

THE DTI'S GENERIC SCORECARD FOR BROAD-BASED BLACK ECONOMIC EMPOWERMENT

CONFIDENTIAL

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Contents of Document

	<u>Page</u>
1. Background to Black Economic Empowerment	3
2. High level summary of the DTI's BEE Codes of Good Practice	8
3. Contact details	21



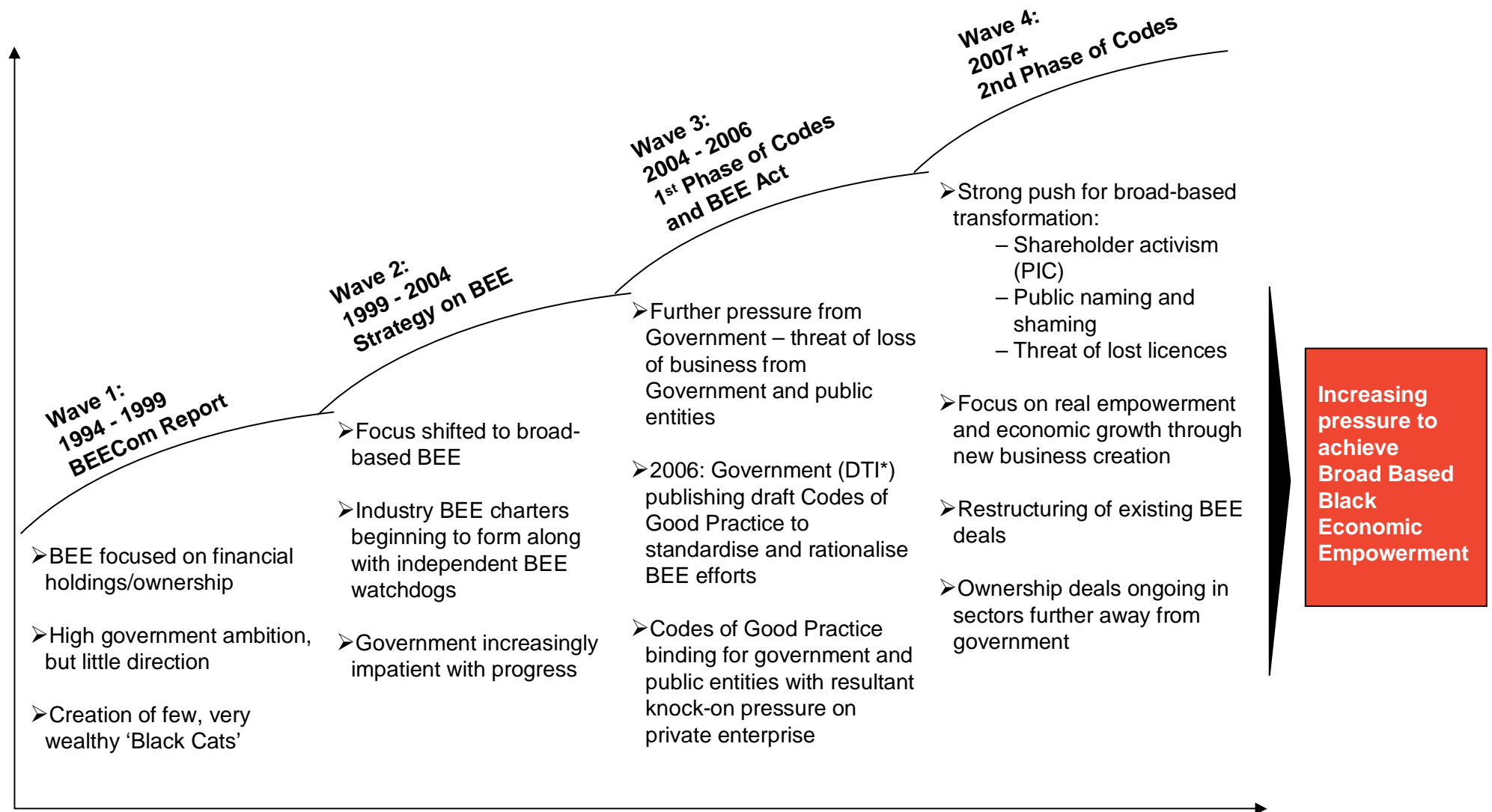
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2. BACKGROUND TO BLACK ECONOMIC EMPOWERMENT



