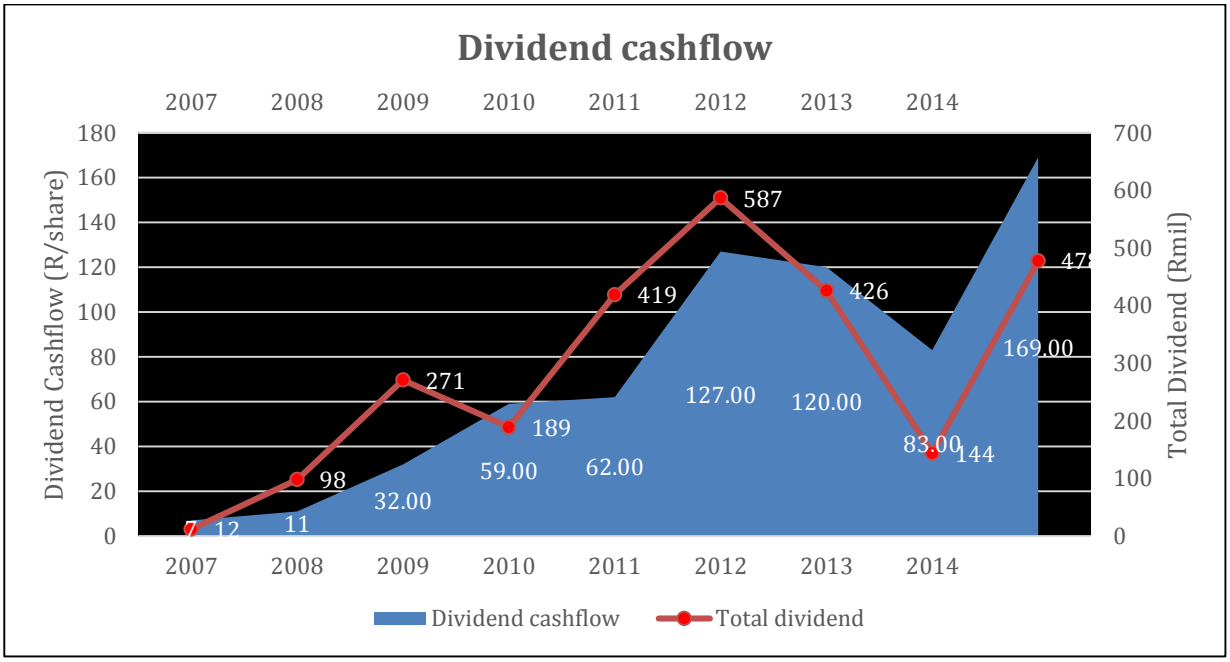


Figure 22: KIO's dividend flow graph

Figure 22 illustrates the difference between the total dividends paid out to the shareholders, and the final dividend paid out to the employees. On average, the total dividend is more than 3 times the dividend cash flow. The difference between the two dividend payments is used to finance the cost of the debt; and it is also used for trust fees and the associated costs.

The performance of Envision was driven mostly by the commodity cycles benefiting from the iron ore up-cycle. Envision's financial performance has been good, with shareholders benefiting from high dividend pay-outs.

6.1.2 Meaningful economic participation

Envision owns a total of 3% of the companies share allocation without any voting rights pre-vesting of the shares.

6.1.3 Instilling ownership culture and aligning goals

In October 2012, KIO employees engaged in unlawful industrial action that resulted in significant losses, in both physical assets and also lost production output. In their 2012 annual report, KIO stated that, *"labour relations issues proved to be the biggest challenge, despite the unprecedented financial payouts to employees at the end of 2011"* (Kumba Iron Ore Limited, 2012).

6.1.4 Productivity

An analysis of KIO's productivity was conducted post the implementation of Envision. Figures were obtained by comparing the production output (million tons) by total permanent employee numbers with data from KIO's annual reports from 2007 to 2015. Figure 23 below displays the results obtained from.

