

**TELKOM SA SOC LIMITED**  
**(Incorporated in the Republic of South Africa)**  
**(Registration Number 1991/005476/30)**  
**(JSE share code: TKG)**  
**(ISIN: ZAE000044897)**  
**(“Telkom” or the “Company”)**

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**EXPLANATORY MEMORANDUM ON THE BUSINESS TO BE TRANSACTED AT THE TELKOM ANNUAL GENERAL MEETING OF SHAREHOLDERS OF THE COMPANY AT GALLAGER CONVENTION CENTRE, GALLAGHER GRILL, 19 RICHARDS DRIVE, MIDRAND ON FRIDAY THE 27<sup>TH</sup> OF SEPTEMBER 2013**  
***(INCLUDING AMENDMENTS TO RESOLUTIONS PREVIOUSLY PUBLISHED BY WAY OF NOTICE OF ANNUAL GENERAL MEETING ON THE 29<sup>TH</sup> AUGUST 2013 (the “NOTICE”)***

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## **I. INTRODUCTION**

As a Company incorporated in terms of the Companies Act No. 71 of 2008 (“the Act”), Telkom belongs to a category of companies required to hold an Annual General Meeting of shareholders (“AGM”) in accordance with the provisions of that Act and its regulations. The purpose of such an AGM is to transact the following business, as a minimum:

- a) presentation of the directors’ report, the Annual Financial Statements as well as the audit committee report;
- b) election of directors
- c) appointment of an auditor; and
- d) any matters raised by shareholders, with or without advance notice to the Company

The Telkom AGM will be held on Friday, 27 September 2013, and the Company’s shareholders (“Shareholders”) are entitled to attend, speak and vote at the AGM. Shareholders may also vote by way of proxy, or they may nominate representatives to attend, speak and vote on their behalf. Should a Shareholder elect to nominate a representative, then such representative must be properly authorised. It is of critical importance that a letter of representation or a power of attorney be provided to such representative to serve as proof of authorisation in such circumstances.

In the notice of the AGM posted to Shareholders on Thursday, 29 August 2013 (“Notice”), Shareholders who have not dematerialised their shares or who have dematerialised their shares with “own-name”

registration were requested to submit their proxy votes to Computershare Investor Services Proprietary Limited 48 hours before the AGM. The board of directors (“the Board”) however wishes to advise Shareholders that proxy forms not delivered to the transfer secretaries by the relevant time, can nevertheless be lodged immediately prior to the AGM, in accordance with the instructions therein, with the Chairperson of the AGM (and Shareholders are requested to do so at least by 08h30, which is 30 minutes prior to the time appointed for the AGM).

Shareholders will be asked to vote on a number of resolutions (ordinary and special) recommended by the Board, after due and careful consideration, as is the Board’s fiduciary responsibility. It should be noted that, in recommending these resolutions, the Board does so in the belief that the Shareholders will support interventions that will enable the success of the Board’s turn-around strategy and lead to the enhancement of Shareholder value. The Board holds the view that approval of the proposals will enhance the Board’s ability to make decisions effectively, thus enabling the Board to properly discharge its fiduciary responsibilities in the best interests of the Company.

It is in the interest of Shareholders to ensure that their actions are directed towards protecting their interests. Shareholders should exercising their voting rights with proper consideration of information provided to them and a firm grasp of the challenges facing their Company, coupled with the proper application of their minds to recommendations presented to them by the Company.

The Board presents the proposals in the knowledge that Shareholders are expecting a change – a significant improvement in the Company’s performance and a determined effort to enhance value for the Company’s stakeholders. It is hoped that Shareholders will provide the support that the Board requires in order to effect the required change and deliver on its mandate.

## **II. BUSINESS TO BE TRANSACTED AT THE AGM**

As set out in the Notice, the following business will be transacted at the AGM:

### **1. Presentation of Annual Financial Statements (“AFS”)**

The audited Group Annual Financial Statements for the year ended 2013, approved by the Board, will be presented to Shareholders for notification. This is in accordance with section 61(8)(a)(ii) of the Act, which calls for presentation of the AFS to Shareholders. The AFS also include the Directors’ Report, the Auditors’ Reports as well as the report of the Audit Committee.

Should a Shareholder believe that the AFS do not comply with the requirements of the Act and applicable regulations, such a Shareholder may follow their statutory and/or common law Shareholder remedies.

The Group Annual Financial Statements to be presented to Shareholders have been duly audited in accordance with required standards, regulations and laws, and the auditors of the Company (E&Y Inc.) have issued an unqualified report in respect thereof.

## **2. Social and Ethics Report**

The Social and Ethics Committee of the Board will provide feedback on its activities as required in terms of the Act Regulations.

After the presentation of the Social and Ethics Committee report, Shareholders will be asked to vote on the following ordinary and special resolutions:

***(The Company's Memorandum of Incorporation ("Mol") requires more than 50% for ordinary resolutions to pass and at least 75% approval is required for special resolutions to pass)***

### **II (A). ORDINARY RESOLUTIONS**

#### **3 – 11**

#### **Ordinary Resolutions 3 to 9**

These resolutions concern the election of all directors appointed to fill vacancies on the Board. Those appointments are those which took place during the intervening period between the last AGM (2012) and the coming AGM (2013). Telkom's Mol provides that the term of office of a director appointed during such a period/ to fill a vacancy will terminate at the end of the first AGM to be held after such director's appointment, unless the director is elected by Shareholder at the AGM or any other Shareholders' Meeting.

