

CESA COMMENT ON THE 'REVISED B-BBE CODES OF GOOD PRACTICE' – VERSION 3

1 INTRODUCTION

CESA wishes to comment on the Generic "Revised BBBEE Code of Good Practice" as the common elements of the Revised Codes will probably carry through to the Construction Charter, under which CESA and its member firms function.

CESA fully supports the aim of the "Revised BBBEE Codes of Good Practice (Codes)" as indicated by Minister Davies who said that BEE remained an imperative in South Africa not only as a social or political imperative but as an economic imperative as well and that the control of companies should be reflective of the demographics of the country.

Within its sphere of influence and more specifically CESA supports the following aims:

- The development and empowerment of black engineers
- The development of EMEs and QSEs in terms of consulting engineering firms
- The elimination of "fronting" and "tenderneership"

2 REVISED GENERIC CODE FRAMEWORK

2.1 Minister Rob Davies' Press Release:

One of new things being proposed in the revised Codes was the introduction of minimum requirements in the following control elements:

- Ownership
- Skills Development
- Enterprise and Supplier Development

Qualifying small enterprises (QSEs) are required to comply with two of the elements (including Ownership which is compulsory), while large entities would need to comply with all priority elements

Firms have to achieve minimum of 40% in the priority elements (threshold elements)

- or face dropping two levels for large firms > R50 million turnover
- or face dropping one level for qualifying small entity (QSE), R10 million \geq \leq R50 million that do not achieve the minimum scores for the Skills Development & Enterprise & Supplier Development priority elements

2.2 Classification of Measured Entities

| Entity classification | Current Limits | Revised Limits |
|-------------------------------|-------------------------------------|--------------------------------------|
| Exempted Micro Entity (EME) | EME < R5 million | EME < R10 million |
| Qualifying Small Entity (QSE) | R5 million \leq QSE < R35 million | R10 million \leq QSE < R50 million |
| Large Entity (LE) | LE \leq R35 million | LE \leq R50 million |

2.3 Revised Generic Scorecard

| Current Generic Scorecard | | | Revised Generic Scorecard | | |
|----------------------------|------------|------|---------------------------|------------|------|
| Control Element | Weigh-ting | Code | Control Element | Weigh-ting | Code |
| 1 Ownership | 20 | 100 | 1 Ownership | 25 | 100 |
| 2 Management Control | 10 | 200 | 2 Management Control | 15 | 200 |
| 3 Employment Equity | 15 | 300 | | | |
| 4 Skills Development | 15 | 400 | 3 Skills Development | 20 | 300 |
| 5 Preferential Procurement | 20 | 500 | | | |

| | | | | | |
|-------------------------------------------------|------------|-----|------------------------------------------------|------------|-----|
| 6 Enterprise Development | 15 | 600 | 4 Enterprise & Supplier Development | 40 | 400 |
| 7 Socio Economic Development Initiatives | 5 | 700 | 5 Socio Economic Development | 5 | 500 |
| Total | 100 | | | 105 | |

The seven elements within the current generic scorecard have been reduced to five as shown above; with which all companies must comply other than the exempted micro enterprises (EMEs).

2.4 Revised BBBEE status/contributor levels

| BBBEE Status | Existing Qualification | Revised Qualification | BBBEE Recognition Level |
|---------------------------|-------------------------------|------------------------------|--------------------------------|
| Level One Contributor | = 100 points | ≥ 100 ≤ 105 points | 135% |
| Level Two Contributor | ≥ 85 < 100 points | ≥ 95 < 100 points | 125% |
| Level Three Contributor | ≥ 75 < 85 points | ≥ 90 < 95 points | 110% |
| Level Four Contributor | ≥ 65 < 75 points | ≥ 80 < 90 points | 100% |
| Level Five Contributor | ≥ 55 < 65 points | ≥ 75 < 80 points | 80% |
| Level Six Contributor | ≥ 45 < 55 points | ≥ 70 < 75 points | 60% |
| Level Seven Contributor | ≥ 40 < 45 points | ≥ 55 < 70 points | 50% |
| Level Eight Contributor | ≥ 30 < 40 points | ≥ 40 < 55 points | 10% |
| Non-compliant Contributor | < 30 points | < 40 points | 0% |

2.5 Revised BBBEE status/contributor levels for EMEs

| Benchmark | Revised BBBEE Status |
|-------------------------------------|------------------------------|
| 100% Black-owned companies | Level One Contributor (EME) |
| More than 50% Black-owned companies | Level Two Contributor (EME) |
| White-owned companies | Level Four Contributor (EME) |