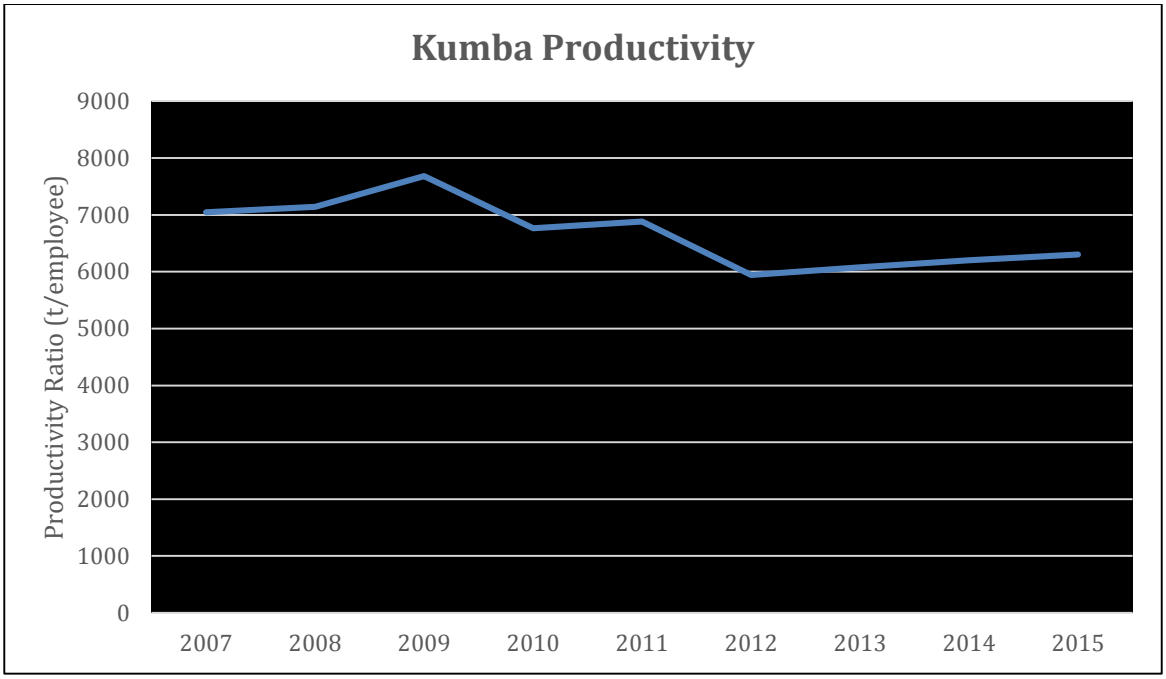


Figure 23: KIO's productivity

KIO has increased its production over the years, however, employee numbers have significantly increased. The increase in employee numbers outpaced the increase in production output, as a result overall employee productivity has reduced. In their 2012 annual report, KIO highlighted absenteeism having a significant impact on productivity.

6.1.5 Engaged and responsive workforce

Labour relations has constantly been a risk highlighted by the company during the past years. According to the 2015 annual report, labour relations formed part of the top 10 risks. This the company asserts is as a result of the restructuring proposed by the company necessitated by declining commodity prices. According to KIO, the risk is also caused by zero dividend pay-outs expected in 2016 due to lower commodity prices (Kumba Iron Ore Limited, 2015).

According to Lucas Phiri, National Union of Mine Workers (NUM) Chief Negotiator at KIO, mining companies do not have the best interest of employees at heart. He said, *"the government must consider taking back mining licences of these mines who their objective is to exploit workers, maximize profit and when they are done they move away from their social responsibilities and leave some workers in bad conditions, injured or sick."* This follows the announcement of the plans by the company to retrench 2633 employees (NUM, 2016).

6.1.6 Regulatory compliance

In their 2015 annual report, KIO highlighted the Department of Mineral Resources' interpretation of the Mining Charter as a significant challenge. Post the implementation of ESOP, the company had complied with all elements of the mining charter. However there still remains uncertainty around the issue of *"once empowered, always empowered"* (Kumba Iron Ore Limited, 2015).

6.1.7 Summary

Figure 24 below contains a dashboard summary of the components discussed above.

