



**TOWARDS A ROBUST, SELF SUSTAINING ECONOMIC
EMPOWERMENT FINANCING PARADIGM**

BY

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A dissertation submitted to the University of Zambia in partial
fulfilment of the requirements of the Bachelor's Degree in Law

**THE UNIVERSITY OF ZAMBIA
LUSAKA**

DECLARATION

I, **Caiaphas Mwanakwale Habasonda**, do hereby declare that this dissertation represents my own work and that it has not been previously submitted for a degree at this or any other university.

Signed.....

APPROVAL

This thesis/dissertation of **Caiaphas Mwanakwale Habasonda** is approved as fulfilling the requirements or partial requirements for the award of the Bachelor's Degree in Law by the University of Zambia.

ABSTRACT

A study of Citizens Economic Empowerment Act CEE Act and the National Assembly Bill debated in run up to the enactment of this statute reveals a gap that needs to be filled with respect to the economic empowerment financing framework. While the failure to deliver of past empowerment financing frameworks is an issue to be explored in this study, the lack of a detailed legal formulation of the empowerment financing paradigm- in the current CEE Act is a serious omission in the law. The law creates an Empowerment Fund that lacks depth in terms of legal, operational and regulatory structure. The lack of depth poses a threat to the success of the Fund be compared with those of the Banking and Financial Services Act, (BSFA) 1996, which sets out in considerable detail, the *modus operandi* and the legal and regulatory framework of the banks and financial institutions under Bank of Zambia supervision. For all intents and purposes and given the amounts of funds envisaged, the Fund should have been set up as financial institution in its own right. The Fund, at K150 billion, at the latest mention, is arguably larger than the minimum capital base of Zambia's commercial banks combined. The management of such huge funds as shall be handled by the Fund, has implications in the economy. A more rigorous risk management and control framework should have been formulated. This dissertation suggests an alternative formulation which could be considered as opportunities for amending the provisions relating to the empowerment Fund present themselves.

PREFACE

Since the enactment into law of the Citizens Economic Empowerment Act, there has been a lot of expectation with respect to the Economic Empowerment Fund. Targeted Citizens have waited with bated breathe, the commencement of the disbursement of funds. The national assembly debate on the bill centered on who a targeted citizen is with some Honorable Members of Parliament insisting that this phrase should be rendered “indigenous black Zambian”. The question as to who a targeted citizen is will be tested as the Fund opens its doors to the public. Consciencious observers sense the onset of another period of financial mismanagement in Zambia. Historians are nursing a sense of *dejavu*, saying ‘we have been this way before.’

This dissertation attempts to suggest ways in which the current empowerment financing program could be protected and made more self sustaining and effective than past schemes tried since independence by ensuring adequate, legal and regulatory safeguards

This research effort, would not have been possible without the supervision and mentorship of prominent constitutional lawyer and lecturer, Mr John P Sangwa to whom I am so grateful. Over the last two years, I had the honor of meeting and discussing with Commissioners of the Citizens Economic Empowerment Commission, the subject matter of this research. I attended seminars and participated actively at various fora where this subject was presented. Without singling out any one individual, I acknowledge the contributions of these learned men and women. To Brenda and the crowd at home, I know how you endured long sleepless nights... be of good cheer. Above all, to God be the glory.

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CHAPTER ONE

RESEARCH FRAMEWORK

1.1 Introduction

In light of signal failure of past attempts at economic empowerment, the enactment on 19th May 2006, of the Citizens Economic Empowerment Act (hereinafter, the CEE Act) was an important milestone. The Act establishes an Empowerment Fund (hereinafter the Fund) to finance empowerment activities. However, it is observed that there is a lack of a detailed legal formulation of the empowerment financing paradigm. The Act does not prescribe the *modus operandi* of the Fund in much detail. Nor does it define a specific legal and regulatory frame work to govern its operations to ensure self sustainability, prevent abuse and ensure efficiency and effectiveness. The lacunae in this respect is surprising considering that there lessons to be learnt from the failed empowerment attempts and that this Fund will be bigger than some banks and non-bank financial institutions whose operating rules and regulatory regimes are clearly defined in the Banking and Financial Services Act, (BFSA) Cap 387 of the Laws of Zambia. This apparent omission is a serious flaw in the Act. A legal response to the causes of failure in past empowerment financing, can only be glossed over at the peril of any attempt at economic empowerment. This threatens the success of the economic empowerment program, *ab initio* as financial sustainability is critical.

1.2 Statement of the Problem

A review of CEE Act, and the National Assembly Bill debate, reveals a gap that needs to be filled with respect to the economic empowerment financing framework. The Fund depends on authority derived from the Citizens Economic Empowerment Commission (CEEC), which is ultimately responsible for the empowerment program, as a whole. Past empowerment schemes can not be faulted for failure to create institutions as these were designed and created deliberately to deliver empowerment financing. While their failure to deliver is a an issue to be explored in this study, the lack of a detailed legal formulation of the

empowerment financing paradigm- in the current CEE Act is a serious omission in the law. There is a certain lack of depth around the Empowerment Fund structure in the Act, where a well thought out financing formulation should have been. The lack of depth seems to stem from the fear of projecting the Fund as a key component so as not to create the impression that “Father Christmas” is back in town-the attitude that dogged previous empowerment financing mechanisms. The provisions of the Act need only be compared with those of the BFSB, which sets out in considerable detail, the *modus operandi* and the regulatory framework of the banks and financial institutions under its supervision. For all intents and purposes and given the amounts of funds envisaged, the Fund should have been set up as financial institution in its own right. The Fund, at K150 billion, at the latest mention, is arguably larger than the minimum capital base of Zambia’s commercial banks combined. Movement of such huge funds as shall be handled by the Fund, has implications in the economy. This begs the question, why should this Fund not be regulated by statute?

Our postulation then, is that given the centrality of an empowerment financing frame work, unless the Fund is a separate and independent entity from the Commission and specific rules are formulated as to its *modus operandi* and regulation, signal failure and loss of public funds is certain. The superficial broad stroke of the legislative painting brush appears to have ignored the clear definition the operating framework and the regulatory rules and left it to the Commission to set the rules and regulate the Fund on an “as you go basis”. The lack of a detailed formulation of the Fund rules in the creating statute portends high risk and potential loss of resources, with the result that the broader economic empowerment program is set up for failure.

1.3 Purpose of Study

The main objective of this research endeavor is to examine why past empowerment financing paradigms failed, picking lessons there from, defining broad principles from which an effective Fund operational strategy might emerge backed by a firm legal framework that will

count for a more robust, lasting and properly regulated financing paradigm for the success of the economic empowerment program.

1.4 Significance of the Study

A review of past financing schemes and the CEE Act forms the backdrop to the topic at hand. It identifies empowerment financing schemes and the reasons for their failures. It reviews the in Act in general and zeroes in on the Empowerment Fund and the National Assembly Bill which quickly leads the perceptive reader into the mind of the legislators of the arguments advanced in formulating the founding statute. However, a lack of a detailed formulation of an operational and regulatory framework for the Fund designed to address the causes of failure in past empowerment financing efforts to ensure that the Fund is self-sustaining, does not depend on Government and donors in perpetuity and delivers on empowerment, is immediately evident. Filling that gap is the subject of this research work, the results of which, it is hoped, will contribute to possible improvements to the Empowerment Fund framework to prevent the dissipation of public resources.

1.5 Methodology

The approach to be used is a cross between the legal centralist and legal pluralist. The research will be qualitative in nature. This will involve an extensive review of literature including statutes such as the Act itself, the Bill leading to the enactment of the empowerment statute, the Banking and Financial Services Act Cap 387, the Companies Act Cap 388 of the laws of Zambia and subsidiary legislation, repealed legislation, financial sector reforms and regulatory frameworks, the Investment Act, the Zambia Development Agency Act and the Privatization Act, as a minimum. And as the Fund, is practically a financial institution, we will draw on literature relating to risk management by financial institutions. The study will be based; predominantly on desk research given budgetary is limitations.

1.6 Time table

The progression of research will follow the prescribed timetable as follows

1. Approved proposal -30th June 2008
2. Literature Review – July/August 2008
3. First Draft- 30 September 2008
4. Discussion with Supervisor –Ongoing September/October 2008
5. Final Draft -15th November 2008
6. Discussion of Final Draft with Supervisor -1st December 2008-15th December 2008.
7. 23rd January- submission of approved version
8. January 6 -15th 2009-Binding
9. 16th January 2009-submission of approved and bound copy to Supervisor

1.7 Budget

Literature	K1,000,000
Materials & Processing	K1,000,000
Other Costs	K 500,000
Total	K2,500,000

CHAPTER TWO

LITERATURE REVIEW

2.1 Economic Empowerment – A General Historical Perspective

In the last 40 years of Zambia's independence, economic empowerment has been on the minds of Zambia's leaders. On 19th April 1968, then Republican President, Dr Kenneth Kaunda bearing the immensity of the need for the economic empowerment of Zambians, launched the historical Mulungushi Economic Reforms which, inter alia, sought to place economic control into Zambian hands; preclude resident expatriates and foreign enterprise structures and individuals from defined commercial and geographic areas; encourage citizens to fill the business void deliberately created by the exclusion of non-Zambians and to acquire majority shareholding in companies operating in key sectors of the economy such as mining, industry and financial services.