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Developments in BEE



* Department of Trade and Industry

How is BEE governed

Attempt 1: Industry Charters

- Various industry Charters: 2003 – 2005, to govern each sector’s contribution to BEE
- Confusion in the market on cross-industry procurement and the rating of BEE suppliers due to different targets and rating systems
- Government publishes the Black Economic Empowerment Act which allows for the Department of Trade and Industry (“the DTI”) to publish “Codes of Good Practice” on BEE

Attempt 2: Codes of Good Practice

- Publishing of Codes:
 - **Draft** Codes (Phase 1): 1 November 2005
 - **Draft** Codes (Phase 2): 20 December 2005
 - Gazetting of **Final Codes** in **February 2007**
 - Codes will apply for 10 years – renewable indefinitely
- For Industry Charters to over-ride DTI’s Codes requires Charters be published as legislation under **Section 9 of the BEE Act**
- Before such publication can take place, will require “substantial alignment” with the DTI’s Codes
- Charters not meeting this requirement are published under **Section 12** of the BEE Act and are for information purposes only and **not binding** on Government or the Sector
- The Codes recommend a **Balanced Scorecard** to measure BEE performance

**The DTI’s Codes of Good Practice regulate BEE,
unless an Industry Charter has been published and promulgated into law**

Summary of the Generic Scorecard as laid out in the Codes of Good Practice

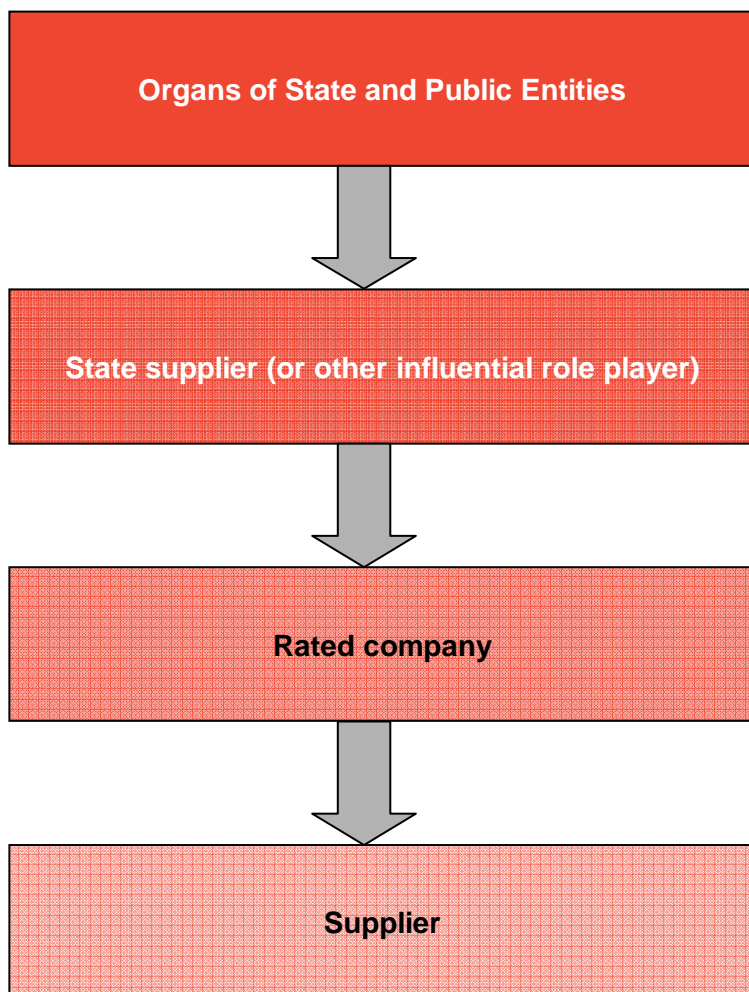
DTI BEE scorecard		Weighting	Regulatory objective
Direct empowerment	Equity Ownership	20%	<ul style="list-style-type: none"> ➤ To encourage the sharing of equity and voting rights with black people and black women ➤ To encourage senior black decision making at Executive Board and Senior Top management levels ➤ To encourage companies to identify, recruit and develop black people at professional, middle and lower management positions as well as skilled worker levels ➤ To promote spending on in-service training and learning programmes for employees ➤ Measures the extent to which enterprises procure from companies that are BEE compliant. Also encourages spend on Small and Micro-enterprises ➤ Encourages the creation or expansion of (particularly black) small, medium enterprises ➤ Encourages initiatives intended to directly provide black people who are natural persons with means of generating income for themselves
	Management	10%	
Employment equity	Employment Equity	15%	
	Skills Development	15%	
Indirect empowerment	Preferential Procurement	20%	
	Enterprise Development	15%	
	Socio-economic Development	5%	

