



Commissioner's Guide & Other Tales

12 April 2017



Amidst the turbulence and distractions of the past few days including an earthquake and the legalized private use of cannabis, a couple of documents have come across my desk that deserve a review.

BEE Commissioner's Practice Guide No 1 of 2017

The BEE Commissioner has issued a [Practice Guide](#) (see attachment). The key paragraph is number 14 which prevents EME's or QSE's who achieve their 51% or 100% black owned status via modified flow-through from benefiting from enhanced recognition to a BEE Level 2 or 1 respectively.

Our reading of this Guide is that proof of BEE status for EMEs or QSEs must now be achieved as follows:-

- Affidavit: EME for a BEE level 4 or a Level 2 or 1 enhanced recognition for 51% or 100% Direct Black ownership.
- Affidavit: QSE with 51% or 100% Direct Black ownership (modified flow-through not used) for BEE Level 2 or 1 enhanced recognition.
- BEE Certificate: for QSEs where modified flow-through has been used for black ownership or where direct black ownership using normal flow-through is less than 51%.

Questions that spring to mind are:

- Is black ownership achieved via modified flow-through for a EME/QSE still considered as a 51% black owned business for procurement recognition or as an ED or SD beneficiary?
- How do Verification Agents test whether modified flow through has or has not been applied when investigating affidavits for procurement measurement?
- Is this a retrospective application or is it ongoing from yesterday's date. Or put another way, do people who already have an affidavit dated prior to yesterday and having used MFT still use their affidavit or are they already fronting?

Radical Socio-Economic Transformation

A brief by Charles Collocott for the Helen Suzman Foundation titled *"Radical Socio-Economic Transformation, State Procurement and Broad-Based Black Economic Empowerment"* is a useful read, to find the whole document go to: [Draft Workplace Based](#)

[Learning Programmes.](#)

The 1st few pages covers the codes and you can skip that part but read on from the section entitled *"Some negative effects of B-BBEE and general misconceptions"*

Here are his conclusions:

"The Government's BEE-policies have had a positive effect in increasing black participation in the economy, and also in an indirect manner, by increasing an awareness that a much more meaningful black participation at all levels of the economy is necessary and needs to be supported. Whilst it is also accepted that the policies were put in place with the best of intentions, it is clear that many problematic consequences of the policies were not foreseen and the practical difficulty of implementing and monitoring them continues to be underestimated.

One of the major obstacles in this context is simply that many state entities lack the resources to deal with intricate policies of this nature. This is quite apart from other factors such as corruption, which seem to have become a widespread feature of state procurement. A lack of resources does not just imply inadequate departmental budgets, but the appropriate personnel and systems are often not available to execute complex projects.

Once again, the SASSA case provides the most extreme example in this context: SASSA's own advocate was forced to admit in the hearing at the Constitutional Court on 15 March 2017 that it had not been able to take over the payment of social grants itself (as it had undertaken to the Constitutional Court in November 2015) because it had been overly ambitious".

"In order for preferential procurement to increase black economic participation in a meaningful manner, the following steps are necessary:

- A review of B-BBEE is needed to mitigate its negative impacts and to make it simpler to implement and monitor;
- Government departments need to have adequate resources available to manage their procurement function (and quite apart from finance, the necessary personnel and systems

need to be at hand) and,

- Greater vigilance and accountability by Government and SOEs is required to combat irregular and fraudulent procurement.

Therefore, the presidential pronouncements on radical economic transformation being supported by Government's procurement policy may have some success in playing to the gallery, but the realization of such a policy is seriously threatened in practice if these minimum steps are not taken."

SA Mining Recovery to be Short-Lived

The Mining Review Africa – 3rd April reports on a BMI research document that concludes that the mining sector will continue to face headwinds from policy uncertainty regarding the passing of the draft mining charter. It forecasts that "the domestic mining industry will contract from US\$33.8 billion in 2017 to \$32.9 billion in 2021" despite a rise in iron ore and gold prices that have improved the outlook for major miners.