Government acquired equity holdings, invariably taking 51% or more- in a number of foreign-owned firms and brought them under the control the parastatal conglomerate, the Industrial Development Corporation (INDECO). By January 1970, Zambia had acquired majority holding in the Zambian operations of the two major foreign mining corporations, the Anglo American Corporation and the Rhodesia Selection Trust (RST). The two became Nchanga Consolidated Copper Mines (NCCM) and Roan Consolidated Mines (RCM), respectively. The Zambian government then created a new parastatal body, the Mining Development Corporation (MINDECO). The Finance and Development Corporation (FINDECO) allowed the Zambian government to gain control of insurance companies and building societies. In 1971, INDECO, MINDECO, and FINDECO were brought together under an omnibus parastatal, the Zambia Industrial and Mining Corporation (ZIMCO), to create one of the largest companies in sub-Saharan Africa, with the country's president,

Kenneth Kaunda as Chairman of the Board. In 1982 NCCM and RCM were merged into the giant Zambia Consolidated Copper Mines Ltd (ZCCM).¹

2.2 Financing Paradigms

The immediate, post independence phase saw the deliberate creation of national financial institutions to provide empowerment finance and to aid development and Zambianisation.

Chiara Chiumya, in her paper, Banking Sector Reform and Financial Regulation: Its effects on Access to Financial Services by Low Income Households in Zambia² sets out an overview of the financial sector landscape relative to historical empowerment financing efforts by the Zambian Government. She traces the need to create financial institutions serving low income Zambians to the domination of the financial sector by foreign owned banks which the Government failed to nationalize during the economic reforms of the late 1960s. Three of the major banks, Barclays Bank, Standard Chartered Bank and ANZ Grindlays Bank (now Stanbic Bank), were established in the colonial era and primarily served the interests of foreign corporate entities. Government set up banks and state owned non-bank financial institutions for various purposes, including the provision of concessional, targeted and long term finance to priority sectors to serve priority sectors and the interests of the local population in need of small and medium scale financial services. The two pronged strategy involved the establishment of government owned banks and development financial institutions on the one hand and the use of administrative controls over interest rates and to a limited extent, credit allocation.

Prior to independence in 1964, credit was provided to small-scale farmers through the then Land Bank. At independence, the Land Bank was replaced with the Credit Organization (COZ) established under the Credit Organization of Zambia Act No 54 of 1967. Poor repayment rates resulted in its insolvency and liquidation. The Agricultural Finance Company

¹ http://en.wikipedia.org/wiki/Economy_of_Zambia

² C. Chiumya 'Banking Sector Reform and Financial Regulation: Its effects on Access to Financial Services by Low Income Households in Zambia, *Development Economics and Public Policy* (November 2004), 10-12.

Limited (AFC) and the Rural Development Corporation (RDC) followed. Then Zambia Agricultural Development Bank (ZADB) which catered for commercial farmers was established. In 1987, ZADB and AFC merged to create Lima Bank which was later liquidated under the strain of non-performing debt inherited from its predecessors. The Co-operative Bank of Zambia was formed as a society under the Cooperatives Act and commenced operations in October 1991. The bank only operated for only five years before folding up due to abuse of depositors' funds. A guarantee scheme was set up in the early 1980s by the Government and administered through the Bank of Zambia to encourage financial services for the majority of the population but it failed because commercial banking models in place could not afford the high transaction costs associated with lending to the small borrowers.

There were also financing initiatives targeted towards industrial development including the Small Industries Development Organization (SIDO) later transformed into the Small Enterprise Development Board (SEDB), Village Industry Service (VIS), and the Small Enterprise Unit. The Development Bank of Zambia was established under the aegis of the Development Bank of Zambia Act Cap 363 in 1972. The Bank survives today, with a severely weakened capital position, only due to the by Government's refusal to liquidate it in 2002 at the instance of the World bank and the International Monetary Fund and its subsequent assumption on the non-performing debt portfolio and amendment of the founding Act Cap 363 to provide for a new legal and corporate structure.

2.3 Pitfalls of Past Economic Empowerment Financing Paradigms

It is a common view that these institutions failed to deliver, not on account of legal and regulatory inadequacy but due to poor corporate governance, executive mismanagement, unsustainable, inefficient and non-effective lending. The attitude by the beneficiaries and would-beneficiaries that financing institutions had been created for dispensing economic largess and independence benefits inevitably resulted in low recovery rates. While the rules

were adequately defined, these financing models failed due to allocation of credit by government and the accompanying financial repression whereby interest rates were dictated rather than determined by the markets. Government intervention led to such absurdities as lending at rates that could not cover cost. These initiatives quickly became unsustainable, depending of continuing injections of capital by Government. The marriage of convenience between the ruling party, the United National Independence Party (UNIP) and the Government as predicated by the 1973 Constitution did help matters. Empowerment Financing depended not on objective financing criteria but on the applicant's connection with the party whose influence permeated all public institutions. The link of empowerment financing to party politics is a danger to any empowerment fund.

By 1991, the one party state had overreached itself, failing to deliver in almost every facet of life. The end was inevitable. The multiparty elections of that year ushered in a new economic epoch as well. The era of liberalisation, born of a political dispensation embracing liberal democratic ideals and free market economics, was characterised by a quick shift to private ownership. Seen as symbols of a failed economic experiment, the parastatal sector and state ownership represented the very epicenter of that signal failure at economic empowerment and independence. The state enterprise sector had become a drain on state resources as it could not survive without leaning on central government for funding.

So, as the generation of new politicians acceded to power, it was not surprising that privatisation was the next logical step to follow in reversing the negative impact of state intervention gone awry. These assets had to be offloaded under the framework of the Zambia Privatisation Act. The sale of these enterprises to private hands was seen as empowerment *par excellency*. Within a decade, however, the experiment had fizzled out in failure, leaving in its wake massive unemployment, poverty and no significant impact on the economy. Most of the state enterprises had been sold off and still Zambians did not control the economy. Yes,

assets had been sold to the highest bidder in an open market but the playing field was far from level. Zambians lacked access to the finances required to take advantage of empowerment under the privatisation model as the free market model espoused private initiative even in raising the funds required to purchase assets on offer.

In the immediate post independence era, an extreme view was taken that private enterprise was an anathema to economic development and equitable distribution of wealth. An equally extreme view was taken in the post 1991 era. The slogan 'government has no business doing business' typified that attitude. With Zambians unable to buy the assets on sale and government taking the view that it had nothing to do with business, except creating an enabling environment, the privatised assets passed, vesting in a few hands, mostly foreign.

And so it has been that 40 years from President Kaunda's watershed speech and more than 280 privatisations later, the majority of Zambians remain outside the circle of major economic activity and are poor.

2.4 Economic Empowerment Revisited

It was thus, a historical moment when the Citizens Economic Empowerment Act, 2006 (hereinafter called the Act), was enacted on 19th May 2006. It portended something new and perhaps, change for the better. Borrowing heavily from South Africa's Black Economic Empowerment programme, the Zambian program was enacted into law.

This author is aware of two studies that have been conducted analyzing the Act. One such study is entitled *Final Report of the Study of the Implementation of the Citizens Economic Empowerment (CEE) Act, 2006*³. The Zambia Business Forum (ZBF) initiated this study in October 2006, with a view to establishing the historical perspectives and substance of empowerment program in Zambia, as well as establishing their successes and failures in order to provide lessons for the current efforts at empowerment.

³ R.K.K Sichinga and C. Musonda, 'Final Report of the Study of the Citizens Economic Empowerment Act 2006 (June 2008) 4-8.

The terms of reference required that the Consultants study the recently enacted CEE Act of 2006, to establish its strengths and opportunities that it offers; and to identify any weaknesses and threats that could hinder its successful implementation. The terms of the study also required that a model be developed to reflect how the Citizens Economic Empowerment law could be implemented insofar as the legislation relates to the employment equity plans; skills development; submission of information on employment policies and practices to the CEEC; the procurement thresholds for public institutions; the reservation of some economic sectors (to citizens only); the development of sector Codes and Codes-of-Good-Practices, and the creation and management of the Citizens Economic Empowerment Fund. The paper merely makes a casual reference to the Empowerment Fund, noting the need for the Empowerment Fund, which at the time of the report stood at **K120 Billion**, to be increased to provide a greater reach to citizens and ensure success through a revolving fund to avoid the pitfalls and failures of previous schemes. The authors note that while the CEEC would have overall responsibility for the implementation of the Fund, the actual management would be undertaken by fund managers and other financial institutions. The authors also pointed to the need for the CEEC to immediately identify the financial institutions and fund managers through whom the empowerment funds would be administered and to develop clear criteria which would be used, well ahead of the actual disbursement of funds and implementation of programs. The study concludes that since the lack of finance constitutes a major constraint to a much fuller realization of the potential of empowering the citizens of Zambia, the establishment of an Empowerment Fund was, therefore, welcome. The authors note the need for a more transparent system of project evaluation and disbursement of funds without elaborating why this is necessary. The report concludes that '... the robustness of the empowerment program will be significantly influenced by the resources - human and financial, which will be made available for the program. They felt that the financial resources, then standing at **K120 Billion**, were much too little to achieve the desired level of

impact that would adequately address poverty and make a significant contribution to the national wealth creation...’