- Performance against this scorecard is assessed on an annual basis
- Accredited Rating Agents will perform the rating

Source: DTI Codes of Good Practice

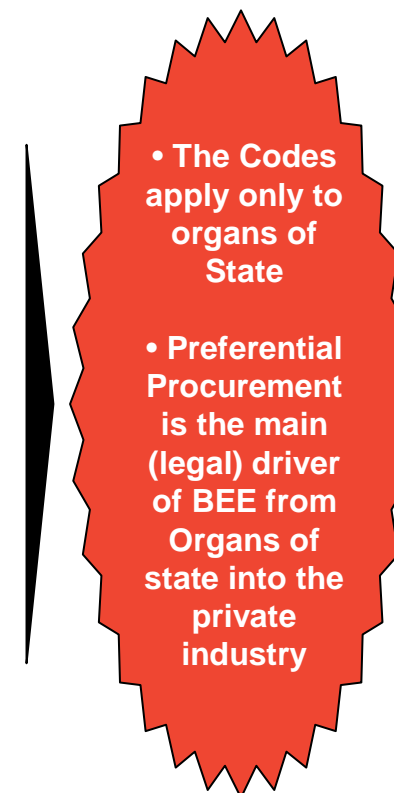
Application of the Codes of Good Practice

Supply chain:



Commentary

- The Codes “**apply to Organs of State and Public Entities**”, and only “**seek to provide guidance to private sector enterprise**”
- Government will only award a tender to the State supplier if he scores highly on the BEE scorecard
- The State Supplier tries to increase its “total score” (i.e. ALL the elements), so as to get the contract
- Preferential procurement (20%) is a key category
- State supplier wants the Rated Company to have high BEE score...
- ...which in turn Rated Company requires of its Suppliers