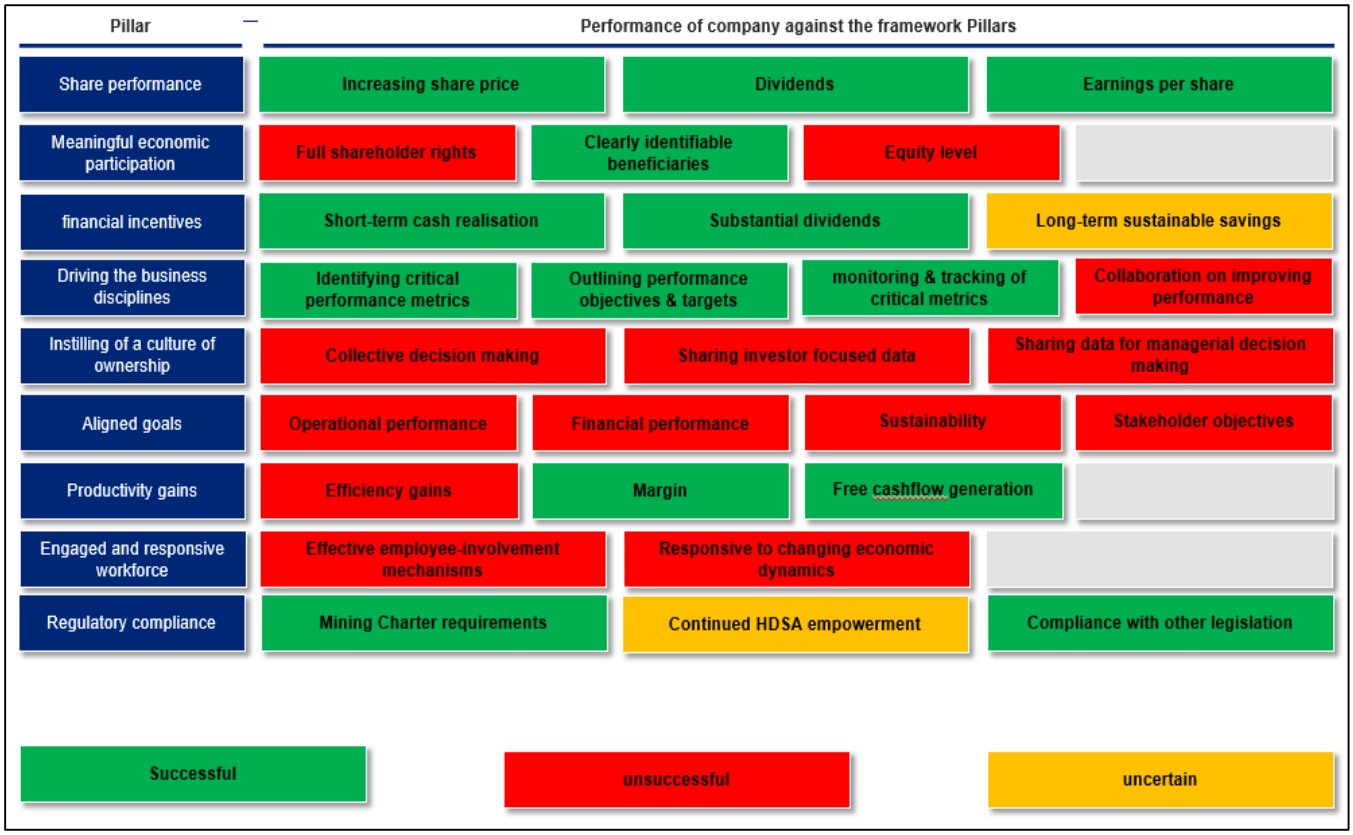


Figure 24: Summary of KIO's performance evaluated against proposed framework

6.2 Anglo American Platinum

In 2008, AAP reached an agreement with its employees and the labour unions on the terms and structure of the companies' ESOP. The AAP Kotula Trust would facilitate the scheme on behalf of the beneficiaries, to a total of 2.5 million shares. These were issued to the trust, equating to approximately 1% of the company's ordinary share capital. When the shares were issued, 90% of the beneficiaries would be HDSAs. The ESOP had a value of R1.5 billion at inception, with a total of 46, 000 beneficiaries (Anglo American Platinum Limited, 2009).

To achieve the 26% ownership target, AAP opted to utilise various mechanisms, such as a community trust, joint ventures, disposal of the assets, and establishing the company's ESOP in order to achieve this milestone.

6.2.1 Share performance and financial incentives

An analysis was conducted, comparing what the dividend flow to individual employees would have been, had the company opted to use only the ESOP as the empowerment vehicle. This was compared to the actual dividend payment that each employee received after the establishment of the program. Table 11 below contains the parameters used for the analysis; and these were obtained from AAP's annual integrated financial report, from 2008-2014.

Table 11: AAP annual financial result (Anglo American Platinum Limited, 2008-2014)

Year	Employee numbers	Dividend/share (c/share)	Shares in issue (million)	Dividend paid (R)	Shares @ 26% (million)	Dividend @ 26% ownership (R)
2008	50152	3500	237.1	704.16	18.53	12205.5
2009	58320	0	236.8	0	18.53	0
2010	54022	683	261.6	135.15	18.53	2342.66
2011	58541	700	261.1	127.82	18.53	2215.63
2012	56379	0	261	0	18.53	0
2013	49816	0	261	0	12.35	0
2014	49763	0	261.2	0	6.18	0

It is important to note that the shares were structured to vest in the fifth, sixth and seventh year from the subscription date. In 2012, some of the shares had vested; and as such, some of the employees were entitled to the capital value of each Kotula share allocated to them. From the dividend paid, provisions had to be made for trust fees and other associated liabilities (Anglo American Platinum Limited, 2009).

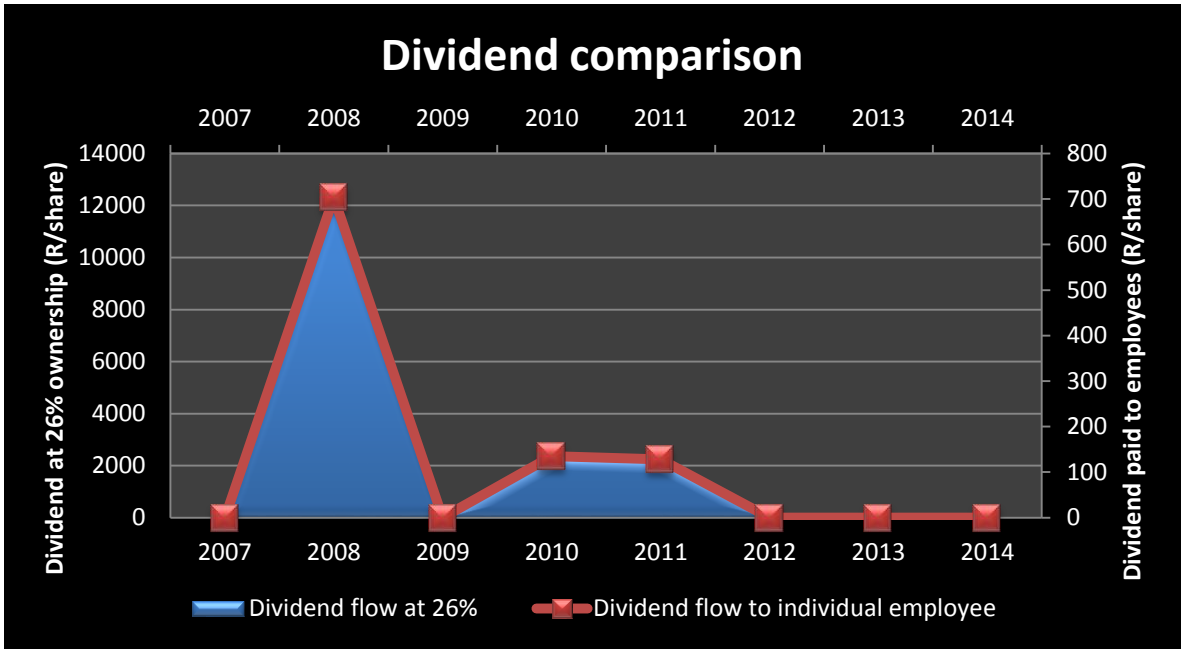


Figure 25: Anglo American Platinum dividend comparison

In 2008, AAP paid a dividend of 3, 500 cents per ordinary share (c/share), as illustrated in Figure 25. The Kotula trust had 1, 069 million shares, which meant that the total ordinary dividend paid to the trust amounted to R53.3 million. This equates to R704.16 per employee for each share that they owned.