The directors proposed to be elected in terms of these provisions are Mr. J Mabuza, Mr. S Maseko, Ms. K Mzondeki, Mr. L Maasdorp, Mr. L Von Zeuner, Ms. F Petersen, Ms. S Botha, Ms. K Kweyama and Dr. C Fynn, respectively. Shareholders are encouraged to familiarise themselves with the respective Board Members' qualifications, skills and experiences through reading their profiles, which are set out in the Integrated Annual Report. The profiles should enable Shareholders to get some sense of the skills set and diversity of experiences that make up the Board.

## 12 –15

### Ordinary Resolutions 10 - 13

These resolutions relate to the re-election of directors who retire by rotation in terms of the provisions of the Company's Mol. A third of directors must retire at every AGM. The directors to retire are determined with reference to length of service since their last election - so that directors who have held office for a period in excess of three years or longer since their last election will be first in line for retirement. Thereafter directors longest in office since their last election or re-election shall be included in the pool of directors required to retire, until the quota of a third is complied with.

It should be noted that the Mol is emphatic on the requirement that a third of directors should retire. It also does not matter whether one had retired at the last AGM, if such director is among a third of directors who fall within the definition of longest serving as outlined in the Mol, then such director will be required to retire again. Directors retiring by rotation may, if eligible, offer themselves for re-election by Shareholders. The Mol further provides that directors who have been in service for a period of 9 years be required to retire at every AGM, and the Board is required to provide a compelling motivation for recommending that a director to continue serving in such cases.

Directors due for retirement in terms of these provisions are Mr. Schindehütte, Mr. Kgaboesele, Mr. Kapila, Mr. Du Plessis and Mr. Molobela respectively. All of these directors have indicated that they are available for re-election, except for Mr. Du Plessis.

Two directors who have been in service on the Board for a relatively long period are Messrs.' Molobela and Du Plessis. Mr. Du Plessis has indicated that he will not be offering himself for re-election. Mr. Molobela is available for re-election but the Board's recommendation in respect of Mr. Molobela is that he should not be re-elected.

The Board wishes to reconstitute itself by injecting fresh skills, appropriate to the growth trajectory that the Company will be pursuing as part of its turn-around objectives. The Board also has a desire to instill and embed an ethos of a focus on one common goal viz. the achievement of its mandate within proper governance parameters, without taking away or detracting from the individual responsibility imposed on directors to act in the interests only of the Company.

The decision of the Board in regard to this recommendation was taken unanimously, and not without due care and careful consideration of all relevant factors, *inter alia*:

- the work of the Board especially in the context of the challenges that lie ahead and the haste with which they have to be dealt with;
- the direction in which the Board seeks to take the Company - in this regard it is important that the Board demonstrates a collective commitment to achieving success in respect of the turn-around objectives; and
- the need for a collegial environment which allows for robust debate and deliberation, insists on adherence to good governance practices and where Board Members show a clear focus on acting in the best interests of the Company etc.

As stated earlier this proposal was considered by the Board and each director supported the proposal. It is also important to note that the proposal was considered with Mr. Molobela's full knowledge and he was present at all Board meetings where the matter was discussed and was given an opportunity to respond.

Shareholders should acquaint themselves sufficiently with the skills and attributes of the directors presenting themselves for election/re-election. To this end, the Company has provided brief resumes of the directors, for the Shareholders' due consideration. Details of committees on which the respective directors serve are also provided, as well as the attendance records of directors. Taken together, this information is intended to aid Shareholders in the proper exercise of their rights in relation to the election of a Board to manage and direct the affairs of their Company. Shareholders may use this information, in addition to any other information available to them, and factor it into their process of decision-making when voting on the proposals relating to the composition of their Board. Shareholders are also referred to the importance of the provisions of the Act in relation to the probity requirements and standards of conduct required of directors.

In recommending these directors, the Board also considered other factors, including but not limited to the skills set required to discharge its mandate and intended objective of turning the business around, the need to inculcate a culture of good governance on the Board and across all levels in the organisation, the Board's commitment to true diversity, the contribution of the respective Board members to the work of the Board, the respective Board members having met the probity requirements set out in the Act and having each demonstrated that they subscribe to the notion of acting in the best interests of the Company to the exclusion of all other considerations that would be contrary to this notion, the desire to effect positive change for the benefit of all stakeholders, the Board's collective commitment to working towards the achievement of its mandate of enhancing stakeholder value through acting in the best interests of the Company at all times, the ability of the Board members to bring their diverse skills and experiences to bear in furtherance of the objective of the Company and in accordance with the requirements set out in King III in relation to the role of a Board (whether acting individually or acting as a collective), the Board's

collective recognition that theirs is to direct the affairs of the Company, and to do so by means of providing ethical leadership as contemplated in King III.

