

Department of Law
School of Economics and Commercial Law
Gothenburg University, Sweden
Juridiska Institutionen
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Black Economic Empowerment

AN INTRODUCTION FOR NON-SOUTH AFRICAN BUSINESSES

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Tillämpade studier omfattande 20 högskolepoäng av:

Cecilia Engdahl
Hannele Hauki
lawmfs@yahoo.com

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Tutor:

Handledare:

Filip Bladini

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| | |
|--------------------------|---|
| <i>Mustapha Adams</i> | <i>Corporate Planning Statistics, Trade and Investment South Africa</i> |
| <i>Philip Armstrong</i> | <i>Lawyer, Edward Nathan & Friedland</i> |
| <i>Eva Bursvik</i> | <i>First Secretary (Development), Sida</i> |
| <i>Benno Engström</i> | <i>Telia Swedtel</i> |
| <i>Meryl Federl</i> | <i>BusinessMap</i> |
| <i>Miranda Feinstein</i> | <i>Lawyer, Edward Nathan & Friedland</i> |
| <i>Joaquim de Gama</i> | <i>University of Pretoria</i> |
| <i>Samuel Gumede</i> | <i>Lawyer, Werksmans Attorneys</i> |
| <i>Judith Hudson</i> | <i>Senior Research Co-ordinator, CDE</i> |
| <i>Per-Olof Jansson</i> | <i>Telia Swedtel</i> |
| <i>Hans Josefsson</i> | <i>Trade Commissioner, Swedish Trade Council</i> |
| <i>Hannu Leiponen</i> | <i>Trade Commissioner, FINPRO</i> |
| <i>Sabelo Macingwane</i> | <i>Chief Executive Officer, NAFCO</i> |
| <i>Don MacRobert</i> | <i>Lawyer, Edward Nathan & Friedland</i> |
| <i>Tiny Maisela</i> | <i>Group Human Resources Director, Murray & Roberts</i> |
| <i>Themba Mhlongo</i> | <i>Chief Director: Industry & Technology Strategy, DTI</i> |
| <i>Gabriel Msithini</i> | <i>Deputy Director: Policy, SACOB</i> |
| <i>Ravi Naidoo</i> | <i>Director, NALEDI</i> |
| <i>Vassi Naidoo</i> | <i>Chief Executive, Deloitte & Touche</i> |
| <i>Anda Ngani</i> | <i>Working Solutions International</i> |
| <i>Andile Nkuhlu</i> | <i>Chief Director: SOE Restructuring, Department of Public Enterprises</i> |
| <i>Ashraf Patel</i> | <i>ICT Program Officer, OSISA</i> |
| <i>Yolisa Pokie</i> | <i>BEE Analyst, BusinessMap</i> |
| <i>Dan Ramahotswa</i> | <i>General Manager, Marketing Key Accounts, ABB Transmission & Distribution</i> |
| <i>Andrew Rens</i> | <i>Wits University</i> |
| <i>Pippa Reyburn</i> | <i>Lawyer, Edward Nathan & Friedland</i> |
| <i>Itumeleng Segaloe</i> | <i>Project Manager, Friedrich Ebert Stiftung</i> |
| <i>Arvid Smedsrud</i> | <i>Swedish South African Business Partnership Fund</i> |
| <i>Per G Wanland</i> | <i>Managing Director, ABB Transmission & Distribution</i> |
| <i>Omari West</i> | <i>Wits University</i> |
| <i>Patric Vestlund</i> | <i>Market Consultant, Swedish Trade Council</i> |

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ABBREVIATIONS

| | |
|-----------------------|--|
| ANC | African National Congress |
| BEE | Black Economic Empowerment |
| BEE Commission | Black Economic Empowerment Commission |
| BMF | Black Management Forum |
| DTI | Department of Trade and Industry |
| ESOP | Employee Share Ownership Plan |
| GEAR | Growth, Employment and Redistribution |
| HDI | Historically Disadvantaged Individual |
| HDP | Historically Disadvantaged Person |
| IDC | Industrial Development Corporation |
| JSE | JSE Securities Exchange South Africa |
| NEF | National Empowerment Fund |
| NEP | New Economic Plan (Malaysia) |
| NGO | Non Governmental Organisation |
| PDI | Previously Disadvantaged Individual |
| PPP | Public-Private Partnership |
| R | Rand, the South African currency |
| RDP | Reconstruction and Development Programme |
| SEP | Strategic Equity Partner |
| SETA | Sector Education and Training Authority |
| SMME | Small, Medium and Micro Enterprise |
| SOE | State Owned Enterprise |
| SPV | Special Purpose Vehicle |