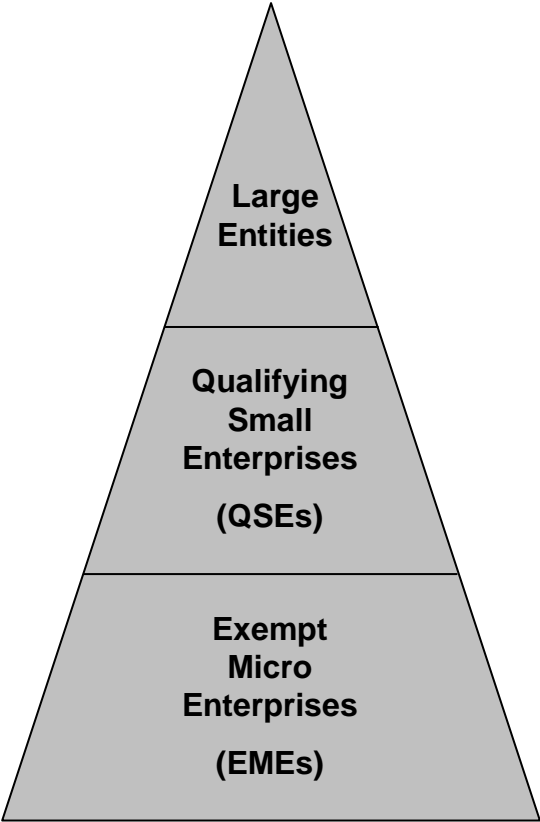


2. HIGH LEVEL SUMMARY OF THE CODES



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BEE applies to suppliers based on their company size

Company Size	Definition	Application of the Codes	Determining BEE % recognition
 <p>Large Entities</p>	<p>Revenue greater than R35m</p>	<p>Generic Scorecard or approved Sector Charter applies</p>	<p>Score on generic scorecard translates to Contribution level and associated BEE recognition %</p>
<p>Qualifying Small Enterprises (QSEs)</p>	<p>Revenue between R5m and R35m</p>	<p>Simplified and less onerous scorecard applies:</p> <ul style="list-style-type: none"> - Choice of 4 of 7 elements - All elements weigh 25% 	<p>Score on QSE scorecard translates to Contribution level and associated BEE recognition %</p>
<p>Exempt Micro Enterprises (EMEs)</p>	<p>Revenue less than R5m</p>	<p>Exempt from BEE</p>	<p>Automatically recognised as Level 4 contributors with 100% BEE recognition</p> <p>EMEs with black ownership > 50% are deemed to be Level 3 Contributors with 110% recognition</p>

Source: DTI Codes of Good Practice

Note: Identifying Qualifying Small Enterprises (QSEs) and Exempted Micro-Enterprises (EMEs) is not always as simple as it might appear, particularly when dealing with agency relationships

There are 3 options for scoring on the BEE Ownership element

Equity Equivalents

- This option removes the requirements for “foreign” multinationals to sell 25,1% of their local operations to a BEE party and replace their efforts with an “Equity Equivalents” contribution to an approved public programme

Sale of Assets

- This option entails disposing of a part of the business to a black company (i.e. with greater than 51% black ownership), with the target that the overall value in black hands is 25% of the combined entity value

Equity Sale

- This option is the standard option which entails the sale of typically 25% of the business to black shareholders – usually in a leveraged ‘buy-in’ manner guaranteed by the company or existing shareholders

• Ownership is the **most complex** area of the Codes and is **frequently misunderstood and incorrectly calculated**

• **Ensure** your corporate finance advisors are **experts** or have relationships with experts in BEE Ownership to ensure your deal is correctly structured **for sustainability and maximum scoring**

Code 100: Key Ownership principles

Principles:

- **Flow Through Principle:** The Flow through principle indicates that if ownership is held by a juristic person, the level of black entitlement will be calculated based on the effective black ownership by black people
- **Modified Flow Through Principle:** The modified flow-through principle allows that in a chain of ownership, one juristic company in the chain which is black majority owned, can be treated as if it were 100% owned by black people provided it is at least 51% black
- **Mandated Investments Principle:** Allows for the exclusion of shareholding by managed investments, government owners and s21 companies when determining BEE ownership targets
- **Equity Equivalents:** Multinationals can claim ownership points based on equity equivalent programmes
- **Continuing Consequences Principle:** Allows max. 40% of black ownership score to be made up of points retained after sale by previous BEE partner
- **Broad-based Ownership schemes:** Limits ownership by employee schemes to 40% of BEE ownership component, except under certain conditions
- **Employee Share Ownership Schemes (ESOPs):** Limits ownership by employee schemes to 40% of BEE ownership component, except under certain conditions
- **Indirect ownership:** Allows indirect black ownership through managed investments to be included up to a max. 40% of the total black ownership, or alternatively excluded up to a maximum of 40% under the Mandated Investments Principle
- **Private equity funds:** May be recognized as 100% Black in the ownership structure under certain conditions