In essence, the Board is satisfied that its recommendations in regard to director elections/re-elections have been thoroughly considered and are designed to enable effective delivery of the turn-around strategy required by Shareholders, and doing so within accepted governance standards, and within parameters of its mandate, the requisite authorities granted to it by the Shareholders of the Company from time to time as well as in compliance with applicable laws.

#### **16 –19 Ordinary Resolutions Numbers 14 - 17**

These resolutions propose the election of an Audit Committee for the Company, in accordance with the requirements of the Act. The directors being put forward to discharge the responsibilities of the audit committee are Mr. Kgaboesele, Ms. Petersen, Ms. Mzondeki and Mr. Von Zeuner respectively. These directors meet the requirements of the Act in respect of the skills and experience that members of an audit committee are required to possess. The profiles of these directors are provided in the Integrated Annual Report of the Company.

#### **20. Ordinary Resolution Number 18**

This resolution is proposed in order to ensure that the Company complies with statutory requirements as these relate to the appointment of auditors and matters related to such appointments. The governance enhancement parts of the Act require that a process be followed for the appointment of auditors for certain categories of companies and Telkom falls into one such category to which these provisions apply. The process entails a level of involvement by Shareholders in such appointments, in that their approval is required for such appointments. Shareholders should examine whether the auditors proposed to them meet certain requirements in relation to e.g. appropriate skills to equip them to deal with the nature and complexity of the Company, possess the requisite (resource) capacity to discharge their responsibilities as required in law, display the requisite levels of independence - which is required to provide comfort to Shareholders on the ability of the auditor to discharge their assurance responsibilities and to lend credibility to their assurances etc.

The Board is recommending the appointment of Ernst and Young Inc. to serve as the Company's auditors for the coming year, such appointment to endure until the Company's next AGM in 2014.

The Board makes the proposal on the basis of a recommendation to this effect made to it by the Audit Committee in accordance with the governance processes of the Company. Having duly applied its

collective mind to all the factors relevant to the appointment of an auditor for the Company, and having duly satisfied itself as to the suitability of the firm to carry out the statutory functions of auditor as required under applicable laws and standards, the Board is comfortable that the proposal it is recommending, if passed, will enable the Company to meet its reporting requirements as laid down in the Act and other applicable regulatory instruments, and will at the same time assist the Board in the discharge of its greater corporate governance responsibilities, in particular those relating to ensuring that proper financial controls and appropriate internal controls are in place as required. The overall objective of the Board in proposing the approval of this resolution is again the preservation and enhancement of value on a sustainable basis, for the benefit of all the Company's stakeholders, including Shareholders.

## **21. Ordinary Resolution Number 19**

The Listings Requirements of the JSE Limited ("JSE") ("the Listings Requirements"), Schedule 10 par 10.1, read together with clause 9.2.2 of the Company's MOI, allow for Shareholders to give a general authority to directors to issue and allot shares (within certain parameters). This authority is such that directors are granted the authority to issue and allot shares as they deem fit, with the effect that any pre-emptive rights that Shareholders may hold "fall away". In other words, should directors exercise this general authority and issue shares, any Shareholders' pre-emptive rights would not be given effect to. Examples of instances where directors might use this authority would be in the case of e.g. issuing share in respect of an acquisition. It is important to note that directors would not be allowed to exercise this authority for major issues of shares - those would still require Shareholder approval in terms of s41(3) of the Act or the Listings Requirements (Sections 9 and 10 thereof). Such JSE transactions are classified as category 1 or 2 transactions or related party transactions, as the case may be, and Shareholder approval is mandatory for such transactions. This should provide some measure of comfort to Shareholders in that the general authority granted in terms of this resolution would have limited application and would not enable the Board to enter into major transactions and issue shares without first calling a General Meeting of Shareholders.

It is also important to note that the Board proposes that the authority to issue and allot shares be subject to certain conditions, including a (voluntary) cap of 5%, which is far below statutory/regulatory thresholds allowed for such resolutions.

Resolutions granting a general authority to directors to issue and allot shares are not uncommon among South African entities, especially listed entities. The value of such an authority to the Board is that it serves as a useful governance/decision making tool. It gives the Board the ability to take advantage of business opportunities that might present themselves in the course of the year, without the need to call a Shareholders' Meeting. It does sometimes happen that an opportunity presents itself to a Company, but

the nature and/or size of such an opportunity is not enough to justify the calling of a Shareholders' Meeting, but is sufficiently significant to require that, in order for the contemplated transaction to be implemented, the Board would be required to issue shares. The Board should be able to transact in such circumstances without the need to call a Shareholders' Meeting - this authority therefore enables directors to enter into transactions that require the issue of shares on the strength of an (pre-approved) authority granted by Shareholders. By allowing for this type of general authority, the law recognises the importance of efficiency in decision-making in the conduct of business and thus seeks to provide a framework for companies to achieve their goals in a balanced manner. This legal/ regulatory framework has the effect of balancing the need to protect Shareholder interests on the one hand, and the need for directors to efficiently make decisions and direct the affairs of the Company on the other hand, all aimed at the fulfillment of one objective - acting in the interests of the Company for the sustained benefit of all its stakeholders.