3 COMMENTS ON GENERIC CODE CHANGES & IMPLICATIONS FOR CONSULTING ENGINEERING SECTOR

3.1 General comment

| No | Comment |
|----|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1 | The objective of aligning the BEE Codes with the key priorities of the Government is supported. |
| 2 | The lack of clarity as to what the status of the Construction Charter will be, given the revised codes, is of concern. |
| 3 | The revised codes subject the Generic and QSE entities to the same five elements, but only the rules for the generic scorecard were published, whereas the scorecard for QSE entities was not published. |
| 4 | <p>To a large extent the B-BBEE scorecard is often irrelevant where CESA members bid for projects advertised by local government institutions and semi-state organizations.</p> <p>Firstly, the bid documents are usually poorly prepared and the scope of works equally poorly described such that true competitive bidding, where firms compete to offer the same service, is not possible. This is witnessed by the wide range of prices regularly seen on such poorly prepared bids. For example, just last week bids for a local project ranged from R550 000 to R3 450 000.</p> <p>Secondly, disregard of the PPPFA by the majority of local authorities makes a mockery of the bid process. Witness the current debacle with Tenders 27/2011/-12 and 28/2011-12 of the Ehlanzeni District Municipality.</p> <p>Bid prices are also frequently not made available at bid openings nor is it possible to establish bid awards. CESA is currently investigating a case where a bid was awarded at R1.2M while a member firm's was some R450 000.</p> |

3.1 Code Series 000 – Application of the Codes

| No | Reference | Comment |
|----|---------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1 | | <p>The impact of the Revised Generic BBEE is substantial and consideration should be given to phasing in the changes to prevent massive disruption/ business failure in the construction/infrastructure delivery sector.</p> <p>The following impact assessment by a medium-sized CESA member firm is provided as a basis for this comment.</p> <p>“Currently we are a Level 4 Contributor at 67 points. New scoring will probably result in a score of 50 points which now is a Level 8 Contributor. Thus by maintaining our current state will reduce our B-BEE recognition from 100% to 10%?”</p> |
| 2 | <p>Para 4, para 4.3 & 4.4, page 6 (referenced to Government Gazette, 5 October 2012)</p> | <p>The revised Contributor Levels allocated to exempted entities (< R10 million) viz</p> <ul style="list-style-type: none"> • Level 1 for 100 % black-owned companies • Level 2 for more than 50% black-owned companies • Level 4 for white-owned companies <p>are considered too high; as the exempted entities have little to gain by addressing the other Control Elements (besides Ownership). Even 100% black-owned companies should be required to invest in 'Skills Development' and 'Enterprise & Supplier development'.</p> <p>Hence it is recommended that the following Contributor Levels be allocated to exempted entities:</p> <ul style="list-style-type: none"> • Level 2 for 100 % black-owned companies • Level 3 for more than 50% black-owned companies • Level 5 for white-owned companies |
| 3 | Para 4, para 4.6, page 6 | The fact that exempted entities are exempted from detailed verification will result in fronting which even further undermines the objectives of the BEE Act. |
| 4 | Para 4, para 4.6.1, page 7 | Exempting 95% of all businesses (< R10 million) in SA from the BEE codes will not only exclude millions of black people and their families from the BEE codes, but also undermines the objectives of the BEE Act. |
| 5 | Para 9, page 11 | It is of concern that the revised Generic Code focuses on Black people and separates out Coloured and Indian people into sub-categories as if they were not equally disadvantaged in the past. This implies racism. |

3.2 Code Series 100 – The Ownership Scorecard

| No | Reference | Comment |
|----|-------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1 | Para 2, Table, page 13 | Include trusts where employees are the beneficiaries as part of designated points and not only ESOP's, BBO schemes and co-ops, as many entities govern the ownership of employees via normal trusts laws. |
| 2 | Para 2, Table, page 13 | For new entrants the focus must be on NEW and not on a threshold. This will focus ownership deals on those black people who do not have any equity yet and not on those who already have less than R50m turnover |
| 3 | Para 3, page 19 (upper table) | Please clarify “D for the purposes of the exclusion principle” and explain why the value of the measurable portion (actual shares minus mandated exclusions multiplied by value of shares) is used and not actual value. |
| 4 | | The compliance target for voting rights is now 25% + 1 vote. This is understood to mean that if a firm has 25% voting rights in the hands of black people, an additional vote from a black person is required to meet the Compliance Target. In a large organisation with many shareholders this may not be significant but in a small firm this may well be significant. |

