

**WILL MORE REGULATION INCREASE PRIVATE SECTOR BBBEE PERFORMANCE?**

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**Background:**

Under pressure from the Black Business Working Group and the South African Government, the Department of Trade and Industry (DTI) initiated a study to undertake a baseline assessment of the state of Black Economic Empowerment in South Africa. To estimate the current performance of South African companies on BEE, Consulta undertook market research in April 2007 through interviewing over 1,700 companies across all sectors of the economy, with an even geographic spread. The study specifically excluded the Public Sector and the results were presented to the President of South Africa and the Presidential Black Business Working Group on 3 August 2007.

**Summary of BBBEE Baseline study: Poor performance all round**

The research highlighted that about **75% of South African businesses estimate** their BEE score to be less than 30 points i.e. they **are recognised as 0% contributors to BEE**. Clearly cause for concern.

The only element of the BEE scorecard that (on a weighted average basis) managed an **'average' performance** was the **Ownership** element (12/20). There was no interesting story to tell on the **Employment Equity** elements other than some very **mediocre performance** (3/10 for management, and around 6/15 for Skills Development and Employment Equity). Probably most confusing is the **poor performance** on the easiest to achieve **Socio-economic Development** (1/5). Finally, although perhaps unsurprisingly given the lack of accredited rating agencies, Indirect Empowerment through **Enterprise Development** (2/15) and **Preferential Procurement** (3/20) are the **worst performers**.

The research also asked qualitative questions of the 1,780 respondents on the perceived constraints and contributing factors to BEE and the top 3 constraints were as follows: "BEE benefits only a small minority of privileged black individuals"; "Skills Shortage"; "High turnover of black people in business". There was a perception that legislation such as the South African Constitution, the Broad-based BEE Act and the Employment Equity Act were the most important factors contributing to BEE.

**Key conclusions of baseline study: More regulation required**

Given the poor overall BBBEE performance noted above, it is perhaps understandable that there is high degree of frustration from black business. It is perhaps unfortunate though that

the research concluded that “push factors” were perceived to contribute the most to BBEE progress and therefore by extension, more regulation was required to improve this performance.

It is our belief, that the conclusion reached needs further debate and - given our view of consulting to industry in South Africa on BEE - a further interpretation of what the baseline study might mean for government policy makers and private sector alike.

### **Companies are already facing significant pressure to achieve BBEE**

There is no doubt that companies are already facing significant pressure to achieve BBEE. Research such as the above, press statements by prominent black business opinion leaders and other ‘name and shame’ campaigns place enormous pressure on companies to “do the right thing” and to prove to all their stakeholders (be they staff, customers, shareholders and government) that they are progressing the aims of BBEE.

In addition, legislation such as the Preferential Procurement Policy Framework Act is creating pressure from a natural market competition perspective as private sector tenders for government business (to be more empowered than their competitors). Additionally, pressure from the Minerals and Petroleum Development Act as an example is already filtering down to second and third tier suppliers in unrelated industries.

### **There is still significant confusion in the new regulatory environment**

Despite BEE-related legislation being many years either in use or in development, the Codes of Good Practice - which draw all these together - were only finalised in February 2007. These Codes describe a ‘balanced scorecard’ which measures a company’s contribution to BEE along 7 elements, with clear targets and not always so well tested techniques of measuring achievement against these targets. Many companies are still learning how to take their current initiatives and obtain a BEE score for these.

Unfortunately, the varying pieces of BEE related legislation are not aligned to the Codes as yet, but this was always going to take time. However, the misalignment of the procurement policies of Government and State Owned Enterprises (SOEs) with the Codes has been more damaging. As the major conduit for BEE into the private sector, inconsistency in this procurement interface sends confusing messages into the private sector. As a result, companies are spending unnecessary amounts of time addressing the procurement policies of the various with SOEs and Government, instead of putting together focussed and sizeable initiatives to achieve real transformation.