The Citizens Economic Empowerment Fund is a critical component of the empowerment program. The study referred to above, gives a kaleidoscopic view of the Act, identifies its weaknesses and strengths and makes recommendation on how the weaknesses can be overcome including amendments to the Act. However, when it comes to the empowerment financing model, the writers merely endorse the position as stipulated in the Act and only recommend the increase of funds from the current level it holds to ensure adequacy. A recommendation as to a detailed formulation of the financing framework is not attempted nor is the regulatory framework thereof.

A second attempt at critiquing the Act has been made by Ndambo in his Directed Research work entitled *An overview of the Citizens Economic Empowerment Act: Does it possess the Requisite Legal Efficacy to Enhance the participation of Indigenous People (Zambian Citizens) in the Economic Affairs of the Country without Stifling the Foreign Direct Investments, UNZA 2008*. The paper discusses the overview of the Economic Empowerment Act in Zambia, its genesis, legal appropriateness, institutional arrangements, implementation targets and measures. It also discusses the risk and challenges of the Act and concludes by making recommendations⁴. This study is also kaleidoscopic in nature, touching on all aspects of the Act without zeroing in on any particular issue. It makes passing references to institutional arrangements in general and the Empowerment Fund, in particular, without delving into the formulation of the appropriate empowerment financing model. It accepts the funding model as given and concludes thus: ‘There is the danger that the Empowerment Fund will become the focus of the CEE. The Fund is not the only answer to economic empowerment. Most fear that it will only benefit the elite and will be administratively

⁴ E M Ndambo, *An overview of the Citizens Economic Empowerment Act: Does it possess the Requisite Legal Efficacy to Enhance the participation of Indigenous People (Zambian Citizens) in the Economic Affairs of the Country without Stifling the Foreign Direct Investments.*(January 2008)..

expensive. Clear guidelines administered by an independent autonomous body are necessary. If not, the Empowerment Fund will meet the same fate as other funds of a similar nature in Zambia'. The paper recommends that the Empowerment Fund should not be the focus of the CEE Act.⁵

2.5 National Assembly Bill No 3/2006: Citizens Economic Empowerment Bill

A review of the parliamentary debate held on the 21st of March 2006 when the Bill came up for second reading, is revealing in its lack of depth in terms of the Citizens Economic Empowerment Bill in general and in particular, the Economic Empowerment Fund.

The then Vice-President (Mr Lupando Mwape) presented the bill for debate⁶, relevant excerpts of which are reproduced ad verbatim:

'Mr Speaker, I beg to move that the Bill be now read a second time. When Zambia attained independence in 1964, Sir, the Government embarked on a number of programmes whose objective was to position the reigns of the economy in the hands of the newly independent nation. Though successive governments introduced economic reforms in the late 1960s and early 1990s, the majority of citizens were restricted from meaningful participation in the economy, mainly because they did not have the means to own the country's economic assets. The ownership of the major economic assets was held and controlled by the State on behalf of its citizens...'

'The disappointment of these economic reforms could be mainly attributed to lack of focus on developing the local spirit of entrepreneurship and the lack of provision of financial and other mechanisms. Similarly, the privatisation programme does not appear to have sufficiently addressed the imbalance in ownership of the means of production. The outcome from these economic policies has been the underdevelopment of a viable middle class, increase in the levels of poverty and subsequently, the emergence of an economically excluded and disadvantaged population in both the rural and urban areas...'

'The Private Sector Development Reform Programme pointed out that local empowerment and business development service for micro, small and medium-sized enterprises (MSME) and availability of finance would ensure growth with equity. Thus, the reform objective for the local empowerment component of the Private Sector Development Plan Reform Programme is to unlock the growth potential of the micro, small and medium enterprise sector through business development support and empowerment initiatives...'

'Four priority actions were identified in this area. The participation of local firms in tendering for donor-funded projects; the development of incentives for voluntary migration from the informal to the formal sector; preferential treatment for local firms tendering for Government contracts and the creation of micro, small and medium enterprises development strategy. While these reforms are

⁵ Ibid at p 47

⁶ National Assembly Bill No. 3/2006

certainly needed to expand the economic activity of the micro, small and medium enterprises, it is felt that the issue of economic empowerment of the majority of our citizens necessitates more individual attention to fully explore the issues of broad-based equitable growth...' Predictability, transparency, accountability and sustainable investor-friendly climate, for both local and foreign investors, coupled with robust simple regulatory framework are the growth (sic). In order to design and develop robust policy and financial mechanisms for measuring and evaluating economic activities, the empowerment of citizens is an imperative...'

'Sir, affirmative action and economic empowerment is not an area without difficulties and challenges... Given the experience of empowerment programmes in the region, the President will have power to prescribe and provide policy direction on the advice of the proposed commission. In practice, this means that the policy will be subject to Cabinet discussion and decision before the President describes policy directives...'

'Empowerments programmes will require political will from the highest office in the land. Therefore, the argument that the commission will be too powerful does not arise... I am, therefore, calling upon all honourable Members of Parliament to support this historical Bill...'

So introduced, the Bill was then open for debate. Member after member dealt with the definition of 'targeted citizens' which opposition members of parliament felt should be rendered 'indigenous Zambian' while the front bench held that this would be inconsistent with the Constitution of Zambia as it relates to Article 23 of the Constitution of Zambia.

Observing the lack of a deeper debate, Mr Speaker noted,

'I still have up to fifteen honourable Members who wish to contribute to the debate on this Bill, and yet, the House has been debating it for **three hours fifteen minutes** and all I have heard ...are two words, 'citizen' versus 'indigenous'. Do I have any guarantee that there will be, at least, one honourable Member who will move away from that so that we can conclude the second reading of this Bill?'

The Minister of Commerce, Trade and Industry (Mr Dipak Patel) took to the floor and addressed the House in the following terms:

'Mr Speaker, after three hours and eighteen minutes, the whole debate has centred on the definition of a targeted citizen...Mr Speaker, in this Bill, we have a provision for an employment equity plan that will make sure that companies have an employment equity plan that will promote Zambians to managerial positions...Sir, there are provisions ... that deal with...skills development...Sir, the Bill provides for preferential procurement...It provides, under Clause 21, investment opportunities...The President can prescribe...economic sectors ...that can be reserved for Zambians...It provides for regional development ...It provides for fronting...Any company that uses a Zambian as a front and is found out will be penalised severely...Mr Speaker, it takes care of the experiences of the 1968 reforms...provides for a fund through the Pensions Funds to securities and the capital market that can be used to empower Zambians...'

The Bill was passed for the second reading. Apart from casual references to the Empowerment Fund, no thought was put to the failed financing paradigms of the past, no

reference was made to the lessons learned and, therefore, no attempt was made to address the risks and short comings of past financing arrangements to ensure the Fund was not at risk. It is not surprising that the *modus operandi* Empowerment Fund, its legal structure and regulatory framework were not defined. No discussion was made relating to the Economic Empowerment Fund or its legal, operating and regulatory structure and functions.

CHAPTER THREE

THEORIES OF EMPOWERMENT

3.1 The Concept of Economic Empowerment

In recent times, there has been a re-conceptualization of economic development policies. Development based on World Bank (WB) and International Monetary Fund (IMF) models of the 1970s and 1980s, met with dismal failure despite debt and aid being pumped into poor countries during that period. One reason cited for this failure has been the lack empowerment on the part of the communities in which these policies were implemented. The 1990s saw the evolution the concept of empowerment, in general and in particular, economic empowerment. This concept has gained currency to the extent that it now informs both economic policy and legislative action.

Economic empowerment may be defined in as many ways as there are people defining. This makes the concept difficult to implement concept, let alone operationalize. Clarity and specifics are, thus, extremely essential, especially where management of funds is the proposition as is the case in the citizens empowerment paradigm in Zambia. The absence of rules or for that matter, the presence of ambiguous rules and regulations only results in confusion and failure.

A strong regulatory framework has a rightful place in financial systems stability. A *laissez faire* approach as encouraged by the Republican Establishment in the United States of America has resulted in an unprecedented global financial crisis with many a once solid finance institution either bankrupt or close to bankruptcy. Believing the virtues of free market capitalism, financial regulation was frowned upon and considered as interference in the market place. The result has been less and less market regulation, over the years so that when the credit crunch arrived, there was no safety net. Without regulations, market players create internal rules as they go along. These rules tend to favor the market makers and to feed their greed.

Abdalla Gergis⁷, in his working paper, *Citizens Economic Empowerment in Botswana: Concepts and Principle* ably presents the current theoretical underpinnings of the concept of economic empowerment. He poses the question, ‘What is empowerment?’ and then proffers a simple Webster’s Dictionary definition, which says to empower is to “‘give power to” or “‘to enable” someone””, before delving into the complexities of empowerment. His discourse is insightful and provides a useful backdrop to the subject of this dissertation. He correctly observes that empowerment is a complex and often misunderstood concept which is connected to concepts of self help, participation, networking and equity. Empowerment has come to refer to popular participation, promotion of community development through self-help with emphasis on the process, rather than on the outcome of particular development projects; transformation of societies into self reliant, endogenously developed communities; and good governance, legitimacy and creativity for a flourishing private sector.