AAP did not pay a dividend in 2009, with dividends of 683 c/share and 700 c/share paid in 2010 and 2011, respectively. This resulted in a dividend per employee amount of R135.15 in 2010 and R127.82 in 2011. From 2012-2014, the company did not pay any dividend.

Had the ownership percentage increased to 26%, instead of the 1% at inception, the dividend flow to the employees would have significantly increased. In 2008, this would have resulted in a total dividend of R648.55m paid to the trust, resulting in R12, 205.50 per employee for every share they owned; and this is significantly higher than the R704.16 received in 2008.

Similarly, the subsequent 2010 and 2011 pay-outs would have been R2, 342.66 and R2, 215.63, respectively. Increasing the equity stake of employees to 26% is not always pragmatic due the responsibilities mining companies have toward communities and other stakeholders. However it does demonstrate the impact of improved equity participation by ESOPs on individual employees.

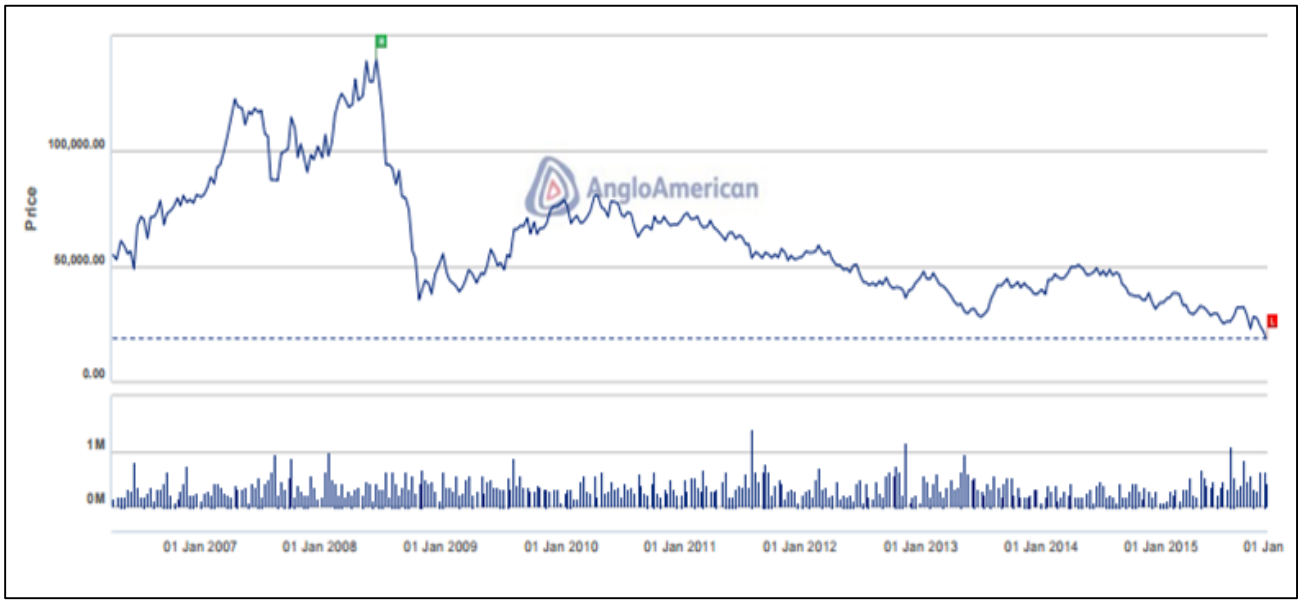


Figure 26: Anglo American Platinum share price (Anglo American Platinum Limited, 2015)

AAP's share price chart has a similar trend to the divided flow chart. The chart reflects the performance of the company. The chart reached a peak above R1, 400 in 2008; and it fell to a price below R200 in 2015. This coincides with the highest dividend paid by the company in 2008. There is also a direct relationship between the earnings per share of the company and the dividend flow, as displayed in Figure 27.