As a rule, the Board would use this authority with a great degree of circumspection and only if it comes to the conclusion that an issue of shares was the only course of action available to it in the circumstances, and doing so would be serving the best interests of the Company. The resolution has been tabled for Shareholder approval previously, and Shareholders approved it. Although it had been granted the authority, the Board did not use it as there was no necessity to do so.

## **22. Endorsement of Remuneration Policy**

The remuneration policy of the Company is set out in the Integrated Annual Report and will be presented for endorsement by Shareholders. The resolution is designed to ensure transparency in relation to the remuneration policies and practices of the Company. Shareholders also have an opportunity to test the adherence of such policies and practices to applicable laws, regulations, as well as acceptable governance standards and norms.

## **II (B) SPECIAL RESOLUTIONS**

(Amendments are proposed to be made to Special Resolutions 1, 4 and 5 respectively. The relevant special resolutions, as amended, are set out below, for due consideration by Shareholders)

### **23. Special Resolution Number 1**

#### **Repurchase of Shares**

**“RESOLVED THAT**, pursuant to the Memorandum of Incorporation (“Moi”), the Company and/or any of its subsidiaries is hereby authorised by way of a general approval to purchase or repurchase, as the case may be, and from time to time ordinary shares issued by the Company from any person,

upon such terms and conditions and in such number as the directors of the Company or subsidiary may determine, but in accordance with and subject to the provisions of the MoI, the Companies Act No. 71 of 2008 (“the Act”), and the Listings Requirements of the JSE Limited, provided that:

- the general authority granted to the directors shall be valid only until the Company’s next annual general meeting and shall not extend beyond 15 (fifteen) months from the date of this Special Resolution Number 1;
- any general purchase by the Company of its ordinary shares in issue shall not in aggregate in any one financial year exceed **10% (ten percent)** of the Company’s issued ordinary share capital at the time that the authority is granted;
- no acquisition may be made at a price more than 10% (ten percent) above the weighted average of the market value of the ordinary share for the 5 (five) business days immediately preceding the date of such acquisition;
- the repurchase of the ordinary shares are effected through the order book operated by JSE trading system and done without any prior understanding or arrangement between the Company and the counter party (reported trades are prohibited);
- the Company may only appoint one agent at any point in time to effect any repurchase(s) on the Company’s behalf;
- the number of shares purchased by subsidiaries of the Company shall not exceed 10% (ten percent) in the aggregate of the number of issued shares in the Company at the relevant times;
- the repurchase of shares by the Company and/or any of its subsidiaries may not be effected during a prohibited period as defined in the Listings Requirements unless the Company has in place a repurchase programme where the dates and quantities of securities to be traded during the period are fixed, i.e. not subject to variation, and full details of the programme have been disclosed in an announcement over SENS prior to the commencement of the prohibited period;
- a resolution by the Board that it authorised the repurchase, that the Company and its subsidiaries have passed the solvency and liquidity test and that, since the test was performed, there have been no material changes to the financial position of the Telkom group;
- the general authority may be varied or revoked by Special Resolution of the Shareholders prior to the next annual general meeting of the Company; and
- should the Company and/or any subsidiary cumulatively repurchase and/or acquire, as the case may be, redeem or cancel 3% (three percent) of the initial number of the Company’s ordinary shares in terms of this general authority and for each 3% (three percent) in aggregate of the initial number of that class repurchased and/or acquired, as the case may be, thereafter in terms of this general authority, an announcement shall be made in terms of the Listings Requirements.

Any decision by the Directors, after considering the effect of a repurchase, of up to **10% (ten percent)** of the Company’s issued ordinary shares, to use the general authority to repurchase

shares of the Company, will be taken with regard to the prevailing market conditions and other factors and provided that, after such repurchase, the Directors are of the opinion that:

- the Company and/or any of its subsidiaries will be able, in the ordinary course of business, to pay its debts for a period of 12 (twelve) months after the date of this notice of the Annual General Meeting;
- the assets of the Company and its subsidiaries will be in excess of the liabilities of the Company and its subsidiaries for a period of 12 (twelve) months after the date of this notice of Annual General Meeting, which assets and liabilities have been valued in accordance with the accounting policies used in the audited financial statements of the group for the year ended 31 March 2013;
- the share capital and reserves of the Company and its subsidiaries will be adequate for the ordinary business purposes for a period of 12 (twelve) months after the date of this notice of Annual General Meeting; and
- the working capital of the Company and its subsidiaries are considered adequate for ordinary business purposes for a period of 12 (twelve) months after the date of this notice of Annual General Meeting.

The Board will, through the Company's sponsor, provide the JSE with the necessary report on the adequacy of the working capital of the Company and its subsidiaries in terms of the Listings Requirements prior to the commencement of any share repurchase in terms of Special Resolution Number 1.

In terms of the Companies Act and the Listings Requirements, this resolution will require the support of at least 75% (seventy five) of the votes exercised by equity securities holders present or represented by proxy at the Annual General Meeting, for it to be approved.

### **Explanatory Notes In Respect of Special Resolution Number 1**

It is not uncommon for listed companies to seek this authority from Shareholders as it enables companies to repurchase shares issued by the Company should the market conditions and price justify such action. The Board would, in accordance with the directors' fiduciary responsibilities, only use this authority if they were of the opinion that it would be in the best interests of the Company to do so. The JSE imposes a number of restrictions in order to protect the interests of Shareholders where such an authority is granted to directors. These conditions include that repurchases have to be done on the open market and the price paid cannot be excessive.