He traces the concept of empowerment as a response to historical paradigms whereby people participated in projects without the power to decide the critical issues of the related to the project. Other authors such as Rappaport [1987] ascribe to empowerment, “‘a psychological sense of personal control or influence and a concern with actual social influence, political power and legal rights””.⁸ McArdle postulates that empowerment is “‘the process whereby decisions are made by people who have to bear the consequences of those decisions””.⁹ Gergis points out that the fundamental goal of empowerment is to help individuals within the society to improve the quality of their own lives and share equitably in the benefits of economic growth. He observes that growth that depends on a constant infusion of grants or subsidized financing from government and other donors is inherently unsustainable.

⁷ A. Gergis, ‘Citizens Economic Empowerment in Botswana: Concepts and Principles’, *BIDPA Working Paper No 22*, July 1999.

⁸ J Rappaport, ‘Terms of Empowerment/Examples of Prevention: Toward a Theory of Community Psychology’, *American Journal of Community Psychology*, Vol.15, No 2, (1987), 121-148.

⁹ J Mc Ardle, (1989), ‘Community development Tools of trade’, *Community Quarterly* 16, (1989), pp47-54.

Empowerment is about helping people unleash their creative and productive energies to achieve sustainable growth and continuous improvement in their living standards. 'More generally, empowerment means engaging the relevant stakeholders in a given process by applying the principles of inclusiveness, transparency and accountability. As such, the empowerment concept goes beyond the notions of democracy, human rights and participation to include enabling people to understand the reality of their environment and to take the necessary actions to improve their well being.' Gergis further speaks of the motivational dimension of empowerment concluding that people have to be motivated. They must to believe in merits and prospects of empowerment. People will not be empowered if they do not want to be. Empowerment is creates the conditions conducive to enhance this motivation to perform by developing the person's sense of self-determination and enhancing his/her belief in self efficacy. It entails providing the individual with the ability to perform-the necessary skills, knowledge, and giving a fair opportunity to perform.

Empowerment is, therefore, multi-dimensional. However, while it is not merely about money and its equitable distribution, money remains the means by which true empowerment might be achieved and measured. Its sourcing, distribution and management and availability are mission critical. Fund is, thus, the cog in the wheel of economic empowerment.

3.2 Empowerment or Entitlement

In South Africa, Black Economic Empowerment is the nomenclature used to describe the empowerment initiative in that country. Its definition is stated as 'an integrated and coherent socio-economic process, located in the context of national transformation that is aimed at redressing the imbalances of the past'¹⁰. The legislative basis is the legal instrument christened the Broad-based Black Economic Empowerment Act No. 53 of 2003. The Black Economic Empowerment Advisory Council directly under the control of the South African President, is the implementing agency.

¹⁰ 'Empowerment Under the Microscope' Enterprise 133, (June 1999) 46-47.

In Botswana 'economic empowerment has been understood to mean a set of policies or programs designed to benefit a specific segment of the society; the Batswana. There is a widespread perception or belief that citizens are disempowered by temporary residents from other countries who command more economic power in business in the form of investment, higher technical skills and entrepreneurship. Thus, some interpret the concept of citizens' economic empowerment to mean the creation of indigenous business elite to rival the more successful foreign business interests within Botswana. Others understand it as acquiring certain exemptions from some business rules or obligations, such as exposure to competition, the provision of security on loans, and even the protection against legal action arising from non-fulfillment of contractual obligations. For others, it means the entitlement to a share in a Government-owned company or public asset'¹¹. Gergis, correctly, observes that this understanding caused concern for the policy makers in Botswana.

Economic empowerment in Zambia is understood not significantly differently from that of their Batswana counterparts. The CEE Act speaks of targeted citizens – defined to include anyone who is or has been marginalized or disadvantaged and whose access to economic resources and development capacity has been constrained due to various factors including race, sex, educational background, status and disability. The concept conveys the same expectations in Zambia. The parliamentary debate during the second reading of the Citizens Economic Empowerment Bill was almost exclusively focused on what targeted citizen and indigenous Zambian. The use of the phrase; targeted citizens' was, clearly, a compromise since reference to indigenous Zambian would have amounted to an inconsistency with Article 23 of the Constitution of Zambia. The parliamentary debate on the bill reveals the mind of parliament on this. While it was understood that the target was the

¹¹ A. Gergis 'Citizens Economic Empowerment in Botswana'.

indigenous Zambian, it was tacitly agreed that the use of that phrase would be offensive and would send the wrong signals to the investor and donor community. An ambiguity which is bound to be problematic was, thus, allowed into the law. The technocrats at the CEEC would carry the burden of discretion in deciding who qualifies since it was assumed they would know who was meant. Thus, one of CEEC's roles is the identifying the beneficiaries. However, administrative discretion comes with arbitrariness and subjectivity.

The preamble to the Citizens' Economic Empowerment Act of 2006, is couched in the following terms; 'An Act to establish the Citizens' Economic Empowerment Commission and to define its function and powers; establish the Citizens Economic Empowerment Fund; promote the economic empowerment of targeted citizens, citizen empowered companies, citizen influenced companies and citizen owned companies, promote gender-equality in accessing, owning, managing, controlling and exploiting economic resources; encourage an increase in broad-based and effective ownership and meaningful participation of targeted citizens, citizen empowered companies, citizen influenced companies and citizen owned companies in the economy in order to contribute to sustainable economic growth; remove social customs, statutory provisions or other practices that limit access to any particular gender to skills training that is essential for effective participation in the economic sector; promote the employment of both gender by removing structural and discriminatory constraints that hinder any particular gender from employment opportunities and in so doing ensure equitable income distribution; promote equal opportunity of targeted citizens and citizen empowered companies, citizen influenced companies and citizen owned companies in accessing and being awarded procurement contracts and other services from State institutions; promote green-field investment through joint ventures and partnerships between local and foreign investors in order to enhance broad-based economic empowerment; and provide for matters incidental to or connected to the foregoing'.¹²

¹² Citizens Economic Empowerment Act No. 9 of 2006

The broad spectrum of issues covered in the preamble reflects the lack of specific focus in identifying the mischief that gave rise to the need to legislate which could explain why the Act does not delve into specific rules when making provisions governing the Fund. And due to the ambiguity arising from the broad descriptions, many would-be beneficiaries tend to entertain notions of entitlement where empowerment is the legislative intention. This attitude was at the root of failure of past empowerment schemes in Zambia. For example, credit facilities deliberately targeted at indigenous Zambians to counter the absence of an existing appropriate financing models for this target group were regarded as part of their share of what has come to be described as the national independence cake and not as contractual obligations to be repaid to the lender. Seen as vehicles for the distribution of political largess and not as a self sustaining means of citizens' economic empowerment, these empowerment schemes failed. The institutions themselves were reluctant to use the hard-nosed commercial risk management approaches in the identification, assessment and management of lending risk and in the monitoring and recovery of bad debt as managements felt such an approach would hurt the entitlement of the people and by extension, the popularity of the party in power. They unwittingly re-enforced the notion that empowerment financing through government was not to revolve on a self sustaining basis but was a gift.

To too many, economic empowerment implies entitlements. Entitlements by their nature 'create a dependency attitude, undermine the power of positive thinking of one's own ability and nurture the feeling of helplessness and being disempowered'...opportunities can be created for citizens [but] equal outcomes can not be guaranteed...'13

3.3 Strategies for Economic Empowerment

To design an economic empowerment strategy, it is necessary to first identify the individuals or groups that need to be empowered and then to understand the sources of their

¹³ Gergis, 10.

disempowerment. A strategy to empower the private sector, for example, will necessarily be different from a strategy to empower women.¹⁴ This informs the correct operational strategy, appropriate risk policy and legal/regulatory framework. In the case of the empowerment fund, it informs the risk profile of the targeted groups, defines the relevant safe guards, the risk-reward paradigm and the strategy that would be appropriate to ensure a self-sustaining empowerment fund.

The strategy mix would include the following components: financial intervention to assist local business activities (increased access to credit); enterprise development for citizens' increased access to skills, business and management training and improved production technologies; marketing strategies for locally produced goods and services to increase access to markets and bargaining strategies (for higher wages, better working conditions etc for citizen employees).

In deciding an empowerment financing strategy due regard should be paid to global competitiveness; economic efficiency; participation of the empowerment target, self-empowerment, empowerment rather than entitlement, the business environment which should ideally be less regulated and to transparency. It should be understood citizenship is not a right to be shielded from the consequences of economic decisions and that education is a fundamental empowerment tool. Creating new jobs leads to more citizen empowerment than providing preferential treatment for citizens in filling existing jobs. While the above list is devoid of any tacit reference to legal principles, in the end, all human activity tends to and must, find convergence in law. Laws and regulations, define relationships, responsibilities and authority, thereby creating a standard of reference for the operating strategy chosen. Without the legal framework, discretion is the source of authority and discretion is abused. Empowerment programs and institutions created to implement and manage the process must themselves be under-girded by strong legal and regulatory frameworks that allow free market

¹⁴ Ibid, 12

efficiencies not to be subsumed by the sense of entitlement rather than empowerment. Corporate Governance must be strong to ensure transparency, accountability and responsibility and when one falls short of these standards, sanctions and penalties must follow to regulate and correct behavior.