3.3 Code Series 200 – Management Control Element

| No | Reference | Comment |
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| 1 | Para 2, para 2.1, page 22 | The compliance targets for Black Senior, Middle and Junior Management (43 – 68% over 5 years and 60 – 80% over the following 5 years) are unrealistically high; there are insufficient experienced black candidates in the workplace |
| 2 | Para 2, para 2.1, page 22 | <p>The compliance target for Black employees in the professional, experienced, specialists and mid-management measurement category is unrealistically high; it means that 3 of every 4 engineers in an entity is expected to be black. These compliance targets are simply unachievable.</p> <p>Awarding full points for compliance on a demographically representative basis presupposes that all races are equally qualified, experienced and competent on a demographically representative basis as well, however as we all know this is, unfortunately, a completely false assumption (at the Construction Industry Transformation Summit held on 23 November 2012, the Council for the Built Environment CEO stated that the total number of Black BEPs (Built environment Professionals) currently stands at 10% whereas the number for White BEPs currently stands at 80%).</p> <p>In practice it is found that many such qualified blacks see far greater rewards for themselves to open their own firms rather than join and remain with an established firm.</p> <p>It is CESA members' experience that many students and newly qualified black people are keen to join an established firm to gain experience but it is very difficult to retain them. This makes it a challenge to find suitable candidates to place in management positions. The medium term compliance targets have remained constant but there is a disproportionately large increase in the short term compliance target. These targets are considered to be unattainable in firm of small-medium size.</p> |
| 3 | Point 2.4 in Table, page 23 | It seems as if the measurement for black women under Middle Management was omitted |
| 4 | Para 2.2, page 23 and C page 25 - 26 | Provide clarity on the formula mentioned in point 2.2, page 23 and C page 25 to 26 especially the targets for race sub groups. |
| 5 | Para 4.3 & 4.4, page 23 | Provide a clear definition for Top Management versus Senior Management. |
| 6 | Para 4.3, page 23 | The exclusion of junior management could result in white employees being favoured above black employees and that the actual % black people in junior management position could be reduced over time. This will also impact negatively on black females in senior and middle management positions where there are currently few black females in junior management. The pipeline for middle and senior management is junior management and if a company has currently few black female in junior management it will surely limit the career opportunities for black females. It is recommended that points be allocated for black females in junior management positions to feed the management pipeline with black females. |

3.4 Code Series 300 – Skills Development Element

| No | Reference | Comment |
|----|------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1 | | Employment Equity element has fallen away completely and Skills Development, which is directed more at rewarding expenditure on programmes, now carries more weight. Experience has shown that valuable, lasting capability is better attained by work experience gained in a functional, quality environment than a “mechanical” learning programme. The incentive to be rewarded by employing black people and giving them the opportunity to “learn by doing” is now removed by the abandoning of the Employment Equity element. |
| 2 | Para 2.1.1, page 27 | Broaden the scope of training in 2.1.1 to black people and not just black employees. This will promote sponsoring scholarships and bursaries for non-employees. |
| 3 | Para 2.1.2.1 & 2.1.2.2, page | Does 2.1.2.1 include unemployed people and as such double counting is allowed for 2.1.2.1 and 2.1.2.2? |
| 4 | Para 2.2, page 28 | Clarify point 2.2 with targets for race sub groups. As commented previously, CESA does not agree with race sub-groups |
| 5 | Para 6, page 31 | Define what is meant by institutions. |
| 6 | Upper Table, page 32 | Cat B refers to internships but the definition describes normal education at a tertiary institution where practical is required to achieve the degree. The concept internship used here is confusing. |
| 7 | Lower Table, page 32 | Cat C should include learnerships and apprenticeships |
| 8 | Table, page 33 | Cat D is again confusing because it duplicates learnerships already awarded in Cat C. |
| 9 | | The following classification is recommended: <ul style="list-style-type: none"> • Cat A Theoretical education at a tertiary education institute such as universities and colleges. • Cat B Theoretical education at a tertiary institute with a practical work experience before the degree or diploma is awarded. • Cat C Internships after obtaining a degree to register as a professional person. • Cat D Learnerships and apprenticeships • Cat E Skills programmes for which unit credits are awarded |
| 10 | Para 7, page 35 | Provide examples of how the formula in point 7 is applied |