The implementation of the revised and aligned Mining Charter has been continuously delayed due to disagreements with the Chamber of Mines and the domestic mining industry over certain revised requirements. One of the biggest obstacles is the DMRs insistence that a mining company must fulfil the ownership requirement at all times and thus must make the necessary adjustments to ensure it abides by the participation target if ever it falls below the 26% threshold.

Charles Collocott In the Helen Susman report explains the predicament of the mines as follows (abbreviated):-

"The DMR proposed B-BBEE Mining Charter specifies that it will require stakeholders to achieve a minimum of 26% black ownership per mining right. It will also require this minimum black shareholding to be maintained, effectively terminating the "once empowered, always empowered" principle. Such is also the stance taken by the B-BBEE Commissioner in her latest newsletter. However, the question surrounding the validity or otherwise of the "once empowered, always empowered" principle has not yet been

resolved.

One problem confronting mining companies is that if their B-BBEE partners sell their shareholding to non-B-BBEE entities after the minimum prescribed lock-in period (assumed here to be 3 years), the owner of the mining right would have to find a new B-BBEE partner to once again achieve the required 26% black ownership level.

This process results in diluted shareholder equity as shown in a worst case scenario calculation as follows:

Let us assume a company has 100 shares: 74 non-BEE and 26 BEE. After holding them for 3 years, the BEE shareholder sells to a non-BEE shareholder. The company will then need to issue 35 new shares to another BEE investor to bring black ownership back to 26% (35 out of 135 shares).

If after another 3 years, the new BEE shareholder sells to yet another non-BEE shareholder, the company will have to issue 47 new shares to a BEE partner to achieve 26% black ownership (47 out of 182 shares). The company now has a total of 182 shares outstanding, with the original non-BEE shareholders holding 74 shares. Their ownership of the company has therefore been diluted to 40%, from the original 74%.

The problem of shareholder dilution applies to all business sectors and not just mining.

The prospect of shareholder dilution decreases the number of companies willing to bid for government procurement, thereby decreasing the level of competition within the process.

According to a report released by the Economist Corporate Network in late March 2017, an anonymous executive said that “My principals in North America are not going to approve of us essentially having to ‘give away’ equity to raise our B-BBEE rating. We would rather run the risk of losing business for now.”

BEE Verification

In the past few months the number of organisations able to issue BEE Certificates has dropped from more than 600 to under 60 yet there is currently no great bottleneck in obtaining a BEE Certificate. Verification Agents are busy but not impossibly booked out. One must presume that most larger companies are maintaining their BEE inertia but

that demand for BEE certificates by smaller business has fallen away significantly due to the use of affidavits and a general wait and see attitude. We have been saying for a while that the cost and complexity of the New BEE Codes is counterproductive to transformation and the current state-of-affairs in the verification industry seems to confirm this view.

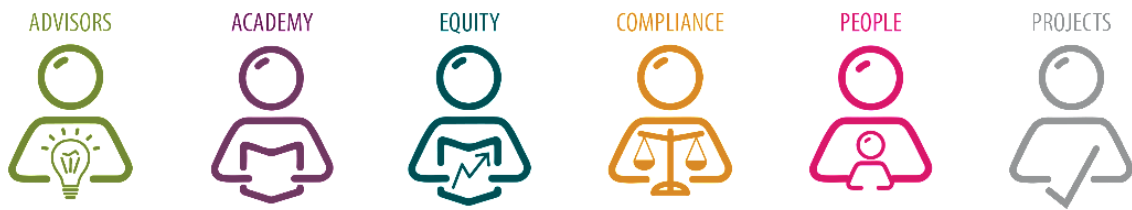
BEE – A Negative Factor for European Investors in SA

Business Day 28th February reported that satisfaction by European investors in SA has deteriorated significantly since 2012. This was the conclusion of the 2016 business climate survey conducted among 211 Europe-owned firms by the EU Chamber of Commerce and Industry of Southern Africa.

The volatility of the rand, government corruption and the cost of compliance with black economic empowerment (BEE) legislation were high on their list of concern. Policy changes, uncertainty and red tape around work permits were also cited as concerns, while perceptions about SA's transformation agenda were mostly negative.



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