As a minimum, the CEE Act should have allowed for the creation of implementing institutions with define rules and/or separate legislation and/or delegated powers to deal with the minute operational rules required to achieve expected operational efficiencies and adherence to the broader principles in key aspects of the empowerment program. In this way, appropriate regulatory oversight, which finds its potency in law, would have been in place to safeguard the Fund. The CEE Act is patently short on sanctions and penalties, delivering an impression that entitlement rather than empowerment is the intent. Legal jurisprudence requires of a good law to encourage good behavior and to frown on non-compliance. And where there are funds to be had and given the historical context of empowerment financing in Zambia, the Act should have been louder and more unequivocal in its punitive aspects.

It is easy to see that the Empowerment Fund will find its force, not in a detailed formulation of rules but rather on the few sweeping provisions carried in the CEE Act. Subsection 6 (6), provides that ‘in the performance of the Commission's functions under this Act, the Commission shall effectively liaise and consult appropriate State institutions and shall have the power to give such instructions or directions to any State institution or a company’. The commissioners are appointed by the President and “the President may give to the Commission such general or specific directions with respect to the discharge of its functions as the President considers necessary and the Commission shall give effect to such directions. Under subsection 5, the Commission shall be empowered to take whatever actions necessary to ensure broad based economic empowerment of targeted citizens, citizen empowered companies, citizen influenced companies, and citizen owned companies. These provisions give the CEEC broad powers. Rather than being a source of effectiveness,

this is bound to spread the energies of the CEEC thin, thereby dissipating them over a larger field of issues.

CHAPTER FOUR

THE EMPOWERMENT FUND

4.1 The Character of the Citizens Economic Empowerment Fund

Section 29 of the CEE Act creates the Citizens Economic Empowerment Fund. The Fund consists of (a) such money as may be appropriated by Parliament for the purpose of the fund; (b) moneys received by way of grants, fees, loans or donations for the purposes of the Fund; and (c) interest accrued from any investment made by the Commission or raised through the local stock exchange. Section 30.(1) defines the seat of the Citizens Economic Empowerment Fund as vesting in the Commission but the Fund shall be managed and administered by various financial institutions and fund managers that meet the criteria prescribed by the President. By Section 30(2), the Commission shall establish the criteria for the application and disbursement of moneys from the Fund. In only two brief sections, the institutional framework of the Fund is defined. At once, one notices that the Fund relies on the juridical identity of the CEEC and does not have a personality separate from the Commission which by Section 4(1), is established as a body corporate with perpetual succession and a common seal, capable of suing and being sued in its corporate name and with power, subject to this Act, to do all such things as a body corporate may by law do or perform. This weakens the mandate of the Fund itself.

The Fund will handle billions of Kwacha. The management of the Fund is likely to be one of the most significant challenges of the Commission and yet the Fund's structure, operating rules, legal and regulatory framework are not elaborately defined. The Act does not provide rules for the supervision and policing of the Fund.

The CEE Act is couched in terms that suggest that the success of the citizen's economic empowerment program will depend on not so much on intrinsic legal power inherent in the Act itself but on the weight of the all-powerful presidency which is given a fair share of power. The language used in the Act, perhaps belies pent up frustration arising out of the

failure of past empowerment programs. The then Leader of the House, Honorable Lupando Mwahe, Vice President, in presenting the empowerment bill for the second reading alluded to what he referred to as 'regional experiences' to justify the central involvement of the President. The centralization of power speaks volumes as to the apparent lack of depth surrounding the institutional framework to deliver the objectives of the Act in general and in particular, around the Empowerment Fund, which we postulate to be a central plank in any well meaning empowerment program.

We hazard that in the wake of failed empowerment financing arrangements of the past, the Act should have been more circumspect, addressed the causes of failure of past financial models and provided a robust legal response as to the legal, regulatory and the operating structure of the Fund so that future empowerment financing would be self-sustained and not be abused to the benefit of the few.

Since the Fund has no rules of its own, it would not be a far fetched proposition to say parliament meant it to be covered by the sweeping provisions enumerated above since 'in the performance of the Commission's functions under this Act... the Commission ... shall have the power to give such instructions or directions to any State institution or a company' and on account of the fact that, 'the President may give to the Commission such general or specific directions with respect to the discharge of its functions as the President considers necessary and the Commission shall give effect to such directions'. The use of the word shall, in law, connotes the absence of discretion, alternative, choice or preference. What the President instructs or directs the Commission has no choice but to implement. Being appointees, the Commissioners would be expected to do the pleasure of the President. The Presidency is inextricably linked to the ruling party, whichever is in power owing to the structure of party politics in Zambia. Under these circumstances, it is not difficult to see that the President could give such general or specific directions or instructions such as serve party interests, for example disbursing funds from the Fund to the party faithful

during an election campaign period without due regard to project viability or financial feasibility.

4.2 Mode of Operation of the Fund

As mentioned already by section 30(1), the Citizens Economic Empowerment Fund has its seat in the Commission but it will be managed and administered by various financial institutions and fund managers that meet the criteria prescribed by the President.

Subsection 30(2) give power to the Commission to establish criteria for the application and disbursement of moneys from the Citizens Economic Empowerment Fund. Other operating rules specifically stipulated are as follows; Section 31 providing that the Citizens Economic Empowerment Fund shall be audited every year by auditors appointed by the Commission with the approval of the Auditor-General and that by Section 32 (1), the Commission shall cause to be prepared an annual audited statement of income and expenditure with respect to the approval of the Auditor-General. Further, according to subsection 32(2), the minister responsible for the commerce, trade and industry shall, not later than seven days after the first sitting of the National Assembly next after receipt of the audited statement of income and expenditure referred to in subsection (1), cause it to be laid before the National Assembly. These provisions are important for transparency and accountability on a *post facto* basis. If there is a problem, little can be done about as revealing problems after the fact is akin to bolting the stable when the horse has already bolted, to use this English adage.

It is provided under Section 32(3) that the Commission shall, in order to facilitate the flow of financial resources to programs for broad based economic empowerment-

(a) on its own or in cooperation with other State institutions identify citizen owned companies, groups of citizens or co-operatives, citizen empowered companies and citizen influenced companies and broad-based economic empowerment programs, which require financial assistance; (b) provide information on sources of finance and promote investments

for companies and programs specified in paragraph (a); (c) on its own or in cooperation with other State institutions and other institutions render development services to companies specified in paragraph (a) so as to enable them access financial resources; (d) in conjunction with any financial institution financing micro and small enterprises, monitor, establish and design standards for loan administration, effective use of loan funds and repayment mechanisms by groups of citizens or co-operatives of companies specified under paragraph (a) so as to curb misuse of financial resources; (e) on its own or in consultation with any relevant financial institution establish or source venture capital funds to promote investments in companies specified under paragraph (a); and (f) secure incentives through relevant authorities for any financial institution which undertakes to finance or develop a company specified under paragraph (a) or any company carrying out any broad based economic empowerment program.

In sub section 32(4), where a company specified under paragraph (a) of subsection (3), has been funded through the Citizens Economic Empowerment Fund the Commission shall, in partnership with any financial institution, devise a mechanism to lock in the equity of the company, for a reasonable period of time, in order to ensure value addition to the company.

4.3 Procedures for Accessing the Fund

The procedures for accessing the Fund have been released. These show that the political structures, namely, the District and Provincial Development Committees which are invariably run by District Commissioners appointed by the President, will be involved in the identification and initial project evaluation and in making recommendations to financing entities where the amount involved is K50m or less. For amounts above this threshold, applications will be evaluated by the CEEC. While it is intended that commercial criteria apply when deciding who is granted access to the Fund, the involvement of political structures is likely to lead to poor client and risk identification. It should be recalled that the

Commission is empowered to take whatever actions necessary to ensure broad based economic empowerment of targeted citizens, citizen empowered companies, citizen influenced companies, citizen influenced companies and citizen owned companies. In the name of economic empowerment, vital safeguards that may be put into place to protect the Fund could easily be overridden if it was felt that they were impeding the empowerment of targeted citizens. Fund management is by nature bureaucratic, if risk is to be properly managed. Pre-conditions are set which must be met prior to a beneficiary accessing the funds. These will be lengthy given that commercial banks will still have to follow their intricate, rigorous internal procedures for identifying, assessing and measuring risk before disbursing the funds. In addition, the majority of the targeted citizens are not financially literate enough to package their project financing proposals in a form required by existing commercial banking financing models which will be the delivery vehicles for disbursing the Funds. The Commission is more than likely to be frustrated, especially that politicians had already taken to the podium to announce the “disbursement” of the funds way before the procedures for accessing the funds had been finalized and the public have been waiting for the Fund too long already.

4.4 Fronting

The Act recognized the problem of Fronting and provides for its penalties in subsection 32 (5), prescribing that where the Commission proves to its satisfaction that any company specified under paragraph (a) of subsection (3), is engaged in fronting, that company shall be barred from accessing any moneys from the Citizens Economic Empowerment Fund or from benefiting from any incentives under this Act and in addition shall be liable to any penalty specified under subsection 32(6) which states that any moneys from the Citizens Economic Empowerment Fund or any incentives under this Act that would have been granted to a Company in which a Director or Shareholder is engaged in fronting, will be withdrawn.

Subsection 32(7) states that any director or shareholder of a company that engages in fronting commits an offence and shall be liable on conviction to a fine not exceeding two hundred thousand penalty units. By subsection 32(8) “fronting” includes holding out as being the de facto director or shareholder of a company in order to hide the true identity of the shareholders or director of that company.

