SABPP FACT SHEET

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THE REVISED BROAD-BASED BLACK ECONOMIC EMPOWERMENT CODES OF GOOD PRACTICE

1. Introduction

The revised Broad-Based Black Economic Empowerment codes of good practice ("the codes") contain some significant amendments that have far reaching implications for any company seeking to measure its contributions to Broad Based Black Economic Empowerment (B-BBEE). How do these amendments affect your company, and should you continue to pursue certification of your B-BBEE status?

Unlike five years ago when the broad-based scorecard was promulgated, today all companies are affected by the measurement of their contribution to B-BBEE. Through the Preferential Procurement Policy Framework Act (PPPFA) and the B-BBEE Act, the Minister of Trade and Industry and his agents have power to withhold or grant almost any economic benefit based on the consideration of an entity's B-BBEE status.

So to those companies who have made strides in advancing their B-BBEE status to access economic benefits such as points on government tenders, the proposed amendments to the codes of good practice, which outline new targets and indicators for measurement of B-BBEE, represent a need to thoroughly understand the new requirements and consider their strategy and tactics.

HR practitioners are often tasked with coordination of the B-BBEE scorecards in general, and are always involved in the alignment of employment equity and skills development activities with scorecard requirements. It is vital therefore that this aspect of regulation is well understood by HR practitioners.

This Fact Sheet summarises some key amendments which may be enacted following publication of the proposed amendments in October 2014 for the 60 day public commentary period. None of

the amendments have yet been implemented. The Fact Sheet is based on the "Demystifying the DTI and BBBEE Workshop" run by the Learning and Growth Development Initiative Committee of the SABPP late in 2014.

2. What is Black Economic Empowerment?

It is an integrated and coherent socio-economic process to contribute to the economic transformation of South Africa and bring about both significant increases in the number of black people that manage, own and control the country's economy as well as significant decreases in income inequalities.

3. What is Broad-Based Black Economic Empowerment?

This involves the economic empowerment of all black people including women, workers, youth, people with disabilities and people living in rural areas through diverse but integrated socio-economic strategies that include but are not limited to:

1. increasing the number of black people skilled to manage, own and control enterprises and productive assets;
2. facilitating ownership and management of enterprises and productive assets by communities, workers, cooperatives and other collective enterprises;
3. human resource and skills development;
4. achieving equitable representation in all occupational categories and levels in the workforce;
5. preferential procurement;
6. investment in enterprises that are owned and managed by black people.

4. The legislative framework

The Broad Based Black Economic Empowerment Act of 2003 is the founding legislation for the promotion of black economic empowerment and empowers the Minister to:

- Issue codes of good practice
- Publish transformation charters
- Establish the Black Economic Empowerment Advisory Council.

5. What is the function of the codes?

The codes are issued in terms of Section 9 of the Act. They function to promote the objectives of the Act, which are to:

- transform South Africa's economy to allow meaningful participation by black people;
- substantially change the racial profile of companies' owners, managers and skilled professionals;

- increase the ownership and management of companies by black women, communities, workers, cooperatives and others, and help them access more economic opportunities;
- promote investment that leads to broad-based and meaningful participation in the economy by black people;
- help rural and local communities access economic opportunities; and
- promote access to finance for black economic empowerment.

6. Scorecard thresholds

The codes contain structured scorecards for:

- large companies (annual turnover greater than R35m – Generic);
- small companies (annual turnover between R5m and R35m – QSE);
- companies with annual turnover below R5m and start-up companies are exempt from compliance and receive exemption certificates (EME's).

The thresholds for these categories have been amended as follows:

Category	Annual turnover threshold	
	Old	**New**
EME's	R5 000 000	R10 000 000
QSE's	R35 000 000	R50 000 000
Generic	Above R35 000 0000	Above R50 000 000

More companies are therefore exempt from compliance, and the burden of compliance is shifted towards larger companies.

The QSE scorecard, together with the specialised scorecard, statement for developing sector codes, statement on recognition of equity equivalent and statement on sale of assets was gazetted for 60 days public comment on 10 October 2014 to 9 December 2014.

7. Scorecard elements

There were previously seven elements against which targets where measured:

- ownership
- management control
- employment equity
- skills development
- preferential procurement
- enterprise development
- socio-economic development.

These seven elements have been consolidated into five elements by combining management control and employment equity and combining enterprise development and preferential procurement into a category now labelled enterprise and supplier development.