Source: DTI Codes of Good Practice

Note that the definition of “black” is **African, Indian, Coloured and Chinese (mainland) South African individuals**

Code 100: Ownership requirements

Category	Indicator	Weighting points	10 Yr target
Voting rights	Exercisable Voting Rights in the hands of black people	3	25%+1 Vote
	Exercisable Voting Rights in the hands of black women	2	10%
Economic interest	Economic interest of black people in the Enterprise	4	25%
	Economic Interest of black women in the Enterprise	2	10%
	Economic Interest in the Enterprise of black designated groups and black participants in Employee Ownership Schemes (ESOPs), broad based ownership schemes and Co-operatives	1	2.5%
Realisation points	Ownership fulfilment	1	No restrictions
	Net Equity Value	7	% of tgt Yr1: 10% Yr 2: 20% Yr 3,4: 40% Yr 5,6: 60% Yr 7,8: 80% Yr 9,10:100%
Bonus points	Involvement in the ownership of the Enterprise of black new entrants	2	10%
	Involvement in the ownership of the Enterprise of black participants in ESOPs, broad-based schemes and co-operatives	1	10%

Requires that **equity instruments** (e.g. ordinary shares or share options) carry a corresponding **ability** for the **BEE shareholder to vote** on shareholder issues

Requires that **equity instruments** allow the holder **access to economic benefit** from holding the shares

In the case of **leveraged transactions** this indicator rewards the extent to which the value of the equity rises and the debt is paid down. This **penalises** overly **aggressive share pricing** or overly **onerous debt** conditions.

Deals **smaller than 25%** and those **applying MFT Principle** on voting rights and economic interest also **penalised**.

Bonus points are awarded if

- Entity has 25% direct black ownership (**applying flow through principle only**) AND
- Includes new entrants and broad-based groups in their ownership

Source: DTI Codes of Good Practice

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Code 200: Management and Control requirements

Key Principles:			
• Aligned with the Employment Equity act			
Category	Indicator	Weighting points	10 Yr target
Board participation	Exercisable Voting Rights of black Board members*	3	50%
	Black Executive Directors*	2	50%
Top management	Black Senior Top Management*	3	40%
	Black Other Top Management*	2	40%
Bonus points	Black Independent Non-Executive Board Members	1	40%

Notes:

- If a company does not distinguish between **senior management and top management**, senior management can be measured under Management and Control, but the targets which apply to senior management under Employment Equity must be used
- If a company does not distinguish between **senior top and other top management**, then top management is measurable as a single indicator with a weighting of 5 points
- If a company does not have any executive directors, only exercisable voting rights will be measured and the weighting will be increased to 5 points

* Using Gender Recognition Adjustment factor = $(\% \text{ black people}/2) + (\% \text{ black women limited to maximum 50\% of the target})$

Note that the definition of "black" is African, Indian, Coloured and Chinese (mainland) South African individuals

Source: DTI Codes of Good Practice

Code 300: Employment Equity requirements

Key Principles and issues:

- Aligned with the Employment Equity act
- Companies exempted from filing Employment Equity reports with the Department of Labour are not exempt from Code 300 unless they are classified as Exempted Micro Enterprises

Category	Indicator	Weighting points	5 Yr Target	10 Yr target
Employment Equity	Black employees in Senior Management as a percentage of all such employees*	5	43%	60%
	Black employees in Middle Management as a percentage of all such employees*	4	63%	75%
	Black employees in Junior Management as a percentage of all such employees*	4	68%	80%
	Black Disabled employees as a percentage of all employees*	2	2%	3%
Bonus Points	Bonus points for meeting or exceeding the EAP targets in each of the above categories (1 point per category)	3	87.5%	