3.5 Code Series 400 – Enterprise and Supplier Development Element

| No | Reference | Comment |
|----|----------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1 | | <p>Enterprise and Supplier Development is now awarded 40 points whereas previously Preferential Procurement (20) and Enterprise Development (10) totalled 30 points. This equals the total points for Ownership and Management Control.</p> <p>A consulting engineering practice is the “end producer” of a service and its main operational expense is the payment of salaries. Relatively little of its operational expense is taken up through the procurement of goods and services from qualifying enterprises.</p> <p>In addition consulting engineers are not “management agents” who farm out their operations to qualifying enterprises for the purpose of gaining BBBEE points. The need to maintain control over the quality of their services and retaining liability for their designs, generally demands that they do the work themselves rather than sub-contract it to other firms. Obtaining recognition for Enterprise Development is, in our members’ experience, frequently extremely difficult. Validating such expenditure requires substantiating documents from the qualifying enterprise which is typically found to be unobtainable as the enterprises could not produce these documents.</p> |
| 2 | Table, page 39 | <p>To only allow suppliers who have the value Adding status is to exclude on average 70% of all suppliers as they do not qualify as Value added suppliers in terms of the definition. Companies with an annual turnover of R1m do not have to register for VAT and as such also do not qualify as a value adding supplier as the prerequisite in terms of the definition is to be registered for VAT. The introduction of the Value Adding concept is to promote the use of local content and to encourage job creation. As a result of the fact that this concept will exclude many suppliers from being recognized for procurement points AND to be selected as beneficiaries of supplier development. If job creation is to be awarded rather provide points for creating new permanent jobs for black people and do so under the Management Control element. Remember BEE compliance is driven by the supply chain and to exclude all Non Value Adding suppliers from this pressure will defeat the purpose of procurement driven BEE compliance.</p> <p>Agree that must include Supplier with Enterprise but should not complicate matters by adding the “Value-Added Suppliers”.</p> |
| 3 | Para 2.4, page 40 | What is the rule for calculating score for Enterprise and Supplier development when an entity makes a loss |
| 4 | Para 3.5.4, page 42 | What is the difference between black owned and black women owned businesses in point 3.5.4? I assume black women owned means more than 30% black women owned and black owned means more than 50% black owned. |
| 5 | Para 3.5.10, page 42 | What is meant with “date of measurement”? it is assumed to be the end of the financial year measured. |
| 6 | Para 9 & 10, pages 46 - 49 | It would prevent confusion if all the examples mentioned in points 9 and 10 were classified in terms of the Benefit Factor Matrix. |
| 7 | | The description of shorter payment periods is confusing. Please clarify “percentage of invoiced amount” under column Contribution amount. |
| 8 | Para 10, page 46 | Statement 400 amended by insertion of list after paragraph 8. The list has an error ie “9.1.5 The following is a non-exhaustive list” should read “9.2 The following is a non-exhaustive list” as it is a sub-heading. The points following 9.2 should read 9.2.1, 9.2.2, 9.2.3 etc |

Note: Value-Adding suppliers = means an Entity registered as a vendor under the Value-Added Tax (VAT) of 1991, whose Net Profit Before Tax summed with its Total Labour Cost exceeds 25% of the value of its Total Revenue.

3.6 Code Series 500 – Socio-Economic Development (ESD) Element

| No | Reference | Comment |
|----|---------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1 | Para 2.2, page 55 | What is the rule for calculating score for SED when an entity makes a loss? |
| 2 | Para 3.2.2, page 56 | The full value of Socio-Economic Development contributions made to beneficiaries is recognisable if at least 100%, previously 75%, of the value directly benefits black people - This is grossly unfair. For instance a multi-racial home for mentally disabled people eg The Avril Elizabeth Home, will be severely disadvantaged by such a regulation. Should the white children be discharged, many of them are orphans?? Why is the proportion of the races not based on demographic representation as in the rest of the regulations?? |

CESA comment is based on the following documents:

1. Engineering News commentary on Minister Rob Davies press release on the "Revised BBBEE Codes of Good Practice"; dated 4 October 2012
2. Government Gazette No 35754, 5 October 2012; General Notice issued by Minister of Trade and Industry, Rob Davies, entitled "Revised BBBEE Codes of Good Practice & BBBEE Tech Assistance Guidelines"