The targets and weightings in these elements change as follows:

Old		**New**	
Element	**Weighting**	**Element**	**Weighting**
Ownership	20	Ownership	25
Management control	10	Management control	15
Employment equity	15		
Skills development	15	Skills development	20
Preferential procurement	20	Enterprise and supplier development	40
Enterprise development	15		
Socio-economic development	5	Socio-economic development	5

8. Priority elements and penalties for not meeting these

Three of the five elements have been designated priority elements - these are ownership, skills development and enterprise and supplier development.

Failure to achieve a sub-minimum of 40% of the targets for any of these priority elements will result in a penalty being applied to the scorecard.

The penalty is a drop of one level down, therefore an entity that achieved a level four before the penalty, will drop to a level five if the penalty is applied.

9. Adjusted B-BBEE recognition levels

B-BBEE recognition levels are measured by points on the scorecard out of 100, and bands of points are allocated into contribution levels, each with a commensurate procurement recognition level.

The number of points at which a company becomes a level four has increased from 65 to 80 points in a 'bracket creep' adjustment (similar to the concept used in tax bracket adjustments). The other levels are affected as follows:

B-BBEE contributor status	Qualification	B-BBEE recognition level
Level one	More than or equal to 100 points on the generic scorecard	135%
Level two	More than or equal to 95 points, but less than 100 points on the generic scorecard	125%
Level three	More than or equal to 90 points, but less than 95 points on the generic scorecard	110%
Level four	More than or equal to 80 points, but less than 90 points on the generic scorecard	100%
Level five	More than or equal to 75 points, but less than 80 points on the generic scorecard	80%
Level six	More than or equal to 70 points, but less than 75 points on the generic scorecard	60%
Level seven	More than or equal to 55 points, but less than 70 points on the generic scorecard	50%
Level eight	More than or equal to 40 points, but less than 55 points on the generic scorecard	10%
Non-compliant	More than 40 points on the generic scorecard	0%

The resulting changes will result in instant reduction of B-BBEE levels upon introduction.

The amendments confer a benefit on black-owned companies in that EME's and start-ups that are 50% or more black-owned and who previously automatically qualified for a level three status now qualify for a level two if at least 51% black-owned and a level one if 100% black owned.

10. Ownership

The overall weighting for ownership has increased from 20 to 25 points, increasing the relative importance of ownership on the scorecard.

The weight attributed to voting rights and economic interest has been equalised. Calculations previously allocated towards bonus points, now form part of the requirements. This means that failure to achieve 40% subminimum on net value will now impact on the overall status.

The points attributed for ownership fulfilment once a share is free of all third party rights has been removed, and added to the overall net value requirement measuring the repayment period of debt on black shares. The sub-minimum penalty requirement is applicable to achieving 40% of the net value targets.

The modified flow-through principle may now not be used in conjunction with exclusion principle. This means that a company that is excluding mandated investments from its scorecard may not apply the modified flow through principle elsewhere.

11. Management control and employment equity

The use of Adjusted Recognition for Gender calculations has been replaced with separate targets for black people and black females. The commensurate penalty on middle managers resulting from the gender adjustment has been removed, while the board of directors and senior management retain the need to have male and female balance. Targets for junior management have been retained.

Although not expressly listed in the target, there is a requirement that each target be broken down into sub-targets determined by the ‘overall demographic representation of black people’. More specifically, “for scoring purposes, the targets should be further broken down into specific criteria according to the different race sub groups within the definition of black in accordance with the employment equity act requirements on equitable representation and weighted accordingly.” This requirement is stated in the Codes that targets for senior management, middle management and junior management will have to be based on overall demographic representation of black people as defined in the Employment Equity Act and Commission on Employment Equity Report.

There are now separate employment targets for Africans, Coloureds, and Indians. The situation as regards acceptable interpretations of the Employment Equity Act in relation to targets is developing with current case law and this could pose a problem in relation to the codes and scorecard measurements.

Previously, a company was required to prove that it had submitted its Employment Equity returns in compliance with the Employment Equity Act, as a pre-requisite for receiving any employment equity recognition. This requirement is now extended by requiring the data submitted in the return to be used in the calculation for the scorecard at the time of measurement.

This creates a timing variance in which a company that has improved its demographic representation will only obtain recognition in the following period, after it has submitted its employment equity return.

12. Skills Development

The target for skills development expenditure is derived from the salaries and wages paid (the leviable amount as calculated in terms of the Skills Development Levy Act), and historically equates to approximately 3% for the period. The target has increased to 6% of the leviable amount.

The training programmes for which skills development expenditure may be counted include category F (informal training outside of the workplace by way of workshops and conferences) and G (informal training that takes place at the workplace) programmes, but these together cannot represent more than 15% of the total skills development expenditure for scorecard purposes. Training spend must also be apportioned between the overall demographic representation of black people, as per employment equity.