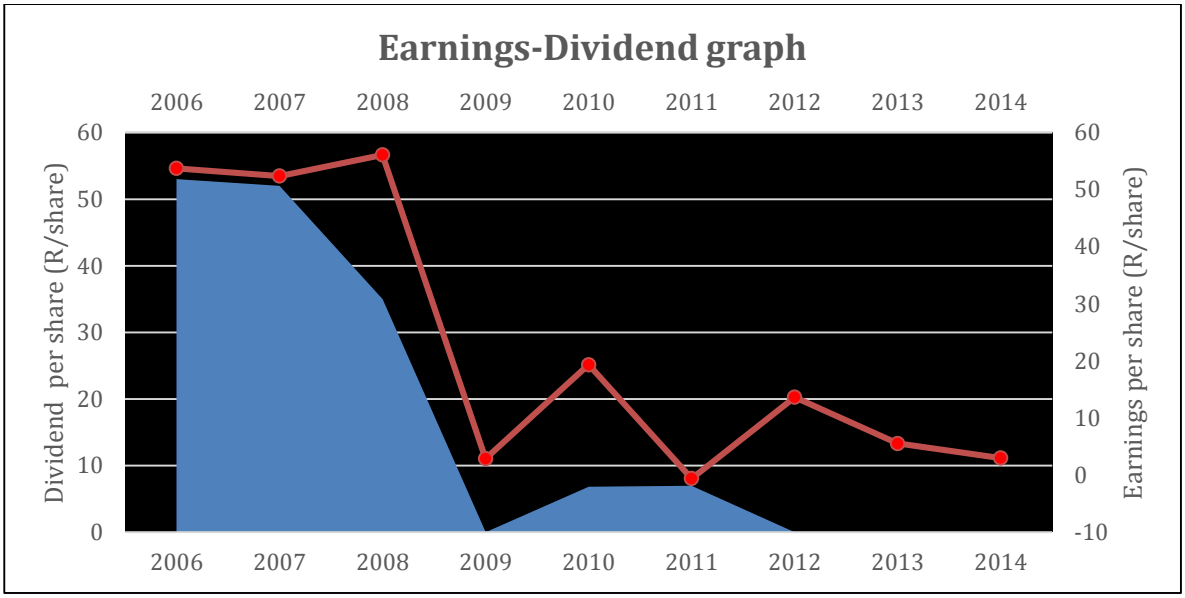


Figure 27: AAP earnings – dividend chart

AAP's ESOP has not paid significant dividends to employees. This was in large part due to the poor financial performance of the company resulting in low dividend payments.

6.2.2 Instilling an ownership culture and aligning goals with an engaged and responsive workforce

Following the tragic events at Marikana in 2012, where an industrial dispute turned violent, resulting in the death of 34 mine workers, followed by a 5 month strike in the platinum belt, the industrial action resulted in significant losses for the company. After reaching an agreement, the company continued to report non-procedural incidents such as underground sit-ins and illegal stoppages in 2013 (Anglo American Platinum Limited, 2014).

Delivering his Chairman's report for the 2014 reporting period, the Chairman of AAP, Valli Moosa, pointed to a need for a renewed emphasis on labour relations. Key amongst the important requirements is a labour force that has a meaningful stake in the business, and a subsequent responsibility in the fortunes of the company, according to the Chairman. This requires more serious engagement with the

employees and increased ownership in the business. This is interpreted as an implicit recognition of the ineffectiveness of the current ESOP.

6.2.3 Meaningful economic participation

Kotula owned 1% of the company's ordinary share capital. When the shares were issued, 90% of the beneficiaries would be HDSAs. Final vesting for Kotula shares was in 2014 with the ESOP subsequently wound up. AAP indicated its intention to consider the implementation of a new ESOP (Anglo American Platinum Limited, 2009).

6.2.4 Productivity

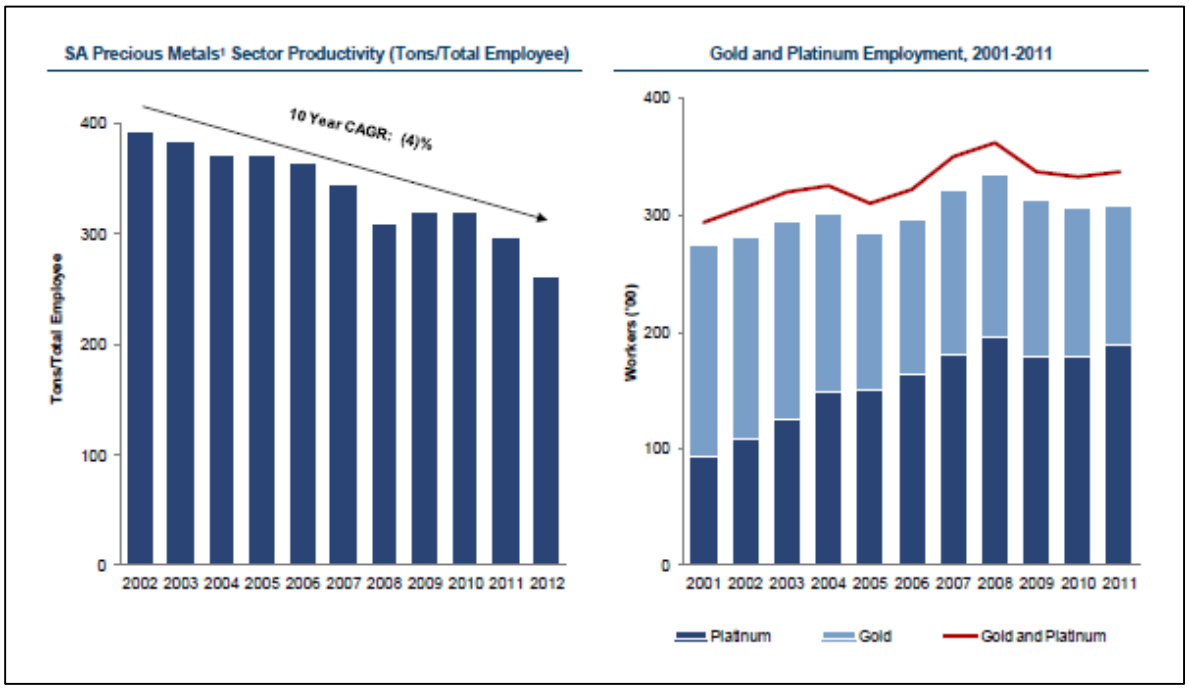


Figure 28: Precious Metals Sector Productivity (Goldman Sachs, 2012).