FACTS AND FIGURES ABOUT SOUTH AFRICA¹

People

| | |
|---------------------|---|
| Population: | 43,421,000 |
| Ethnic groups: | Black 75%, White 13%, Coloured 9%, Indian 3% |
| Age structure: | 0-14-years: 32%, 15-64 years: 63%, 65 years and over: 5% |
| Religions: | Christian 68%, indigenous beliefs 28%, Muslim 2%, Hindu 2% |
| Official languages: | Afrikaans, English, Ndebele, Pedi, Sotho, Swazi, Tsonga, Tswana, Venda, Xhosa, Zulu |
| Literacy: | 82% |

Geography

| | |
|-------------------|--|
| Area: | 1,291,912 sq km |
| Time zone: | GMT + 2h |
| Capital cities: | Pretoria (administrative capital) Cape Town (parliamentary capital) Bloemfontein (judicial capital) |
| Provinces: | Eastern Cape, Free State, Gauteng, KwaZulu-Natal, Mpumalanga, North-West, Northern Cape, Northern Province, Western Cape |
| Border countries: | Botswana, Lesotho, Mozambique, Namibia, Swaziland, Zimbabwe |

Government

| | |
|---------------------|---|
| Government type: | republic |
| Chief of state: | President Thabo Mbeki (since 16 th June 1999) |
| Head of government: | President Thabo Mbeki |
| Legislation: | bicameral parliament consisting of the National Assembly (400 seats) and the National Council of Provinces (90 seats) |
| Legal system: | based on Roman-Dutch law and English common law; accepts compulsory ICJ jurisdiction, with reservations |

Economy

| | |
|---------------------|---|
| Currency: | 1 rand (R) = 100 cents, 1 rand = SEK 1.29 ² |
| GDP: | USD 127 billion, per capita USD 3000 (1999) ³ |
| GDP composition: | agriculture: 5%, industry: 35%, services: 60% (1999 est.) |
| Natural resources: | gold, chromium, antimony, coal, iron ore, manganese, nickel, phosphates, tin, uranium, gem diamonds, platinum, copper, vanadium |
| Industries: | mining (world's largest producer of platinum, gold, chromium), automobile assembly, metalworking, machinery, textile, iron and steel, chemicals, fertiliser, foodstuffs |
| Exports: | USD 28 billion (f.o.b., 1999 est.) |
| Export commodities: | gold, diamonds, other metals and minerals, machinery and equipment |
| Export partners: | UK, Italy, Japan, US, Germany (1997) |
| Imports: | USD 26 billion (f.o.b., 1999 est.) |
| Import commodities: | machinery, foodstuffs and equipment, chemicals, petroleum products, scientific instruments |
| Import partners: | Germany, US, UK, Japan (1997) |
| Labour force: | agriculture 30%, industry 25%, services 45% (1999 est.) |
| Unemployment rate: | 30% (1999 est.) |

¹ Source: <http://www.cia.gov/cia/publications/factbook/geos/sf.html> (2001-06-15), unless otherwise indicated

² <http://www.forex.se> 2001-07-09

³ <http://www.swedishtrade.se/sydafrika> 2001-07-09

This is an empirical study performed in Johannesburg and Pretoria, South Africa, during the period of mid October to the end of December year 2000. The Thesis constitutes the Graduate Thesis at the Master of Law Programme at School of Economics and Commercial Law at the Gothenburg University, Sweden.

The topic of the Thesis is chosen after consultation with Swedish companies active in South Africa. Our aim was to find a topic within the field of Commercial Law that is of current interest for business life. Black economic empowerment was pointed out as one of the most central questions for business within the region at present.

1 INTRODUCTION

Since the first democratic elections in South Africa in 1994, black economic empowerment has been one of the foremost issues on the government's agenda.

The government of South Africa recognises that the majority of the people of South Africa for decades have been deprived of all influence in the society. As a result of discriminatory laws and practices, there are firmly established structures and patterns that do not vanish simply by repealing discriminatory laws. Black economic empowerment has a key role in the transformation process aimed at re-balancing the society after the years of apartheid. It is the government's policy to actively promote a more equitable distribution of wealth. This is believed to be necessary in order to secure the newly started democratic process in South Africa.