In addition, “a measured entity must achieve a minimum of 40% of the target set out in the skills development scorecard in order to avoid discounting of its overall scorecard.”

Other changes include:

- The adjusted recognition for gender adjustments has been removed;
- Overall weighting for this element has increased from 15 to 20 points;
- 5 bonus points have been added for achieving a labour absorption target. So if black people trained on learnerships, internships and apprenticeships should progress toward formal employment, the measured entity may recognise that as a bonus point.

13. Enterprise and supplier development

This element combines preferential procurement and enterprise development in a single element and introduced a third criteria referred to as “supplier development” with a combined weighting for all three of 40 points. The focus of this elements has shifted from random development of black owned enterprises and purchasing from other B-BBEE contributors to deliberate meaningful development of suppliers that have a high labour component.

13.1. “Empowering suppliers”

Previously, to qualify for procurement recognition, a company had to purchase from suppliers that had a B-BBEE certificate. There is now a requirement that only suppliers designated as “empowering suppliers” may be counted.

To be recognised as an empowering supplier an entity must meet the following criteria:

(a) At least 25% of cost of sales, excluding labour cost and depreciation, must be procured from local producers or local suppliers in SA. (For the service industry labour costs are included but capped to 15 %.)
(b) Job creation – 50% of jobs created are for Black people provided that the number of Black employees since the immediate prior verified B-BBEE measurement is maintained.
(c) At least 25% of the transformation of raw material/beneficiation should include local manufacturing, production and/or assembly, and/or packaging.
(d) Skills transfer - spend at least 12 days per annum of productive time deployed in assisting Black EMEs and QSEs beneficiaries to increase their operational or financial capacity.

Clearly, this provision affects most organisations as they are usually both suppliers to and customers of other organisations.

13.2. Target and sub-minimum

The target has increased from 70% to 80%, while the eligible suppliers have been reduced to include only empowering suppliers. The overall weight attributed to procurement was 20, and is now 25. The number of points attributed to QSE's and black owned companies has increased from 8 to 17.

An entity must achieve a minimum of 40% for preferential procurement, supplier development and enterprise development, in order to avoid overall discounting of its scorecard.

13.3. Enterprise development and supplier development

Ten points will be allocated to expenditure on supplier development of 2% of net profit after tax (NPAT) (note again that there are now targeted beneficiaries within the supply chain, and no longer recognition for random contributions to qualifying black-owned companies). Five points are allocated for achieving expenditure of 1% of NPAT for enterprise development contributions.

There is also a requirement to develop an enterprise and supplier development plan for qualifying beneficiaries which includes clear objectives, priority interventions, key performance indicators and a concise implementation plan with clearly articulated milestones in the case of imported goods and service. This is to support localisation. The plan will be monitored when verification is done.

A multiplier of recognition is provided for companies that grant three year contracts to first time suppliers. There is clearly an intention to stimulate enterprises by providing opportunities to sell, and assistance through supplier development. Further multipliers are granted enterprises that are not supplier development beneficiaries.

13.4. Imports

Limitations are placed on what imports may be counted as part of procurement costs. Details of these are in the codes.

13.5. Expedited payment periods

A limitation has been applied to contributions made in the form of shorter payment periods to suppliers. The invoice value is multiplied by 15% (an approximation of the cost of capital) and then multiplied by the applicable benefit percentage based on the number of days between issuing an invoice and receiving payment.

13.6. Annual measurement of development

Supplier development, enterprise and socio-economic development is now measured annually and may no longer be measured cumulatively.

14.Future changes

The previous 10 year term of application of the codes has been removed, with no new limitation imposed. As per section 9 (7) of the Amended B-BBEE Act the Codes remain until amended, replaced or repealed.

15.Conclusion

The amendments, as they stand in the version published for comment, represent a significant tightening up of the codes and the measurement system for B-BBEE. All organisations will need to conduct an impact assessment together with their verification agency.

The amendments offer the opportunity to take a more strategic approach to economic transformation by each organisation so that B-BBEE becomes more than a points-shopping exercise.

THIS FACT SHEET HAS BEEN PREPARED BY NAREN VASSAN, HEAD OF LEARNING AND QUALITY ASSURANCE AT THE SABPP. THE CONTENT HAS BEEN UPDATED AND VERIFIED BY:
MS. LINDIWE MANDONSELA – DEPUTY DIRECTOR ADVISORY COUNCIL - THE DEPARTMENT OF TRADE INDUSTRY; SATISH ROOPA – JFK CONSULTING; LOUIS MCLAREN – DIRECTOR - BLACK SEED INVESTMENTS; WERNER DYER – MANAGING DIRECTOR -EMPOWERMENT ACADEMY.

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