The general authority is required in order to enable the Board to implement the proposed share scheme. On the passing of the resolution proposing the share scheme, the Company will be required to perform certain settlement obligations to employees participating in the scheme. The settlement obligations entail

that the Company has to deliver shares to qualifying scheme participants and these shares have to be sourced from either the market or have to be issued. If sourced from the market (as this authority would allow), there will be no dilutive effect to the holdings of Shareholders. It is therefore prudent that the authority be obtained as it will set the Company on a course towards achieving its stated objective namely: turning the business around for the benefit of all its stakeholders through the use of an appropriate instrument for providing incentives employees. Once again, the proposed resolution is designed to balance the needs of the Company's key stakeholders (employees and Shareholders) within allowable parameters and acceptable governance norms.

The Board is proposing that the authority be limited to 10% of the issued share capital of the Company, which would fall far below the limits allowed under the Listings Requirements of the JSE for general repurchases of shares.

This resolution has also served at the Company's previous AGMs, and was tabled at last year's AGM and approved by Shareholders. The Board did not use the authority as the intended purpose for proposing the resolution was defeated at that same AGM, i.e. the approval of a share scheme.

#### **24. Special Resolution Number 2**

As regards special resolution number 2 it is noted that an issue "for cash" is a concept under the JSE Listings Requirements and is by definition an issue of equity securities in consideration for cash, or in the extinction of a liability, obligation or commitment, restraint or settlement of expenses. In practice, issues for cash would most commonly occur where shares are subscribed for in exchange for a cash consideration. The maximum discount at which the equity securities may be issued is 10% of their weighted average traded price over the preceding 30 business days and the number of equity securities that may be issued in any one financial year is capped at 15% of the Company's equity securities of that class in issue. The Board has, however, voluntarily imposed a 5% limit on this authority.

Again, the Board does not currently foresee that it would use the authority, but, in the event that the need to do so arises, it would not have to incur the cost and attendant delay of convening a General Meeting to seek authority to issue shares for cash, should it be granted the contemplated authority by the passing of special resolution number 2 at the annual general meeting, subject to all the applicable restrictions to the authority.

The authority to issue shares under this special resolution is independent of the share scheme.

## **25. Special Resolution Number 3**

The resolution relating to the remuneration of non- executive directors is proposed in accordance with applicable statutory/ regulatory requirements. It should be noted that the directors are recommending a 0% increase in non-executive directors' remuneration, in acknowledgement of the need for cost containment given the challenging circumstances facing the Company.

## **26. Special Resolution Number 4**

### **Financial Assistance to Subsidiaries and Other Related Entities and Inter-related Entities and to Directors and Prescribed Officers and Other Persons who may participate in the Employee Forfeitable Share Plan ("Employee FSP")**

**RESOLVED THAT**, to the extent required by the Companies Act, the Board may, subject to compliance with the requirements of the Memorandum of Incorporation, the Companies Act and the Listings Requirements, each as presently constituted and as amended from time to time, authorise the Company to provide direct or indirect financial assistance by way of loan, guarantee, the provision of security or otherwise, to:-

1. any of its present or future subsidiaries and/or any other company or entity that is or becomes related or inter-related to the Company for any purpose or in connection with any matter, including, but not limited to, the subscription of any option, or any securities issued or to be issued by the Company or a related or inter-related company or entity, or for the purchase of any securities of the company or a related or inter-related company or entity;
2. any of the present or future directors or prescribed officers of the Company or of a related or inter-related company or entity, or to any other person who is or may be a participant in the Company's Employee FSP proposed to be adopted at the Annual General Meeting, for the purpose of, or in connection with, the subscription for any securities, issued or to be issued by the Company, or for the purchase of any securities of the Company, where such financial assistance is provided in terms of such scheme;
3. any of its present or future directors for the purpose of, or in connection with, the subscription for any option, or any securities, issued or to be issued by the Company, or for the purchase of any securities of the Company, where such financial assistance is provided to enable a director to subscribe for or acquire shares to meet the Company's share ownership requirements for top management, such authority to continue until the forthcoming annual general meeting of the Company.

## **Explanatory Notes In Relation To The Amended Special Resolution Number 4**

The Act contains two sections governing financial assistance by a company, namely –

- section 44, which applies to the provision by a company of financial assistance to any person, for the purpose of, or in connection with, the subscription of any option, or any securities, issued or to be issued by the company or a related or inter-related company, or for the purchase of any securities of the company or a related or inter-related company. It is derived from section 38 of the now repealed Companies Act, 61 of 1973 ("Old Act"), but differs in several respects; and
- section 45 applies to the provision by a company of financial assistance to various categories of recipients, which can broadly be classified as -
  - o the company's related or inter-related companies (e.g. its subsidiaries); and
  - o directors and prescribed officers of the company and/or its related or inter-related companies (e.g. its subsidiaries);
  - o any person related to any of the foregoing.