The government of South Africa promotes black economic empowerment in a number of ways. Beyond enforcing empowerment through legislative measures, emphasis is put on how well the business is compatible with the principles of black economic empowerment when granting State contracts, licences (for example broadcasting, fishing, casino, radio and cellular telephone licences), and giving financial and other assistance to business. Therefore, it is critical for all companies, and particularly companies having dealings with the government in the course of business, to understand the concept of black economic empowerment and its impact on business in South Africa today.

The Thesis is written with the ambition to serve non-South African companies newly established or in the process of establishing in South Africa. In the Thesis we present the elements of black economic empowerment which we consider to be the most relevant in order to be well-informed on the topic.

South Africa is a country in transition. To fully understand black economic empowerment and what it is all about, it has to be placed in South Africa's historical context. Therefore, the Thesis starts with a short summary of the situation of the country in 1994 and what has led it to that position.

1.1 Purpose

Our aim with the Thesis is to provide the reader with a sound basis for the understanding of black economic empowerment in South Africa, with an emphasis on the following questions:

- What is the essence of black economic empowerment, and what is it meant to achieve?
- How does black economic empowerment affect business life in general?
- How has black economic empowerment been approached by business life?
- What is the regulatory framework and what are the consequences of non-compliance?
- Are there other reasons, beyond complying with the law, to implement black economic empowerment policies in business life?
- What are the future prospects of black economic empowerment?

It is our belief that in order to get a solid understanding of black economic empowerment, you must be acquainted with not only the aspects that directly influences your own business, but also to understand the conditions for black businesses. These will most likely be co-workers in one way or another at some point in time. Therefore, we will briefly present different empowerment aspects that are relevant from black entrepreneurs' point of view as well.

1.2 Delimitations

The concept of black economic empowerment is much wider than the area presented in this Thesis, covering everything from improving infrastructure in the rural areas to increasing black ownership on the stock exchange. We will only present the aspects of black economic empowerment that are relevant for the target group we have chosen.

It is not our ambition to give an overall presentation of the conditions for business in South Africa. Our ambition is to give a presentation of how the process of black economic empowerment affects business life in general. The conditions for, and the

varying impact of black economic empowerment in different sectors, will not be specifically discussed.

1.3 Perspective

It is our belief that black economic empowerment must be taken most seriously. Not only because a successful restructuring of the society is of utmost importance for South Africa as a country, but also because, in the long run, we trust it to be in the best interest of companies active in the country as well.

From our point of view, black economic empowerment is not a separate question that can be handled over to consultants or company legal councillors. In this Thesis we will promote that black economic empowerment has to be a vital element in building up the company, permeate the management and be a fully integrated part of a company's policies and strategies for the future. Taking this approach, the understanding of black economic empowerment is crucial for people in leading positions in corporations.

The government of South Africa has a firm commitment to black economic empowerment. This commitment results in, from different groups criticised, interventions in the market. Given the very specific history of South Africa, we have an understanding for the need of these interventions. We will present the government interventions as facts of reality that need to be approached, and we do not have the ambition to evaluate them as such.

1.4 Method

During our 10-week stay in South Africa we met with and interviewed representatives from business life, universities, authorities and relevant organisations, in order to get a broad understanding of black economic empowerment. The interviews served as a problem orientation and guide into what is most relevant and of interest for the chosen target group. Our further research is based on books, newspapers and magazines.

The interviews were often conducted in a confidential atmosphere and took the form of personal discussions, with an open exchange of views. Therefore, we will not name the sources of various opinions that are presented in the Thesis since this in several cases was a precondition for the openness.

This method was chosen since we believe that the personal opinions of people in leading positions are as interesting as, if not more than, the public policies of the organisations they represent.

1.5 Goals

Our goal is to present a Thesis that can serve as an introduction to and a problem orientation in black economic empowerment for non-South African companies established or in the process of establishing in South Africa.

Our hope is that the Thesis will give such an understanding of the empowerment process that an active decision on how black economic empowerment shall impact the strategies of a company can be taken. Furthermore, our aim is to initiate the question on what needs to be done in an organisation to secure the compliance with black economic empowerment regulations and policies.

After having read this Thesis, the reader shall also have the basic knowledge needed to identify unintended conducts that do not comply with the approach chosen by his or her organisation.

2 CONTEXT

Introduction

This chapter begins with a historical section, where we will focus on the part of the apartheid legacy that suppressed the Black, Coloured and Asian South Africans' ability to participate in the economy and conduct business, as well as acquire skills necessary for this. The deprivation of political rights will not be discussed, as it falls outside the scope of this Thesis.

