

BEE AND PREFERENTIAL PROCUREMENT

Preferential Procurement is an important element in the Department of Trade and Industry's BEE Codes of Good Practice weighing the same as the Ownership element at 20 points out of 100. In most companies, payments to suppliers make up a large portion of the money they spend – running in many cases to greater than 60% of revenues. As a consequence, preferential procurement has potential to not only provide strong support to the aims of Black Economic Empowerment (BEE), but also local economic development in its broader sense.

The theory sounds simple: Government (either through government departments or through the State Owned Entities) requires good BEE credentials from any private sector entity supplying a product or service to Government or requiring a licence from Government. Private Sector companies measure their BEE performance using the 7-element balanced scorecard described in the Codes of Good Practice, which in turn requires them to ask the BEE status of their suppliers in order for them to score on the Preferential Procurement element. The Preferential Procurement element also requires companies to procure from BEE compliant Small and Micro enterprises, as well as Black and Black Women owned enterprises.

But that is where the theoretical simplicity ends and the practical challenges come to the fore.

Firstly, the administrative process behind preferential procurement is not to be scoffed at. Mid-sized JSE listed companies with annual turnover of around R10b can have supplier database in excess of 1,000 suppliers. The favoured approach is to focus on the top 20% of suppliers as they invariably provide 80% of supply. But getting formal BEE certificates from 200 suppliers on an annual basis is no easy task. The central database promised by the Department of Trade and Industry to house up to date BEE certificates still does not exist.

Secondly, the system of rating agencies has yet to be bedded down. A year after the Codes were finalised, we still do not have officially recognised rating agencies. In addition, Industry Charters are still aligning their scorecards to the Codes (hopefully to be complete by the end of this year), resulting in ongoing uncertainty as to which scorecard to use.

Simply getting a formal BEE scorecard for the top tier suppliers would be good, however, to get scoring on the Black and Black female ownership sub-element, requires almost all supplier information to be captured. One can not rely on only the top 20% of suppliers, as the larger suppliers tend to be publicly listed with less than 50% direct black or black female ownership meaning that the next tier in the supplier base also needs to be interrogated.

Finally, to get scoring on the Qualifying Small Enterprise or Exempt Micro Enterprise sub-element invariably means interacting with the full remainder of the supplier base.

A BEE Baseline study undertaken by Consulta Research for the Presidency in May 2007 highlights that SA companies are not performing particularly well on the Preferential Procurement element with an average of 3.3 points out of the 20 being achieved. Is this an indication that companies are doing nothing about preferential procurement?

No! Our experience has been that there is a correlation between companies scoring higher on this element and the amount of administrative effort they have put into collecting BEE scorecards, and has very little to do with whether their preferential procurement policies are in place and working. We expect preferential procurement scores to improve significantly when the rating agencies are finalised and a central scorecard database is created.

If we look at the preferential procurement discussion in the context of the standard procurement relationship, we need to consider to what extent a buyer can really impact on the BEE score of its suppliers. In an arms-length procurement relationship, even a large company buying a critical input from a smaller supplier might have limited ability to threaten the supplier with “give me good BEE credentials...or else”.

If the buyer has market power, there is still the business reality that procurement interactions have been refined over time and there is significant business risk to simply remove a major supplier of a critical input.

Even when it comes to smaller, less strategically important suppliers, a further issue that has raised its head is whether there really are any alternative BEE suppliers available (although this is becoming a cliché of late).

Nevertheless, this highlights that performance on the Preferential Procurement can be difficult to influence directly and clear thinking is needed to ensure that BEE strategy aligns with Procurement strategy (and vice versa).

So how do good corporate citizens achieve impact on BEE and local development without being bogged down in an endless paper chase?

Proactive companies **are** achieving great impact on BEE and local economic development through focussed efforts which take BEE and local development into account in their procurement decisions.

In the procurement and price-setting environment where tough negotiation is expected, companies find themselves unusually working **with** their key suppliers to find ways to improve BEE performance. While this can not be done for all suppliers, having an understanding of the BEE strategy (not just current scorecard) of one's key suppliers allows space for sizeable creative solutions. In the simplest form, this could be an understanding of the projected BEE score of the major supplier and how this will impact on your scorecard. More exciting would be

opportunities to outsource a non-core business function through a BEE compliant Joint Venture – achieving preferential procurement, enterprise development **and** business objectives.

These opportunities can not be brought to fruition purely through the procurement function. The “business development function” needs to be involved to support the creation of the new businesses and the growth of local suppliers through linking Enterprise Development initiatives with these procurement initiatives. This is not intended to be a hand-holding exercise, but one of opening up opportunities for bone fide supplier development to occur. Where these opportunities are more of a social nature, the appropriate links to development institutions are needed to provide ongoing support.


Larger companies are realising that Small and Micro Enterprises form an important part of their supply chain and usually provide innovative solutions to everyday problems which allow them to compete with even the larger suppliers. Companies realise that encouraging these smaller suppliers to grow in scale and in performance (usually through indirect financial support such as preferential payment terms) is the only way to make them sustainable and to support ongoing growth and access to innovation in their own company. Offering indirect financial support builds a positive incentive for Black owned Exempt Micro Enterprises and Qualifying small enterprises to self identify, saving procurement practitioners the effort of trying to contact smaller suppliers themselves.

Then there is the large number of middle tier suppliers who are not big enough to be worked with directly and are large enough not to need indirect financial support. Companies are interacting with these suppliers through offering supplier conferences to highlight expectations on both BEE and other business metrics. Education on BEE and dialogue to demystify the topic is usually sufficient to have significant and efficient impact with this level of company.

Finally where all else fails, company procurement policy should make it clear to suppliers who are unwilling to achieve acceptable BEE performance that time is running out and the company will be always be looking for alternative suppliers with better overall supplier performance (including BEE) to work with.

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