The section 45 financial assistance provision is a construction of the Act. The provision was inserted in the new Act to enhance the governance of companies by ensuring that shareholders have some 'say' over some of the affairs and/or governance processes of the company in which they are invested.

The purpose of the proposal is to allow the Board to have the ability to provide financial assistance, and to do so having complied with the requirements of the law. The granting of this authority will enable efficiency in decision-making, and will do away with the need for the Board to call a Shareholders' Meeting when it requires entering into certain transactions where financial assistance might be required. The Act contemplates the application of this kind of authority across a very broad range of situations, including financial assistance to subsidiaries, financial assistance to directors and/or prescribed officers, financial assistance to a Company's employees to facilitate participation in such Company's share scheme ( where such scheme does not enjoy the exemptions provided for under section 197 of the Act). The Act also allows for financial assistance to be provided to persons related to directors (and persons in such cases would include family members and companies associated with that particular director) with the approval from shareholders. The effect of this construction is that it allows for directors to provide financial assistance to vehicles intended to be used to facilitate estate planning, should shareholders consent thereto. The Board's proposal in relation to the approval of a resolution authorising directors to provide financial assistance, as currently set out in the Notice, is reflective of the broad nature of the powers contemplated in the Act, and in fact is based on the wording of the Act. The Board acknowledges that the proposed resolution as it stands would have a very broad application, which the Board does not

necessarily require for the purposes of delivering on its mandate. As such, the Board is proposing a modification (as set out above), which will ensure a more limited application of the authority. The intention is to arrive at a construction that will fit more appropriately with the intentions of the Board in relation to the authority.

The modified resolution will excise all references to "persons related to director" and is amended such that the end result is a resolution authorising directors to provide financial assistance to subsidiaries as well as to executive directors and prescribed officers (by way of loans). The resolution will be used for purposes of enabling the Board to provide financial assistance to the Company's subsidiaries in appropriate circumstances. It is apposite at this point to note that the Board will use this resolution for these purposes with the requisite degree of circumspection required of directors, and within acceptable governance norms and standards, with the aim being to enhance Shareholder value and acting in the best interests of the Company and its stakeholders.

The Board will also use the authority for the purpose of giving effect to its goal of providing incentives to all qualifying Telkom employees, through the implementation of a share scheme as will be proposed at the AGM (see item 27 below). For the avoidance of doubt, it should be noted that the share scheme for which this authority is required is the particular share scheme that the Board is proposing for approval at this AGM - there are no other share schemes in place, with the old share schemes having been terminated and duly wound down. The resolution is also modified such that it will only apply to the provision of financial assistance in respect of Telkom shares, and not those of related entities as would have been possible were the amendment not to be effected.

The Board will also be able to use the authority to provide loans to qualifying participants (under the LTI component of the scheme) who are required to meet share ownership requirements in the terms of the share scheme.

This resolution was proposed to Shareholders at the last AGM (2012) and was approved by Shareholders.

## **27. Special Resolution Number 5**

### **Adoption of the Telkom SA SOC Limited Employee FSP**

**RESOLVED THAT** the adoption by the Company of the Telkom SA SOC Limited Employee FSP ("Employee FSP"), a draft of which has been tabled at this Annual General Meeting and initialled by the Chairperson for purposes of identification, is hereby approved and that Directors are authorised to implement the Employee FSP in accordance with its terms.

Special resolution number 5 must, in terms of and for purposes of paragraph 14.1 of Schedule 14 to the Listings Requirements of the JSE Limited, be approved by a 75% majority of the votes exercised by Shareholders present or represented by proxy at this Annual General Meeting. Since this is the Company's threshold for special resolutions, the resolution is instead proposed as a special resolution.

### **Explanatory Notes In Relation To The Amended Special Resolution Number 5**

This special resolution relates to a proposal that Shareholders approve a share incentive scheme aimed at ensuring that employees are rewarded for contributing to the success of the turn-around strategy of the Company, thereby ensuring sustained performance improvements and enhancing value for the benefit of all stakeholders. The resolution seeks to ensure that rewards are linked to the achievement of the Company's performance targets as set out by the Board from time to time.

Hereunder is a fuller exposition of the philosophy and key principles which were pillars of the decision-making framework of the Board when agreeing a share scheme for the Company:

#### **A. Key Considerations**

In designing an appropriate share scheme for the Company, the guiding principle was that the Company is in turn-around mode and therefore requires a share scheme that will match the needs of Company ("fit for purpose") by channeling appropriate behavior among employees. The following key principles were taken into consideration by the Board, amongst others:

##### **i) Linking Rewards to Performance**

The scheme is designed to serve as a mechanism that will allow the Company to achieve its goals through a structured and deliberate focus of employee time and efforts on activities that will ensure delivery of the Company's performance targets and strategic goals. The performance targets applicable to each employee will be appropriate to the level of such employee, as determined in relation to factors such as:

- (a) the employee's skills and experience,
- (b) the decision-making mandate given to that employee as a consequence of his/ her role in the Company,
- (c) the performance indicators applicable to such employee (including stretched targets where appropriate),

- (d) the degree to which an employee determines the future direction of the Company as evidenced by their level of involvement in the strategy formulation and/or implementation processes of the Company etc.