Wage inflation has increased by 11% whilst productivity levels in the gold and platinum sectors have declined by 4% per annum over a 10-year period as depicted in figure 28 above.

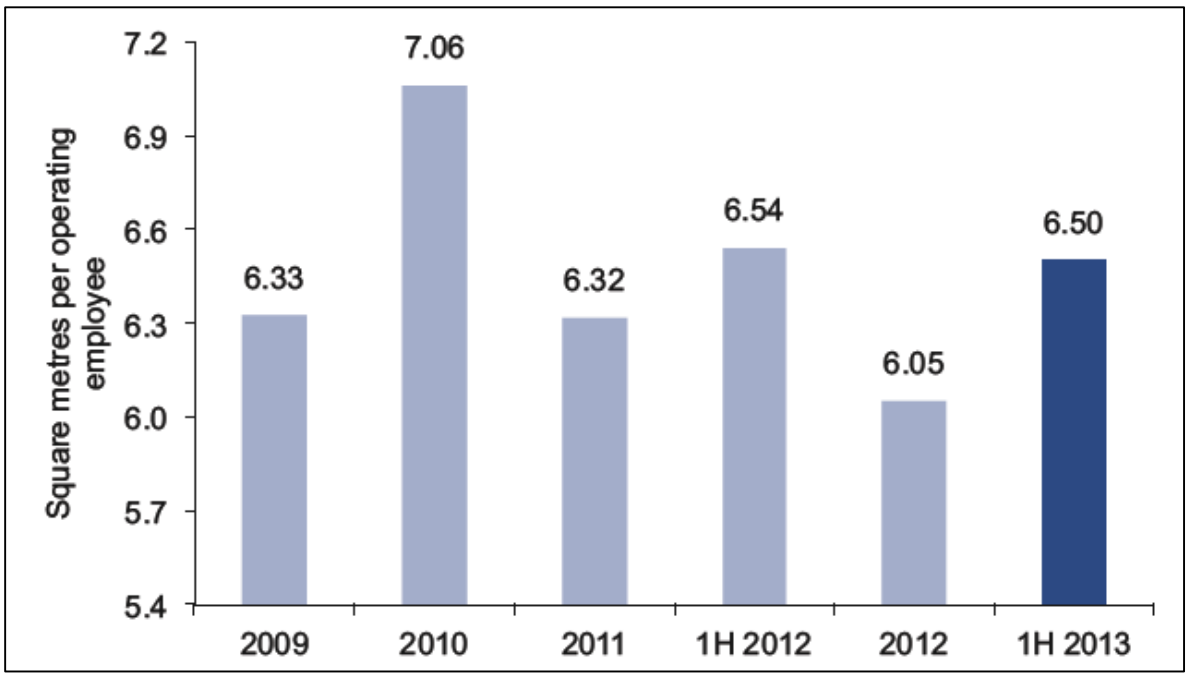


Figure 29: AAP labour productivity profile (Anglo American Platinum Limited, 2008-2015).

For AAP Productivity levels vary year on year without a significant positive or negative trend. Figure 29 above reflects the productivity level at AAP post the implementation of the ESOP.

6.2.5 Regulatory compliance

Similar to KIO, the implementation Kotula ensured compliance with HDSA ownership requirements of the Charter with uncertainty around interpretation with the DMR remaining an issue.