We use the political label 'black' and thereby refer to the three 'non-white' groups of people, in recognition of their common discriminated status in the apartheid society. The degree of suppression varied somewhat between the groups.

The chapter continues by presenting the evolution of black economic empowerment, and concludes by offering a brief international empowerment comparison.

2.1 Historical Context

The history of the apartheid state can be described as institutionalised disempowerment of the black population. Black South Africans were discriminated against in employment, skills development, in ownership and control of business as well as in access to basic social and physical infrastructures.⁴ They were legally barred from any political participation. The oppression was extreme, and in many cases basic human rights were denied.

One of the most important aims of the apartheid legacy was to suppress black entrepreneurship in order to defend and support the interests of white economy. The *Groups Areas Act* decided where black people were allowed to live and the *Influx Control Act* denied them the right to move freely around the country. Blacks were regarded as temporary residents in the 'white urban areas', with the only purpose to provide labour for white industry and commerce. The *Native (Urban Areas) Consolidation Act* of 1945 only allowed small businesses, selling the daily essentials of living, to operate in the urban black townships. The authorities controlled the allocation of all business sites in the area.⁵

In 1963 black businesses were further limited by the 'one-man business' policy that was introduced. This policy hindered black people to run more than one business and prevented them from forming partnerships with the objective of initiating larger business ventures. The 1963 legislation also blocked the establishment of black-controlled financial institutions, wholesale businesses and manufacturing industries in white areas. A decree in the legislation stating that local authorities, not blacks, were to erect all buildings necessary for business activities, gave the authorities further control over black business. Another policy designed to protect white business and limit black entrepreneurship was the 'job reservation'. The job reservation created a white monopoly by restricting blacks, until 1979, from jobs in certain skilled trades and from holding positions above a certain level. This has led to that the technical and managerial skills necessary to operate businesses is severely constrained in the black population.⁶

⁴ NALEDI, draft document - The evolution of "Black Economic Empowerment" in South Africa: From the lenses of business, the tripartite alliance, community groups, and the apartheid and post-apartheid governments (1985 – 1999), Omano Emma Edigheji, 2000, p 15

⁵ Abeluleki Consulting, draft document - Towards an Economic Empowerment Strategy in South Africa, 2000, p 6

⁶ Abeluleki Consulting, draft document, p 6

The Bantu Education system, introduced in 1953, deliberately underdeveloped the capacity of blacks and prepared them for lives of subordination. Science and Maths were practically excluded from the Bantu Education. The black universities were structured to mainly produce social scientists, teachers and lawyers. A number of professions, especially in the natural sciences, were closed to black people and the vast majority was denied the opportunity of higher education.⁷

The *Land Act* of 1913 prohibited blacks from purchasing land outside the 'native areas'. The land allocation to the rural population was disproportionately low. This affected black people in many ways. It did not only curtail development of the farming sector, it excluded them from the financial market by denying them the means to provide sound security for loans.⁸

The effect of the apartheid politics was disastrous for black business and for the human capital essential to self-fulfilment, social development and economic advancement in a modern society. In 1996 these figures were facts;

- Whites, 13 percent of the population, held 80 percent of the professional positions and 93 percent of management positions in private business.
- Less than 7 percent of South African Ph.D. holders were black. Very few black South Africans had higher education in Business, Finance, Engineering and the sciences, as they needed a special government permit to attend white universities where these skills were taught.
- In 1996 adult literacy in South Africa was about 73 percent, but 80 percent of the black people were unable to read beyond the fifth grade level.⁹

South Africa has one of the most unequal distributions of income in the world. This is caused by the extremely low levels of black participation in the economy. In 1994, a black person's income was 13 percent of a white person's income. A Coloured person's income amounted to 27 percent and an Indian income to 40 percent of a white person's income.¹⁰ For many black people in South Africa the only difference in their existence today, compared to the era of apartheid, is that their legal status has improved.