Additionally, many companies are still being side-tracked in debating scoring systems in industry charter processes which adds minimal value over and above the Codes of Good Practice. Corporates spanning several sectors find themselves having to understand numerous separate industry charter scoring systems as well as the Generic Codes. Given the research above, it strikes us that spending further time debating scoring systems is time wasted and their focus should be on determining what is to be done.

## **Negative publicity around BEE results in a mindset of ‘minimising risk’ and opting out rather than maximising return**

It is sometimes difficult to separate perception from reality, and public debate on this topic tends to be emotionally charged. Perceived skills shortages and high turnover of black people in business; perceived shifting goal posts as a result of inconsistent procurement policies and ongoing charter discussions; and perceived high cost to implement. All these perceptions – whether real or not - lead to inaction and an inability to move forward.

However, we have some startling opposites all operating in the same South Africa - from extremely positive examples such as Bidvest, ABSA and Edcon; to negative examples such as those constantly being named and shamed in the press. There are those that see the challenge as too daunting to achieve and therefore never begin the journey...and those that have seen a way to achieve transformation despite the hurdles they face.

Unfortunately, emotive and negative press debates seem not to resolve issues but create further emotion - tipping companies who are already feeling the pressure into the mindset of ‘minimising the risk’ in BEE instead of ‘maximising the returns’ from BEE.

With the above in mind, increasing the regulatory bite through penalties and increased targets (unless carefully done) is unlikely to have the effect intended and is more likely to result in attempts to minimise risk rather than maximise returns in BEE.

So how do we create the right environment for companies to undertake what is arguably one of the largest country-wide transformation programmes?

### **Recommendations**

Addressing each issue in reverse order:

#### **1) Creating a positive environment for transformation**

Global strategy consultancy McKinsey & Company in its Quarterly article on ‘Driving Radical Change’ highlights the need for clear and inspirational leadership in a Corporate transformation programme, and a National transformation programme is no different. In the absence of leadership indicating clear and consistent direction, fears and rumours abound and paralysis sets in.

In the case of BEE, this leadership was intended to come from a BEE Advisory Council made up of representation from all stakeholders – Government, business and labour.

In our view, this Council needs to address negative mindsets around BEE through both investigation into real issues around achieving BEE and through clear and positive communications, i.e.:

- **Understand real bottlenecks** through ongoing research, dialogue and debate such as this;
- **Address these bottlenecks** through combined government and private sector interventions to create successful BEE initiatives; and

- **Communicate success** in these initiatives and the build a common and compelling vision of a transformed future

## 2) Removing residual uncertainty

In our view three key issues need to be addressed here:

- **Increase clarity in interpretation of the Codes** through the continued publishing of Guidelines and the removal of unintended consequences in the new legislation;
- **Ensure consistent application** of the Codes through educating management and procurement officers at both public and private sector companies; and
- **Insist on standardised** methods of measuring BEE compliance by ensuring that industry charters align with the Codes

Continually addressing these uncertainties will build a strong platform for clear communications to reduce negative mindsets.

## 3) Maintaining pressure

While, in our view, increasing the regulatory bite could lead to inadvertently negative consequences, we recognise the success that regulatory pressure has had. We believe that the following actions will improve the performance of existing legislation:


- **Improve BBEE reporting and verification** through urgently finalising the mandate of the BEE verification industry, establishing a national database of rated companies and require rated BEE certification as part of company annual reporting;
- **Deepen the reach of the Codes** through continuing to link Industrial and Government policies e.g. MIDP and NIPP to BEE performance as per the Codes; continuing to link BEE performance as per the Codes to licensing requirements where procurement pressure is insufficient; and ensuring existing BEE-related legislation aligns with the Codes.

We believe that performing these activities will create a firm but fair environment for companies to undertake their own individual transformation programmes and achieve BEE performance as per the DTI's balanced scorecard over the next 5 years and improve that performance to achieve the 10 year targets thereafter.

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