6.2.6 Summary of Kotula

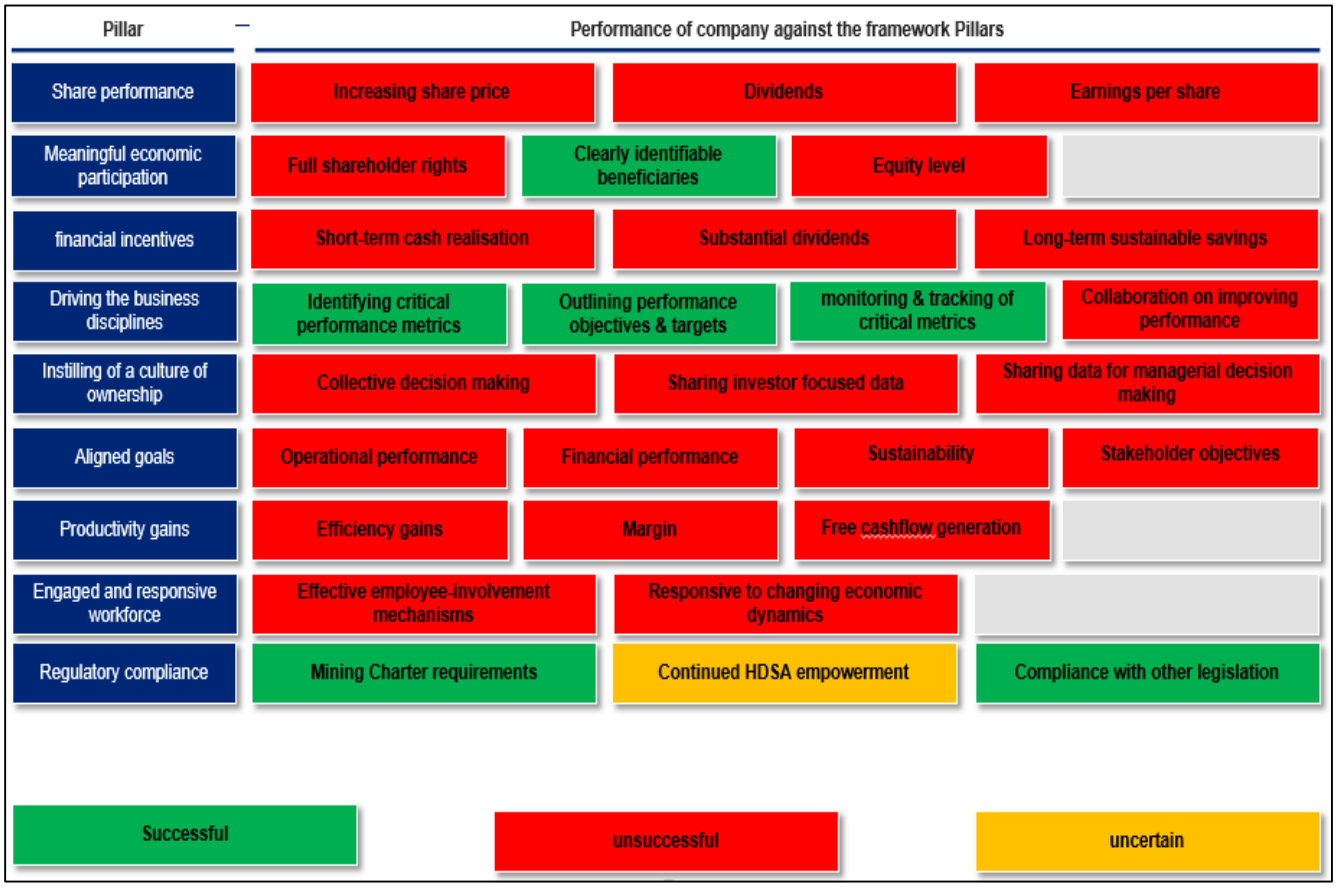


Figure 30: Summary of AAP performance evaluated against proposed framework

6.3 Summary

Anglo American's two listed entities had ESOPs that had varying financial performance. High company earnings lead to higher dividend payments, which are ultimately reflected in a rising share price. High company earnings are achieved through productivity gains and demand factors. When measured against the other success criteria, the ESOPs did not compare favorably. Productivity levels, instilling an ownership culture and aligning goals with employees remain a challenge.

7 CONCLUSION AND RECOMMENDATIONS

Empowerment of previously disadvantaged groups has been applied in various countries throughout history; and it has been applied in many different forms aiming to achieve specific political, social and economic objectives. In the profiled countries, these policies have had varying degrees of success.

South Africa continues to struggle with poverty, unemployment and inequality; realities brought about by past policy instruments and bias. BEE is seen as an appropriate approach for providing opportunities for HDSAs who suffered from economic exclusion.

The major mining houses have completed empowerment deals, with the most significant deals involving individual HDSA entrepreneurs. The deals have been completed as a response to the requirement of the Mining Charter, governed under the MPRDA, for more ownership participation by HDSAs.

These empowerment deals have garnered criticism for not being sufficiently broad-based, and for empowering a few individuals. Mining companies have also implemented ESOPs in their respective businesses.

In this report, Anglo American was used as a proxy for the industry, due to its size and diverse nature. Current ESOPs in Anglo American were found to be inconsistent, sometimes complicated; and they remain largely opaque to the employees.

When employees are made to be part owners and meaningful participants in the success of the business, this leads to a more productive workforce that is engaged, and has an increased sense of responsibility in generating higher returns. Current ESOPs have failed to imbue an ownership culture within their employees. An

employee's ability and opportunity to participate in the decision-making processes contributes to the success of an ESOP.

A successful ESOP should not just pay out money to employees, but it should change behaviors of both beneficiaries, management and owners of the business. This report has proposed a new framework for ESOPs under which it is envisaged that future ESOPs be modelled. The framework takes into account the needs of all important stakeholders, namely employers, employees and government. The framework is centred on 9 key pillars.

These are share performance, meaningful economic participation, financial incentives, driving the business disciplines, instilling a culture of ownership, aligned goals, productivity gains, and engaged and responsive workforce and regulatory compliance.

The new framework is underpinned by a set of key fundamental principles. Employees short term needs should be reconciled with the long term aspiration of the organisation. The technical aspects of the ESOP should be aligned with the change management requirements for effective implementation. The impact of the ESOP needs to change employee behaviour and thus benefits should be immediate and meaningful.

The performance of ESOPs in Anglo American varied when assessed against the framework. With the exception of Envision, Anglo American's ESOPs have delivered very modest financial benefits to employees. They have not achieved their intended purpose, of empowering employees and aligning company performance with individual employee performance. Envision has benefited from the iron ore up-cycle; but Kotula and AASA have suffered from a general weakness in AAP and AA plc's share prices, respectively. When assessed against the other pillars of the framework, KIO and AAP did not perform satisfactorily.