⁷ The impact of black economic empowerment initiatives, Accountancy and Finance Update, August 1997

⁸ Abeluleki Consulting, draft document, p 7

⁹ Ford, Christopher A., Challenges and Dilemmas of Racial and Ethnic Identity in American and Post-Apartheid South African Affirmative Action, UCLA Law Review, vol. 43, August 1996, number 6, p 1973ff

¹⁰ Women lose out in Africa's richest nation, The Star, 31 October 2000

Though the apartheid system has been abolished in South Africa, race and colour still determine the economic and social structure of the society. President Thabo Mbeki described the status, year 2000, in the nation like this: "... South Africa is two nations in one – one white, affluent and privileged and the other black and disadvantaged."¹¹ The previous race ideology, the President pointed out, has led to that distribution of wealth, income, intellectual resources, land and opportunity for personal advancement are skewed in favour of whites in South Africa. He summarised by stating that the aim of the whole system was that whites should always remain the dominant group and the black majority the dominated.¹²

2.2 The Evolution of Black Economic Empowerment

There is a considerable lack of clarity as to what the concept of black economic empowerment really is. Different people and constituencies define it in different ways and assign it different meaning. Consequently, it is important to be aware of who defines black economic empowerment in the discussion.

The definition also varies over time. Black economic empowerment (BEE), Affirmative Action, National Economic Empowerment and Development (NEED) are different terms used from the late 1980's and onwards to describe mainly the same thing.

In the late 1980's, white business regarded black economic empowerment as a mechanism to create a black middle class with interests in the economy. The initial thought was that by partly re-arranging the racial composition of the ownership structure of the economy, the market economy and political stability would be ensured. Corporate social responsibility programmes and black advancement initiatives were introduced to achieve black economic empowerment. The creation of a small influential black business class was part of the goal. Blacks were to gain access in to the formal economy at the same time as the underlying structures of the economy were to be left unaffected.¹³ At this time black people were mostly put in middle management positions without any managerial responsibility.¹⁴ The black people that did have managerial responsibility were mainly taken in of pure business sense. This was when for example black people were needed to give the company insight into black peoples' consumption needs and habits.

¹¹ A long way towards combating racism, Enterprise, October 2000

¹² A long way towards combating racism, Enterprise, October 2000

¹³ NALEDI, draft document - The evolution of "Black Economic Empowerment" in South Africa, p 6f

¹⁴ The impact of black economic empowerment initiatives, Accountancy and Finance Update, August 1997

The first democratic elections in 1994, when the African National Congress, ANC, came to power, were a political turning point. Corporate South Africa responded by appointing black non-executive directors and by selling businesses to black empowerment groups. Financial institutions provided funding to so-called Special Purpose Vehicles (SPVs)¹⁵, which enabled black people without capital to go into business.¹⁶ At this point, black economic empowerment was largely a function of the white businesses' efforts to change themselves.¹⁷ Political correctness became very important in corporate South Africa.

Black economic empowerment was met with suspicion from the black community in the late 1980's, as they feared that it would only create a black middle class without fundamentally transforming the oppressive political system and give full political rights to all. It was not until in the early 1990's that ANC converted to the concept of black economic empowerment. The ANC's position has thereafter been characterised by concepts such as de-racialisation and democratisation of the economy and economic emancipation of the black majority.¹⁸

After the 1994 elections, the ANC-led Government of National Unity (GNU) was focused on reconstruction and reconciliation. Emphasis was put on economic inclusivity, aimed at broadening the economic base of South Africa. This was done by promoting small, medium and micro enterprises (SMMEs) and through the Reconstruction and Development Programme (RDP). Black economic empowerment was on the government's agenda from the very beginning, although not as strongly as it is today.¹⁹

Black economic empowerment of today can be described as a process aimed at redressing the imbalances in the ownership and control of South Africa's economic resources by increasing black participation at all levels of the economy. This shall be done by job creation, poverty alleviation, specific measures to empower black women, education, skills transfer and management development, meaningful ownership and access to finance to conduct business.²⁰

¹⁵ SPVs are presented in chapter 6.2

¹⁶ TIPS Annual Forum "Growth and Investment in South Africa", Johannesburg 21 of September 1999, Panel - National economic empowerment, <http://www.tips.org.za/events/proceedings/bee.html> 2001-07-11

¹⁷ Empowerment companies no longer there for the picking', Business Day, 9 May 2000

¹⁸ NALEDI, draft document - The evolution of "Black Economic Empowerment" in South Africa, p 8ff

¹⁹ BusinessMap, Empowerment 2000 – New Directions, 2000, (BusinessMap 2000), p 49

²⁰ BEE moves to phase two, Enterprise, October 2000

Over the years, the government has expanded the parameters of its empowerment objectives in business to include training, affirmative action, affirmative procurement and equity ownership. The empowerment requirements vary between different state departments, agencies and governments on local, provincial or national level. Several government departments have for example articulated their own policies for empowerment. Subsequently, it is difficult to determine what aspects of empowerment that are most relevant in doing business with these public entities.²¹