- ii) Differentiation

The proposed scheme would also need to include an element of differentiation - this was one of the key principles in the design of the share scheme, aimed at rewarding employees for performance on a differentiated basis. Thus high performers will be appropriately rewarded to reflect their level of performance and to encourage such behaviour on a sustained basis, and the same principle will apply (in reverse) in respect of poor performers.

- iii) Equity and Fairness

The scheme and the reward structures embedded therein would need to be underpinned by a rigorous performance management system which will be structured to ensure that there is certainty in regard to the rules of the scheme, including certainty on the application of such rules. In addition, the performance management system would need to ensure a structured approach to performance management, with clear objectives and attendant rewards etc. – all aimed at ensuring equitable and fair treatment of employees.

- iv) Alignment of Interests

The share scheme seeks to align the interests of employees with those of Shareholders by e.g. introducing ownership conditions on certain levels of employees (who participate in LTI component of the scheme). Such a proviso would enable Management to demonstrate their long-term commitment to the Company and their belief in the strategic vision and direction of the Company by having 'skin in the game'. In addition, the proposed scheme envisages that stringent performance conditions will be imposed, with e.g. strict vesting conditions in respect of shares awarded in terms of the LTI - vesting of such shares will subject to meeting performance targets on a sustained basis.

## **B. Salient Features Of The Proposed Share Scheme**

- i) LTI and ESOP

The proposed share scheme comprises two components, a Long Term Incentive Scheme (“LTI”) designed to provide incentives to qualifying employees who are in levels M0 to M3, as well as an

Employee Share Ownership Scheme (“ESOP”) designed to provide incentives to qualifying employees in levels M4/S4 and below.

ii) The Shares

The total number of shares in issue by Telkom is approximately 520 million, and the number of shares which can be utilised for purposes of giving effect to the Company's obligations under the share scheme is a maximum of **5%** of the shares in issue or approximately **26 million shares**. The shares can be sourced through different methods, including an issue of shares, a share purchase or through the utilisation of treasury shares (where available). The required shares can therefore be sourced from a pool made up of issue, purchase or treasury shares, but the Board’s preferred method would be the repurchase route. An issue of shares for the purposes of the share scheme would be used as an absolute last resort, and with great circumspection. The allocation of the 26 million shares will be spread over a **six** year period.

iii) How Will The Allocations Work?

In terms of the rules of the share scheme, the basis upon which the grants will be made will take account of the employee’s base pay and grade. The number of shares to be comprised in the grant shall be as determined by the Remuneration Committee, in its discretion.

The shares will be available to all the employees of Telkom who are eligible to participate in the LTI and ESOP schemes respectively. The shares available for the scheme are **5%** of the Company’s issued share capital, translating to approximately **26 million** shares. The allocation proposed for the inaugural year shall be as illustrated in the table below:

<b>1st Allocation based on 5% Share Capital</b>			
<b>Grade</b>	<b>Number of Shares</b>	<b>Percentage allocation</b>	<b>Rand Value @ R21.97 Share Price</b>
Exco	1 198 058	0.70	26 321 334
M2	805 569	0.47	17 698 351
M3	1 282 396	0.74	28 174 240
<b>LTIP Total</b>	<b>3 286 023</b>	<b>1.91</b>	<b>72 193 925</b>

ESOP	5 327 816	3.09	117 052 118
<b>Grand Total</b>	<b>8 613 839</b>	<b>5.00</b>	<b>189 246 043</b>

The awards under the LTI component of the scheme vest over a 5 year period - commencing in year three (50%), 30% in year 4 and 20% in year 5 respectively, with additional awards to Executives vesting over 3 years (provided that the required performance conditions for additional awards are met). For the ESOP component of the share scheme, the vesting period will be 3 years. The shares will last for about 5 years only, and it might therefore be necessary in another three years or so for the Board to approach Shareholders with a recommendation to allocate more shares.

iv) Performance Targets

It is envisaged that the grants to vest under the share scheme will be calculated with reference to the financial performance of the Company in a given financial period. The financial performance of the Company is intended to be measured with reference to a combination of performance measures, with a view to ensuring both optimal Company performance as well as appropriate risk-adjusted returns for Shareholders. These performance measures include:

(a) Total Shareholder Return ("TSR")

40% is dependent on the generating returns for Shareholders that meet Shareholder expectations - to achieve minimum vesting the compounded return to Shareholders (over the vesting period) must exceed the Risk Free Interest Rate plus 2% and to achieve full vesting the compounded return must be greater than the Risk Free Interest rate plus 6%. This means Shareholders must receive an annual return of approximately 14%.

(b) Net Promoter Score

30% is dependent on a significant improvement in the Net Promoter Score assigned by customers (i.e. customer service must improve dramatically). To support its performance improvement objectives, the Company intends to embark on an aggressive focus to improve customer experience by enhancing the quality of its products as well as the levels of service to customers. There is evidence to suggest a correlation between a Company's improvement in its financial performance and the level to which customers who are happy with the service and quality of that Company and its products/services are willing to recommend the Company to family and friends.

Whether the Company actually achieves the required levels of customer satisfaction will be measured and tested against accepted industry benchmarks. As a service driven company, Telkom will use the Net Promoter Score ("NPS") as a tool to measure its performance in respect of customer happiness with its

quality and service. The NPS will be conducted and verified independently to ensure robustness and credibility.