This report recommends that mining companies, irrespective of size and commodity group, implement this proposed approach, in order to fully harness the virtues of ESOPs. The report further recommends that appropriate programmes specific to each pillar be instituted.

Further work needs to be conducted on how to create a working environment where employees can participate in the decision-making processes of the business. Programmes that that will give effect to the framework can be investigated. Clarity needs to be sought on the relationship between the BBBEE Amendment Act and the Mining Charter. Issues around interpretation of the ownership pillar (*"once empowered always empowered")* is also required.

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9 APPENDICES

Appendix 1: Summarised HDSA ownership results

SECTOR	HDSA OWNERSHIP (%)	PARTICIPANTS (million)	MIN. NET VALUE (R billion)	MAX. NET VALUE (R billion)
Mining Industry	37.7	7.0	155.32	282.018
Black investors	22.8			
Community	10.8			
ESOPs	4.2			
PGM	39.5	2.77	43.442	65.987
Black investors	19.5			
Community	18			
ESOPs	2			
Gold	28.8	0.14	7.182	32.267
Black investors	18.6			
Community	0.9			
ESOPs	9.2			
Coal	43.9	1.75	24	49.512
Black investors	32			
Community	5.3			
ESOPs	6.3			
Diamonds	26	0.11	0.616	5.29
Black investors	4.4			
Community	11.6			
ESOPs	10			
Iron Ore	38.2	1.48	53.22	115.33
Black investors	24			
Community	12			
ESOPs	2.2			
Manganese	50.1	0.41	-0.436	8.389
Black investors	33.3			
Community	16.3			
ESOPs	0			
Chrome	28.1	0.45	1.824	5.242
Black investors	15.9			
Community	7			
ESOPs	5.2			

Appendix 2: Summary of Anglo American Platinum Atlatsa/Bokoni empowerment deal

Sources of funds	Rmil	Application of funds	Rmil
Atlatsa/Pelawan/Plateau			
Plateau "A" prefs issued to APL	1, 193	Equity acquired in Holdco	2, 600
Pelawan "B" prefs offered to APL	1, 100	Repayment of bridge finance to APL	93
APL free contribution to communities and ESOP	149		
Total 1*	2, 442	Total 2*	2, 693
SBC loan	500	Costs, community, ESOP	249
	2, 942		2, 942

Appendix 3: Anglo American Platinum Joint Ventures (JVs)

BEE partner	Asset	Status
ARM Mining Consortium: **- 83% ARM;** **- 17% Communities**	Modikwa	AAP contributed mineral rights to the 50:50 JV for no consideration. The mine is at steady state production. ARM is a listed company with substance and significant other interests and should be able to stand behind its own obligations. AAP has been vendor-funded, through a loan, ARM's and, to an extent, the community's portion of the expansion capital. Should Modikwa underperform, this loan could be at risk of default. At present, there is a limited risk of refinancing or default. Approximately R17 million of the R131 million loan has been re-paid to date.
Northam	Pandora	AAP gave 5% of its 50% interest to Mvelaphanda Resources Limited *("Mvela")* – now a subsidiary of Northam - and sold another 2.5% for R65 million. The R65 million remains receivable.
Bakgatla	Union	Royalty agreement conversion and purchase consideration of R420 million in return for 15% participation interest. All funding to Bakgatla has been repaid. The Bakgatla has assets and it is unlikely that Anglo American would need to provide funding to the Bakgatla. The Bakgatla have expressed a desire to take up an additional 11% of Union. The additional take up right would be on a commercial basis and not vendor funded by Anglo American.

Africa Wide Minerals Prospecting a subsidiary of Wesizwe Platinum Limited	Wesizwe	AAP holds 211.9 million shares in Wesizwe (26.6%). An equalisation payment amounting to circa US$18m is still due by Wesizwe. Wesizwe completed a deal with Jinchuan in May 2011, which would fund the entire project capital of the company's project to full production through debt and equity.
RBN	BRPM	The BRPM JV was initially established in 2002 as a 50:50 JV between Royal Bafokeng Resources (Proprietary) Limited and AAP. The JV was reconfigured in 2009 to enable RB Resources to acquire a majority 67%interest in the JV with the remaining 33% held by AAP RB Plat was formed as a new company with a 67% ownership in the BRPM JV. From the 4th January 2010, operational control of BRPM vested with RB Plat. The successful listing of RB Plat on the JSE took place in November 2010 with AAP, holding an effective interest in the listed company of 12.6%. AAP received R1.452 billion by selling shares in the IPO process.

Appendix 4: Funding model for Anglo-Inyosi Coal

Source of funds	Rmil	Application of funds	Rmil
Equity Contribution	185	Acquisition capital	6, 971
Equity Inyosi	50	Project expenditure	4, 400
Equity ASAC	135		
Preference shares			
Preference shares ASAC	6, 786		
Debt finance			
Loan facility AASAF	4, 400		
Total	11, 371		11, 371

Appendix 5: Ponahalo-funding Structure

Sources of funds	Rmil	Application of funds	Rmil
Equity Contributions to Ponahalo	10	Acquisition of 26% in DBCM	3 710
Equity	10		
Preference shares to Ponahalo	3 700		
Preference shares Standard	2 900		
Guaranteed preference shares Standard	800		
Debt finance			
Loan facility AASAF	4 400		
Total	3 710		3 710