The CEE Act provides sanctions for fronting only as if this is the only source of abuse and yet there are a myriad ways of abusing the Fund for which no sanction or penalty is provided. It may be that the framers of this law thought these abuses were adequately covered by other laws. From failed empowerment schemes in the past, it would have been possible to provide for regulations that would prevent such occurrences.

4.5 Implications of the Lacunae in the Law

It would seem that the void on the legal, operational and regulatory arrangements in the with respect to Fund derives from the assumptions implied in the sweeping provisions. These provisions clearly assume either that the financial institutions and fund managers to manage and administer the funds are already adequately regulated and, therefore, the need for Fund specific legal, statutory and regulatory rules is dispensable or that the Commission will apply its sweeping powers to cover the lacunae. This is a false dichotomy.

First, commercial banks, non-bank financial institutions and fund managers have their operating mandates under their respective articles of association which may not coincide with citizens’ economic empowerment financing objectives. The mandates given to them by their shareholders may only dovetail with that of the CEEC coincidentally and they will, thus, not be overly concerned with meeting empowerment objectives and protecting the empowerment fund, if there is a divergence of interests. For example, if the commercial banks have surplus funds from deposits and lending opportunities are tight, the banks will always seek to lend out their won funds as opposed to lending out the empowerment fund since banks are subject

to reserving requirements for any deposit they hold. The Fund monies may not move in this case.

Secondly, their objectives, policies and financing models will diverge when seen in the light of the empowerment fund's objects. Certainly empowerment is not among the objectives of their existence and if it happens to be, it is certainly the least.

Thirdly, these institutions are not homogeneous. Financial institutions include commercial banks, non-bank financial institutions, insurance companies and pension funds. Different pieces of legislation provide for their regulatory oversight. While regulatory paradigms exist for each segment of financial institutions, it is arguable whether these will be adequate to protect the Fund since the operative instrument between the Commission and the institutions would only be the memorandum of co-operation.

Fourthly, these institutions are not all regulated under the same rules and regulations. Nor do they fall under the same supervisory authorities. These authorities have different minimum regulatory requirements and criteria which have nothing to do with citizens' empowerment goals and will, not therefore, have the proper oversight framework to regulate the Fund. Monitoring of the Fund will be complex, cumbersome and expensive. This is not to speak of the burden of new reporting requirements that would enable the Commission monitor the respective portfolios effectively.

While the CEE Act is overarching in its reach and is couched to be superior to other pieces of legislation, it is inconceivable that an institution will pay more attention to the provisions and objectives of the CEE Act at the expense of its founding legislation or, indeed, its articles of association let alone its policies and priorities.

There is a very real possibility of the empowerment funds not being accessed as envisaged under the Act. Being entrusted in the hands of private institutions with financing models not compatible with empowerment financing, and given the quest to maintain efficiencies,

commercial criteria of individual institutions, must apply. Only a few good projects may be funded under these circumstances.

4.6 Prognosis and Prescription

On account of the above prognosis, this author argues that a special purpose vehicle is required to ensure a targeted well regulated, operated and managed fund separate from existing financing structures which could only come in as a second line of intervention in a tiered model. If the Empowerment Fund will handle much larger sums than the minimum capital requirements of, say, the whole banking commercial banking sector combined, then risk management and control regime which, at a minimum, is as rigorous as that of the banking sector is required on the basis the Fund will handle public funds, a fiduciary duty to which the Fund must remain true to at all times. The empowerment Fund should be an accountable, transparent and responsible entity. This will not be the case under the current arrangements as the Commission will, at once, make funding policies, police them, decide the criteria, identify beneficiaries and process funding. A separation of powers is necessary with the CEEC retaining a policy making and supervisory function. The day to day empowerment financing issues are better left with the Empowerment Fund, one of whose responsibilities would be to keep a pulse on market trends to ensure that idle funds are well invested.

The Companies Act Cap 388 and the Banking and Financial Services Act (BFSA) Cap 387, provide for operating and the regulatory principles of all companies and banking and non-bank financial institutions. In addition, these institutions are governed internally by their articles of association and risk policies and practices. The policies at play take into account these overriding pieces of legislation. A cursory examination of such policies shows that the rules for operating and managing these institutions are specific almost to the smallest detail. The framers of both the BFSA and the Companies Act bothered to include in parliamentary legislation such minute details as qualification and disqualification of directors, proceedings of the Board of Directors or the winding up of such institutions in addition to delegated

legislative and regulatory powers. If empowerment revolves around the distribution of advantage whose currency is inevitably money, there is no escaping the fact that, there will be interests and where there are interests to be served, conflicts which need clear rules to resolve should be designed upfront and have the force of law. If it was possible to include regulatory and institutional detail in the BFSA and the Companies Act, a detailed formulation of the Empowerment Fund legislation would not have been beyond the framers of the founding empowerment statute.

CHAPTER FIVE

NATIONAL EMPOWERMENT FUND ACT 1998, SOUTH AFRICA:

A CASE IN POINT

5.1 The Character of the National Empowerment Fund of South Africa

The National Empowerment Fund Act 1998 (NAF) of South Africa suggests an alternative legal and regulatory framework for a stand alone empowerment fund. Christened Act No. 105 of 1998, the bill was assented to by President Nelson Mandela on 19th November 1998. The Act establishes the Fund as a trust for the promotion and facilitation of ownership of income generating assets by historically disadvantaged persons; to set out the objects of the trust; to provide for the powers, appointment and mode of operation of the trustees; to provide for the establishment of other investment entities for the attainment of the objects; to provide for the powers of the Minister to give implementation directives; to provide for the sale of shares in State Owned Commercial Enterprises at a discount to the trust or by the trust to the beneficiaries; to provide for the control of the financial affairs of the trust; to provide for the establishment of an investment holding company by the trust; to provide for the promulgation of regulations; to provide for the dissolution of the trust; and to provide for other incidental matters.

The NAF Act, sets out objectives of the Trust, provides for the powers and appointment of the Trustees and prescribes the mode of operation of the Fund. It provides for the control of the financial affairs of the trust and gives provision for the creation of a holding company. The Act also provides for the promulgation of regulations and the dissolution of the trust. This Act recognizes the primacy of legislation in creating the funding structure of economic empowerment financing. The structure is set up with the mandate that it 'must distribute wealth, boost the small and medium enterprise sector, have sustainable affirmative action implication and facilitate genuine black economic empowerment' and 'in order to establish

structures and mechanisms to redress the inequalities brought about by apartheid by facilitating the broader economic ownership by historically disadvantaged persons’.

The “Trust” is defined as the National Empowerment Fund established in terms of section 2 of the NAF Act and the “trustees” as trustees of the Trust constituted in terms of section 8. By section 4(1) of the NAF Act, the Trust is constituted as a body corporate with perpetual succession, and subject to the provisions of this Act, is capable in law, in its own name, of suing and being sued, of acquiring, holding and alienating movable and immovable property, and of performing such acts as a body corporate may by law funding mandate. By placing the Fund under the aegis of the CEE commission, the Zambian Funds mandate is stifled.

The Act defines the meanings relevant for the operationalisation of the Fund, rendering clarity of meaning from the onset. For example, in this Act, unless the context indicates otherwise- “Assets” or “fund” or “trust assets” or “trust fund” mean and include-(i) shares in State Owned Commercial Enterprises or private business enterprises acquired by the trustees; (ii) monies, securities, investments, properties or any other assets which may be acquired by the trustees or which any person may vest or cause to be vested in the trustees as part and for purposes, of the Trust; (iii) income of the Trust. The NAF Act covers a wider spectrum of financial instruments and activities all of which add to the self-sustenance of the fund and which are separate from the Black Economic Empowerment legislation which deals with issues at a broader macro level.

5.2 Objects of the Fund

The object of the Trust is to facilitate the redressing of economic inequality which resulted from the past unfair discrimination against historically disadvantaged persons by providing historically disadvantaged persons with the opportunity of, directly or indirectly, acquiring shares or interest in State Owned Commercial Enterprises that are being restructured or in private business enterprises; encouraging and promoting savings, investments and meaningful

economic participation by historically disadvantaged persons; promoting and supporting business ventures pioneered and run by historically disadvantaged persons; promoting the universal understanding of equity ownership among historically disadvantaged persons; encouraging the development of a competitive and effective equities market inclusive of all persons in the Republic; contributing to the creation of employment opportunities; and generally employing such schemes, businesses and enterprises as may be necessary to achieve the objects of this Act.

Unlike that of its Zambian counterpart, the South African Fund defines the various objectives and areas of intervention. The Fund's functions are wide ranging so as to encompass direct and indirect ownership of shares in state and private business, the encouragement of savings and investment, business ventures, development of an equities market (financial deepening and widening), employment generation etc. The Trust has a broad-based mandate not merely confined to liquid or near liquid investments. As a stand alone entity, the Fund is given power to do more than just paying out funds.

5.3 Duty of Care

A duty of care is imposed on the Trustees. Under Section 5, a trustee must in the performance and execution of his or her duties and the exercise of his or her powers act with such care, diligence and skill as may reasonably be expected of a person who manages the affairs of another person. Where a duty of care is imposed, consequences are bound to follow, if that duty of care is neglected.