(c) Free Cash Flow Performance Indicator

30% is dependent on Telkom generating operational free cash flow commensurate with the Shareholder Returns depicted above.

In F2013 the group generated Cash from operating activities of R7474m (before dividends to Telkom Shareholders) and invested in Capex approximately R5519m - thus generating Operational Free Cash Flow of R1955m. In F2012 the equivalent amount was cR1620.

The Board anticipates (in our post-new strategy) a modest growth (of between 5-7%) in EBITDA over the next five years and the next three years EBITDA is projected to be R7.6bn, R8.4bn and R9.2bn. respectively. This means that EBITDA of R25.2bn will be delivered over three years. A sensible target of between 8 and 9bn of Operational Free Cash Flow is expected for the three year performance period.

**C. Other Important Considerations**

It should be noted that, in practice the 26 million shares that are set aside for the scheme are not likely to all vest. The shares will not vest if the required performance targets are not achieved on a sustained basis.

Given the challenges facing the Company and the requirement for the Board to deliver on the expectations of Shareholders, it is imperative for the Board to have the necessary tools and resources to enable it to carry out its turnaround plan. In order to be able to properly discharge its fiduciary responsibilities towards the Company, the Board requires to have the ability to introduce and implement (sometimes bold) interventions, as deemed appropriate, in the furtherance of the of its mandate and the preservation and enhancement of value for Shareholders. This share scheme represents one such bold intervention, and the Board is confident that if implemented, it will go a long way towards enabling the success of the turn-around strategy.

**D. Telkom's Classification As A State-Owned Company ("SOC")**

Whilst Telkom is classified as an SOC, it has special characteristics which require a different incentivisation approach in comparison to other SOCs. For instance, Telkom operates within a highly competitive industry insofar as skills are concerns, in particular the availability of appropriate skills.

Because of the specialist and technical nature of the telecommunications industry, and the limited pool of appropriate skills, Telkom has to offer as competitive a remuneration package to employees as those offered by its competitors in this space. Currently Telkom's competitors in this space offer very lucrative packages to their employees (including attractive incentive schemes) , so Telkom has to offer a similarly attractive proposition if it is to succeed in its bid to deliver on its turn-around strategy and deliver the performance improvements that Shareholders require. To do this, Telkom needs a package that will be sufficiently attractive and substantially similar to the incentive packages offered by its competitors to persuade a prospective employee to join the Company as well as convince high performers currently in the employ of the Company to stay in the Company and be a part of the sea change that the Company is embarking on.

The success of the Company's turn-around journey is dependent on the Company having the right resources to effect the turn-around. Appropriate skills, fit for the purpose, are one of the key resources required if the turn-around such as the one that Management and the Board are envisaging for the Company is to have any chance of success - in fact it would be safe to say that the journey to success is predicated on having the right skills for the challenge at hand, supported by an appropriate performance culture.

It is instructive to note that some SOCs, such as Transnet, Eskom, SAA , even though not listed entities, do have similar forms of in-house long term incentive schemes, typically referred to as 'deferred cash awards'. The objectives of these deferred schemes are similar to what the Telkom Board wants to achieve with the proposed share scheme. The deferred cash awards applicable under these schemes are locked in for a period of 3 to 4 years to align the interests of top leadership with those of their respective Shareholders and are paid out upon certain performance conditions being met. The deferred cash awards in the above- mentioned SOCs are approved by their respective Boards and Shareholders.

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## **28. Special Resolutions Numbers 6 - 8**

These resolutions seek to bring the Company's Mol in line with the Listings Requirements of the JSE as well as the Act in relation to the rotation of directors. Insofar as director rotation is concerned, the Listings Requirements make reference only to non-executive directors. The Act provides for a framework in terms of which the *ex officio* directors of a Company (e.g. the CEO and CFO) do not have to retire, provided that the Company's Mol expressly makes reference to *ex officio* directors in accordance with the applicable provisions of the Act. South Africa is widely recognised for its advanced system of corporate governance, with appropriate checks and balances to ensure performance by executive directors. The legal

framework relating to the retirement of directors reflects an established practised which enables the correct balance of power and constructive tension between executive and non-executive directors on the Board. It is also believed that there could potentially be adverse consequences in subjecting executive directors to retirement by rotation, which may include the following:

- the power balance between executive and non-executive directors, which is important to secure effective governance, may be disturbed and the situation may consequently arise where the executive is perceived to be primarily accountable to the Shareholders or certain of them;
- Shareholders would not have all the insights that the board has into the management of the Company as they are not privy to all the relevant information that would enable the board to judge the performance of the executive directors in terms of fulfilling their executive functions and their role as directors;
- the loss of a key employees contrary to the formal succession plan put in place by the board, could lead to all sorts of problems relating to succession.

The board therefore believes that the succession of executive directors should rather be dealt with by the board of a Company through processes other than retirement by rotation.

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*This memorandum does not replace the Notice of AGM published by the Company on the 29<sup>th</sup> August 2013, nor does it constitute legal advice. The memorandum is intended only to provide clarity and context on the Board's proposals.*