Note:

- A sub-minimum applies to each indicator whereby any company which does not achieve at least 40% of each target in any year will receive 0 points for that indicator
- Current Black EAP target is 87.5% (i.e.. Gender recognition factor does not apply)

* Using Gender Recognition Adjustment factor = (% black people/2) + (% black women limited to maximum 50% of the target)

Note that the definition of “black” is African, Indian, Coloured and Chinese (mainland) South African individuals

Source: DTI Codes of Good Practice

Code 400: Skills Development requirements

Key Principles:			
<ul style="list-style-type: none"> • Aligned with National Skills Development Act , and National Skills Development Strategy • 3% target is over and above the 1% Skills development levy 			
Category	Indicator	Weighting points	10 Yr target
Skills Development	Adjusted Skills Development expenditure on training for black employees as a percentage of Leviaible amount*	6	3%
	Adjusted Skills Development expenditure on training for black employees with disabilities as a percentage of Leviaible amount*	3	0.3%
Learning programmes	Adjusted number of black employees participating in Learning Programmes as a percentage of total employees*	6	5%

Notes:

- **No points can be scored** unless companies comply with the Acts pertaining to skills development, register with applicable SETA, develop Workplace Skills Plan and **implement programmes developing Priority Skills for black employees**
- **Bursaries and scholarships for employees are encouraged but only recognised under certain conditions**
- **ABET Programmes** receive spend recognition at a **multiple of 1.25**
- Concept of a **Learnership programme** introduced to encouraging **industry working together with education institutions** to create **formally recognised training aligned with practical experience in industry**
- Skills development from **Uncertified Learning Programmes** or **work-based informal programmes** are **limited to 15%** of the total skills development expenditure

* Using Gender Recognition Adjustment factor = % black people/2 + % black women (maximum 50% of the target)

Note that the definition of “black” is African, Indian, Coloured and Chinese (mainland) South African individuals

Source: DTI Codes of Good Practice

Code 500: Preferential Procurement requirements

Key Principles:

- Includes all operational spend i.e. non labour-related or tax/levy spend e.g. COGS, SG&A, CAPEX etc.
- Includes capital expenditure, goods procured from monopolistic suppliers and from organs of state / public entities
- Excludes donations or investments in associates
- Excludes imported goods if:
 - Goods are capital goods for value-add production (provided there is no existing local production)
 - There is no local production of the imported goods **except if**:
 - The only difference between imported good/service is cost
 - The imported goods carry a brand different to locally produced brand
 - Unnecessary technical specs are applied which have no direct impact on value

Category	Indicator	Weighting points	5 Yr Target	10 Yr target
Preferential procurement	BEE Procurement Spend from all Suppliers based on the BEE Procurement Recognition Levels*	12	50%	70%
	BEE Procurement Spend from Qualifying Small Enterprises or Exempted Micro Enterprises based on the applicable BEE Procurement Recognition Levels*	3	10%	15%
	BEE Procurement Spend from any of the following suppliers*: <ul style="list-style-type: none"> ➤ Suppliers that are more than 50% black owners; or ➤ Suppliers that are more than 30% black women owned 	3 2	9% 6%	12% 8%

Note:

- Procurement from a company's **Enterprise Development initiatives** receive a **multiple of 1.2**
- A **multiple of 1.25** applies if an entity is a **'Value Adding Supplier'****
- **Black owned*** professional service providers** and entrepreneurs **complying with all elements of the Codes also qualify as value-adding**

Source: DTI Codes of Good Practice

* As a percentage of Total Measured Procurement Spend >25% of revenue

** Value adding supplier = (profit before tax + employee costs)

*** Black owned means > 50% economic interest and voting rights, not applying the MFT principle

Page 16 of 22

Code 600: Enterprise Development requirements

Key Principles:

Example Qualifying Contributions:

- Provision of seed capital
- Professional /consulting services
- Licensing/registration fees
- Industry specific levies
- IT services
- Payments made to 3rd parties to perform enterprise development on their behalf
- Preferential Credit facilities/Guarantees/ better payment terms
- Training/mentoring
- Enterprise development unit

Category	Indicator	Weighting points	10 Yr target
Enterprise Development	Average annual value of all Qualifying Contributions made by the Measured Entity measured from the commencement of this statement or the Inception Date to the date of measurement as a percentage of the target	15	3% of NPAT

Notes:

- **Small, 50% black-owned enterprises** are favoured, but **development of larger black owned companies** and any **entity with a BEE status of level 1 to 6** is also encouraged
- If company **does not make a profit** or the profit margin is < 25% of industry norm, **target is based on 'Indicative Profit Margin'**, which is the profit margin in the last year where the company's profit was ≥ 25% of industry norm
- **'Benefit Factor Matrix'** has been introduced and governs the **extent to which contributions are recognisable**

Code 700: Socio-economic Development requirements

Key Principles:

Aimed at natural black persons, communities where **at least 75% are natural black persons or rural infrastructure development**. For example:

- Rural development programmes
- Health, HIV/Aids programmes
- Education support
- Environment
- Arts & culture
- Sport
- Allows for average over 5 year period

Category	Indicator	Weighting points	10 Yr target
Socio-Economic Development	Average annual value of all Qualifying Contributions made by the Measured Entity measured from the commencement of this statement or the Inception Date to the date of measurement as a percentage of the target	5	1% of NPAT

Notes:

- If company **does not make a profit** or the profit margin is < 25% of industry norm, **target** is based on 'Indicative Profit Margin', which is the profit margin in the last year where the company's profit was ≥ 25% of industry norm
- A 'Benefit Factor Matrix' has been introduced and governs the **extent to which contributions are recognisable**

Qualifying Small Enterprises: Statement 801: Ownership

Overall Principles:

- Qualifying small enterprises with turnover between R5m and R35m can chose any 4 of the 7 elements to be rated on
- Each of the elements carries a weighting of 25%

Ownership	Indicator	Weighting Points	10 Yr target
Voting rights	Exercisable Voting Rights in the hands of black people	6	25%+1 Vote
Economic interest	Economic interest of black people in the Enterprise	9	25%
Realisation points	Ownership fulfilment	1	No restrictions
	Net Equity Value	9	Refer to formula in main codes
Bonus points	Involvement in the ownership of the Enterprise of black women	2	10%
	Involvement in the ownership of the Enterprise by black participants: <ul style="list-style-type: none"> ➤ In the employee Ownership Schemes ➤ Of Broad-based Ownership Schemes ➤ Co-operatives 	1	10%

Source: DTI Codes of Good Practice

Qualifying Small Enterprises: Statements 802-806: Remaining elements

Element	Indicator	Weighting Points	5 Yr Target	10 Yr target
Management control	Black representation at Top-Manager level	25	n/a	50.1%
	Black women representation as Top-Managers	2	n/a	25%
Employment Equity	Black employees of the Measured Entity who are Management as a percentage of all Management*	15	40%	60%
	Black employees of the Measured Entity as a percentage of all employees*	10	60%	70%
Skills Development	Adjusted Skills Development spend on training for black employees as a percentage of Leviable Amount	25	n/a	2%
Preferential Procurement	BEE Procurement Spend from all Suppliers based on the BEE Procurement Recognition Levels as a percentage of Total Measured Procurement Spend	25	40%	50%
Enterprise Development	Average annual value of all Qualifying Contributions made by the Measured Entity measured from the commencement of this statement or the Inception Date to the date of measurement as a percentage of the target	25	n/a	2% of NPAT
Social Development	Average annual value of all Qualifying Contributions made by the Measured Entity measured from the commencement of this statement or the Inception Date to the date of measurement as a percentage of the target	25	n/a	1% of NPAT

Source: DTI Codes of Good Practice

3. CONTACT DETAILS



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