The CEE Act is silent on this duty of care. The implication is that once appointed by the President, the Commissioners may operate as they think fit (which may not always be in the best interest of the country) provided they do the pleasure of the President. Where the latter has party interests, it is easy to see how the strict duty of care to country can be neglected in the empowerment process. That is why the CEEC, standing on the same platform as ruling

party campaigners during the Presidential by-election, announced the release of K10 billion each to the provinces, even though fund administrative structures had yet to be in place, provincial fund managers had not yet been appointed and procedures were still being prepared. It is paramount that officers charged with managing the Fund are sworn to a duty of care.

5.4 Qualification/Disqualification of the Trustees

Section 6 (1) stipulates the general qualifications of trustees which include that of being persons who are committed to fairness, transparency and accountability. Section 7 (1) presents the disqualifications. A person, who is not a citizen of the Republic of South Africa, one who is adjudged to be of unsound mind, an undischarged bankrupt (an un-rehabilitated insolvent) or otherwise declared bankrupt and one with a criminal record is ineligible to hold the office of trustee for obvious reasons. These disqualifications are as stringent as those of being a director under the Companies Act Cap 388 of the laws of Zambia. They are also similar to those governing elections for members of the National Assembly according to Article 65 of the Constitution of Zambia. This suggests that the management of the Fund is taken very seriously. The Empowerment Fund structure in Zambia does not explicitly impose such a standard on those tasked to manage the Fund. It is implied that the Commissioners meet these standards.

5.6 Appointment of trustees

The process of appointment of trustees is prescribed. Under section 8(1), the President must on the advice of the Minister appoint not more than seven but not less than five trustees and the procedure is clearly elaborated. The number of candidates must not be less than 5 and should not exceed 7. Section (4) (a) provides that the additional trustees, to make the complete number of 11, must be appointed by the Minister on the recommendation of the trustees.

5.7 Term of office of trustees

The term of office of trustees is prescribed by 9(1). The chairperson must hold office for three years as will the other trustees appointed by the President. (d) The term of office of additional trustees will run concurrently with their term of employment, which term of office will be prescribed by regulations. The trustees appointed in terms of section 8(1) by the President are engaged on a non-executive basis and the trustees appointed in terms of section 8(4) by the Minister are engaged on an executive basis for the daily management of the office of the Trust.

5.8 Removal from office

By Section 11, a trustee may be removed from office by the Minister on account of misconduct; inability to perform the duties of his or her office effectively; absence from three consecutive meetings of the Board without the prior permission of the chairperson, except on good cause shown; failure to disclose an interest in terms of section 14(2) or attendance at, or participation in, proceedings of the Board while having an interest as contemplated in section 14(1); or any other ground which in terms of the laws and principles governing trusts constitutes the basis for his or her removal as a trustee.

5.9 Meetings of Board

By Section 13(1), meetings of the Board must be held at such times and places as may be determined by the Board. Subsection 2 provides that in the absence of the chairperson at a meeting the remaining trustees must from their number elect an acting chairperson. And that by sub section 13(3)(a) the chairperson may, at any time within reasonable notice, convene a special meeting of the Board, which must be held at such time and place as the chairperson may determine. (b) Two trustees may in writing request the Chairperson to convene a special meeting. (c) The trustees must convene a special meeting if the chairperson fails to convene a special meeting within seven days after receiving a request.

Under subsection 13(4)(a), the quorum for any meeting of the Board, at any time must either be a minimum of five trustees or 50 per cent of the trustees in office at that time, whichever number is the greater; (b) If 50 per cent of the trustees is a fraction, the number required shall be the nearest higher whole number. Under subsection (5)(a), a decision of the Board must be taken by resolution agreed to by the majority of trustees present at a meeting of the Board subject to subsection 13(4). By subsection 13(5)(b) The Chairperson must have a deliberative vote, and in the event of an equality of votes, a casting vote.

5.10 Disclosure of conflicting interests

By Section 14 (1) a trustee must not participate in the proceedings at any meeting of the Board if he or she or his or her family member or business partner is a director, trustee or business partner of, or has an interest in the business in question, or in relation to any matter before the Board which may preclude him or her from performing his or her other functions as a trustee in a fair, unbiased and proper manner. Section 14(2), provides that if at any stage during the proceedings of the Board there is reason to believe that a trustee has an interest, that trustee must-(a)disclose fully the nature of his or her interest; and (b)leave the meeting or hearing in question. By subsection 14(3), the remaining trustees must discuss the matter and determine whether that trustee is to be precluded from participating in such proceedings and make a decision in terms sub-section 14(4). The disclosure and the decision taken by the trustees regarding such determination must be recorded in the minutes of such proceedings.

5.11 Proceedings of Board not invalid in certain circumstances

Section 15 covers protects the decision making process. A decision taken by the Board or an act performed under the authority of such a decision must not be invalid by reason of- (a) an irregularity in the appointment of a trustee; (b) a vacancy on the Board; (c) the fact that a trustee is guilty of an act or omission justifying his or her removal from office; or (d) the fact that any person who is disqualified from being a trustee or who was removed from that office

sat as such on the Board at the time when such decision was taken, if such decision was taken by a majority of the trustees lawfully entitled to vote and the said trustees at the time constituted a quorum.

5.12 Powers of Trustees

The powers of the Trustee are provided for under section 16 and include the acquisition, administration and control the assets of the Trust in accordance with its objects subject to the provisions of this Act. In addition, the trustees must have all such powers as may be necessary to enable them to administer the trust and may procure the incorporation of a company or companies registered in terms of the Companies Act for the purpose of holding all or any of the trust assets; and require such company or companies to dispose of all or any of the shares in any such company to such persons and on such terms and conditions as the trustees may from time to time determine; invest in such manner as they may think fit, subject to the provisions of this Act, the capital amount and such income from the trust which may not be immediately required; and realize vary and transpose any securities, assets, investments and property as they may determine; purchase, sell, exchange, lease, hire or otherwise acquire or dispose of movable or immovable property or any right therein; and improve and develop any property or assets of the trust; expend trust funds pertaining to any immovable property on maintenance, construction, improvement, alteration, payment of rates, taxes, insurance premiums and other charges; advance and lend money to any person, company, corporation, association or institution, either with or without security and upon such terms and conditions regarding repayment or otherwise as the trustees may decide; borrow money and in order to provide security for such borrowing, mortgage or pledge trust assets and arrange the manner of repayment of such loans; pay all expenses incurred in connection with the administration of the trust; employ any person to manage or assist in the management of the assets of the trust and to remunerate including traveling and other expenses which may necessarily be incurred by such employee from funds or income of the

trust; appoint agents for any specific purpose, including the power to appoint accountants, attorneys, advocates and other professional persons for any specific purpose; take action in a court of law for the recovery of any amounts due to the trust or compel the fulfillment of obligations in its favor and defend any proceedings that may be instituted against the trust; enter into an agreement or arrangement regarding the terms and conditions of payment of money due to the Trust and the abandonment of any claims by the Trust, accept grants and transfers from the State or donations from other persons in favor of the Trust, subject to the terms and conditions as may be imposed by the State or other persons, but such terms and conditions must not be inconsistent with the terms of the Trust; purchase or otherwise acquire any equipment that may be necessary for the purpose of meeting the administrative requirements of the Trust; open and control any bank account or building society account and draw, accept or give promissory notes, bills of exchange and other negotiable instruments; and finance, undertake and promote the education of the historically disadvantaged persons in economic and investment issues and their participation in economic and investment activities.

The Trust has powers akin to that of a financial institution so that it may not be constrained in dealing with the assets of the fund. This is important since the Fund must be able to create assets and liabilities in order to grow its balance sheet and to support the many activities it is tasked to undertake. This is does not only diversify risk but also provides the Fund with the flexibility required to implement targeted actions to fulfill its mandate. Thus under Section 21(c) ...the Trust may establish, promote or facilitate the establishment of companies, trusts, unit trusts, management companies, or other suitable business entities for purposes of engaging in activities or schemes designed to economically empower historically disadvantaged persons.

The Trust itself is organized and regulated by the NAF Act so as to ensure good corporate governance. It does not take this important issue for granted. The undefined nature of the

Fund structure in Zambia assumes the issue of governance and yet it has been one of the most important reasons for failed empowerment financing schemes.

5.13 Chief Executive Officer and his qualifications

In terms of Section 17(1) the board with the approval of the Minister, appoint a Chief Executive Officer of the Trust, subject to the terms and conditions and employment contract which he or she may conclude with Trust. According to sub section 17(2), the personal requirements and the disqualifications applicable to the trustees as referred to in sections 6 and 7, respectively, with the necessary changes, apply to the Chief Executive Officer. By section 17(3) the Chief Executive Officer is by virtue of his or her office a member of the Board with full powers accorded to any other trustee of the Trust. The Chief Executive Officer is the executive officer of the Trust and shall be responsible for the management of the activities of the Trust and under section (5)(a), the board may delegate to the Chief Executive Officer such powers as may be necessary in managing the activities of the Trust and under subsection (b), the Chief Executive Officer may delegate such powers to the staff, committees, other trustees or other structures of the Trust.

5.14 Financing of Trust

Section 18(1) provides for the operating and capital expenses of the Trust which is financed by grants, loans, income generated by the Trust or money appropriated by Parliament for that purpose. Section 18(2) required that the Trust utilizes any money referred to in subsection (1) in accordance with the statement of estimated expenditure referred to in subsection (3) which states that the Trust- (a) must in each financial year, at a time determined by the Minister, submit to him or her for his or her approval granted with the concurrence of the Minister of Finance, a statement of estimated income and expenditure, for the next financial year; (b) may in any financial year submit adjusted statements of estimated income and expenditure to the Minister for his or her approval, granted with the concurrence of the Minister of Finance;

and (c) must comply with the provisions of the Reporting by Public Entities Act, 1992 (Act No. 93 of 1992). Notice that what is described given for operating expenses under the NAF Act is what appears as the mainstay of the Zambian Fund. Sustainability will not be easy.

5.15 Banking account

Section 19 authorizes the Trust must open and maintain an account in the name of the Trust, with a bank registered as a bank in terms of the Banks Act, 1990 (Act No. 94 of 1990).

5.16 Reports

Reporting is covered under section 20(1) whereby the Trust must furnish the Minister with information and particulars as he or she may in writing require in connection with the activities of the Trust; and annually, within six months from the end of each financial year, furnish the Minister with a consolidated report with regard to the functions, affairs, activities and financial position of the Trust during that financial year and provide a statement of the progress achieved towards realization of the purposes of this Act in that financial year. The annual report referred to in subsection (1) may include such other information as the Minister may determine.

Under subsection 20(3), the Minister must, within 14 days after he or she has received a copy of the annual report, table it in Parliament if Parliament is then in ordinary session or, if Parliament is not then in ordinary session, within 14 days after the commencement of its next ordinary session. The Trust is accountable to parliament.

5.17 Transfer of State Assets

Section 23(1)(a) allows the Trust to purchase or acquire shares in State Owned Commercial Enterprises, as such shares may be offered to the Trust by the State, on such terms and conditions as may be determined by the Minister in consultation with the Ministers in charge having regard to the recommendations of the trustees. Under section 23(b), the Minister is

authorized to determine or agree to a price for the shares which price may be less than the market related price of the shares. In terms of section 23(2), the terms and conditions of sale of shares to the Trust may include (a) deferred payment of the purchase price payable by the Trust;(b) the minimum or maximum price at which the Trust may sell the shares to the historically disadvantaged persons, or business entities; (c) such other terms and conditions as the Minister may determine with the concurrence of the Minister of Finance and the trustees.

Under section 23(3), the Trust is entitled to, either partly or wholly sell, transfer, or in any way deal with the said assets or shares for the purpose of meeting the objects of the Trust, subject to the provisions of any agreement applicable to the shares in question.

5.18 Establishment of Investment Holding Company

Owing to the vast nature of the interests contemplated in respect of the NAF section 24(1), authorizes the Trust to establish an investment holding company known as the National Empowerment Fund Corporation. The object of the Corporation is to hold investments of the Trust in a commercially sound manner and carry out such investment activities as its directors may determine. The Trust may transfer into the Corporation any of its assets in exchange for the shares issued to the trust. The Trust may, in consultation with the Minister, invite any strategic equity partner to acquire shares in the Corporation, but the Trust will not hold less than 70 per cent of the shares in the Corporation. The Corporation must be registered in terms of, and be governed by, the provisions of the Companies Act, 1973 (Act No. 61 of 1973).

5.19 Funds of Trust

The responsibilities of the Chief Executive Officer spelt out in section 25. The Chief Executive Officer of the Trust is charged with the responsibility of accounting for all assets, shares or money received by the Trust, and payments, discharges or loans made by the Trust. The trust assets or funds must not form part of the assets of the trustees. The funds of the Trust consist of (a) money appropriated by Parliament; (b) interest or income derived from

investments of the Trust; and (c) grants, donations and bequests made to the Trust; (d) money lawfully obtained by the Trust from any other source.

5.20 Financial Year

The financial year of the Trust is the period extending from 1 April in any year to 31 March in the succeeding year. The Board must (a) keep proper records of all the financial transactions, assets and liabilities of the Trust; (b) prepare financial statements, as soon as possible but not later than six months after the end of the financial year or such other period as the Minister may by notice in the *Gazette* determine. The financial statements of the Trust must be audited by an auditor or firm of auditors registered in terms of section 20 of the Public Accountants and Auditors Act, 1991 (Act No. 80 of 1991), appointed by the Board. The audit must be completed within six months from the end of the financial year of the Trust. The chairperson of the Board must furnish the Minister with such information as the Minister may require relating to the activities of the Trust.

5.21 Dissolution of Trust and Distribution

Section 28(1) anticipates dissolution on a date determined by an Act of Parliament. Subsection (2) stipulates that the assets or the proceeds of those assets must, after the payment of all the liabilities of the Trust or the assumption thereof by the State pursuant to an Act of Parliament, upon dissolution of the Trust, be ceded and transferred to the State or any beneficiary as may be appointed by the Act of Parliament referred to in subsection (1).

5.22 Application of Trust laws and principles

29. The Trust is governed by all laws applicable to trusts.

5.23 Suggestions from the NAF Model

In Zambia, the founding Act, does not specifically define the Fund but only describes as consisting of- (a) such money as may be appropriated by Parliament for the purpose of the

fund; (b) moneys received by way of grants, fees, loans or donations for the purposes of the Fund; and (c) interest accrued from any investment made by the Commission or raised through the local stock exchange. This description immediately narrows the scope of the definition of Fund. The word investment, for example, is supposed to be a catch-all phrase for the activities of the Fund. However, the specific reference to interest income only suggests investment is defined in its narrowest sense-that is money in its liquid or near liquid form. This seems to exclude investments in property or any other assets where interest is not the income earned or which can not be dealt with on the stock exchange. Thus, sources of funding for Zambian Empowerment Fund appear limited, being confined to money that may be appropriated by Parliament, grants, fees, loans or donations for the purposes of the Fund, interest accruing on any investment or money raised through the stock exchange.

The alternative model on the lines of the South African NAF, established as an independent, entity regulated by statute and with clear internal policies and rules gives the NAF powers to invest not just monies appropriated by parliament, monies obtained from grants, loans and donations turn over the initial moneys and interest accruing on investments or raised on the stock exchange. The Zambian Fund should have had power to acquire shares in state and private enterprises, acquire and utilize for empowerment, idle public assets and in addition to granting lines of credit to commercial banks, non-bank financial institutions and pension funds for on lending, powers to establish companies in areas such as banking to handle its investments and lend in its own right to grow the Fund in a diversified manner, limit the Fund's vulnerability to shocks and to deliberately channel Funds were private commercial financial intermediaries may not venture. The Fund would also run advisory services directly linked to empowerment funding so that money lent is applied productively.

The NAF Act provides for a "Board" which is defined to mean the board of trustees as constituted from time to time and for the appointment of a "Chief Executive Officer" in accordance with section 17 of the Act. The Act envisages possible conflict of interest and

defines “Family member” or “member of the family”, in relation to any person, means his or her parent, siblings, child, including adopted child, or spouse, including a person living with that person as if they were married to each other. This definition anticipates a situation whereby the beneficiary may be selected on the basis of an influential related party and not on an objective and fair basis. The CEE Act does not anticipate this. Having not anticipated situations of abuse, the CEE Act is silent on issues such disclosure, conflict of interest and how to deal with such situations. It assumes regulations will be made on an “as we go basis”.

The CEE Act speaks of targeted citizens, citizen empowered companies, citizen influenced companies and citizen owned companies, promote gender-equality in accessing, owning, managing, controlling and exploiting economic resources; definitions are supplied. However, lack of clarity remains. For example, a company where 25% of the shares are owned by citizens is described as “citizen’s influenced”. This is inconsistent with corporate governance in reality. An individual or entity holding a 25% shareholding in a company is a minority in relation to the rest of the shareholding and has, therefore, no influence in the decisions of a company.

CHAPTER SIX

CONCLUSION AND RECOMMENDATIONS

6.1 Conclusions

The operating structure and the legal and regulatory framework on which Economic Empowerment Fund is premised appears weak because the formulators of the CEE Act did not pay much attention to the legal, regulatory and operating structure of the Fund. This is bound to constrain the effective operation of the Fund and make it inefficient and prone to waste. While past empowerment models were backed adequately by law but lacked adequate supervisory oversight, failure resulted mainly from operating in a controlled market environment. The close link between politics and these financing schemes was another source of problems which manifested in management by political appointees and operations being imposed by the political superstructure. Inefficiency, corruption and mismanagement impaired risk identification, assessment, measurement and mitigation. Financing facilities were viewed as entitlements rather than as means of economic empowerment. Loans were not repaid resulting in low recovery rates, high loan loss ratios and the eventual liquidation of carrying entities. Current economic fundamentals appear right for an efficient empowerment financing framework. The legal, operating and regulatory structures need to be robust.

6.2 Recommendation

An alternative formulation based along the South African National Empowerment Fund model provides a more comprehensive, properly structured and more robust framework. A stand alone entity with a distinct legal personality being able to sue and be sued in its own right and having powers to provide a wide variety of financial and related interventions without having to derive its mandate from CEEC and which is subject to the Companies Act Cap 388 and the Banking and Financial Services Act is recommended. Future amendments should focus on these matters to allow for proper accountability at entity level and for risk based regulatory and supervisory oversight of this Fund.