Black economic empowerment can also be seen as a way to deepen the economy and stimulate growth in the country by releasing the economic potential of the black population.²²

Under President Thabo Mbeki's leadership work has been put in to create a more coherent, over-reaching approach towards black economic empowerment. The speed to enforce change in the South African society has been picked up and empowerment is becoming a vital part in most of the government's policies. The government is now increasingly using both legislative leverage and its buying power to promote black economic empowerment.²³

The sectors most affected by empowerment are broadcasting, gaming, fishing, IT and telecommunications, construction, transport, energy, mining, asset management in the financial services sector, municipal services (including water and sewage provision), education, health care and the defence industry. Altogether these sectors contributed to the GDP with 38.5 percent in 1998.²⁴

2.3 Empowerment Comparisons²⁵

Black economic empowerment is not a unique phenomenon. Various forms of affirmative action have, and are, taking place around the world. In Malaysia, a programme similar to the one in South Africa was launched in 1969. South Africa has learned a lot from their experiences. Likewise, Malaysia is a country where affirmative action targets a majority of the population. Affirmative action is also used to achieve gender equity in several countries.

²¹ BusinessMap 2000, p 49

²² Need to clean up, Enterprise, May 2000

²³ BusinessMap, Empowerment Guidelines for Investors: Mapping state requirements and investor experiences, 2000, (BusinessMap, Empowerment Guidelines), p 4

²⁴ BusinessMap, Empowerment Guidelines, p 7

²⁵ BusinessMap 2000, p 40f

South Africa's history makes it unique from other nations where affirmative action has or is taking place. In South Africa the majority, approximately 87 percent, of the population has been disadvantaged and is now subject to affirmative action. The gravity of suppression is also making South Africa unique in that the empowerment process has to be very extensive.

2.3.1 South Africa

Empowerment has successfully taken place in South Africa before. Starting in 1948, the Afrikaners²⁶ were subject to economic empowerment. However, the Afrikaners began their process of economic empowerment from a far better position than blacks did in 1994. The Afrikaners were on average relatively more educated than the average black in South Africa and they had the advantage of a major capital base in the form of land. The labour market was also substantially different from today, with focus on manual labour force. Another difference is that the growth rates in South Africa of today (2.5% in average since 1994) are much lower than the ones during the period of 1948-1970 (5% per annum).

2.3.2 United States

In the early 1970's, shortly after the Civil Rights movement, there was a conscious decision by the government in the United States to create a class of black capitalists. The government was proactive in trying to create equal opportunities for blacks in employment, education, housing and business. To facilitate black business development special government structures were set up for the delivery of loans, grants, and technical assistance to black entrepreneurs. In government procurement policies special preferences were granted to black-owned businesses.

The efforts in the United States had a material effect; from 1972 to 1992 the number of black owned businesses grew from 188,000 to 621,000.

The situation in the United States was significantly different from the one in South Africa today. Empowerment in the United States was focused on a minority group, just as the Afrikaners' empowerment in South Africa was, whereas the now ongoing empowerment in South Africa has the majority of the population as its target. Another difference is the economy; the fiscal resources of South Africa cannot be measured against the much greater ones of the United States at the time. The United

²⁶ Afrikaners, also known as Boers, descend from the Dutch settlers in mid 1600.

States also had a number of good black universities that produced a well-educated black managerial and entrepreneurial class.

The economic position of blacks and whites in the United States still, after some 30 years of various initiatives, remains unequal. Affirmative action is now stigmatised as reverse racism. What South Africa can learn from this is that measures beyond affirmative action are needed and that various efforts are required to make real empowerment progress.

2.3.3 Malaysia

Given the population and income statistics, Malaysia is the most relevant example for South Africa. In 1969, the Malaysian government launched the New Economic Plan (NEP), which aimed to eliminate poverty and promote greater economic equality between the different racial groups. Specifically the Bumiputra (indigenous groups, principally Malays) were empowered through expanded educational opportunities, employment quotas and incentives for corporate restructuring. If a non-Malay company wanted to bid for government contracts, for example, or if they wanted to go public, they had to restructure the company and 30% of their stocks were to be sold to Bumiputras at a discount. In order to promote the growth of an industrial and commercial Bumiputra community the government also used the allocation of contracts, quotas and licenses.

The NEP worked very well in Malaysia for the Bumiputras, which previously were the disadvantaged group. In 1970 the Bumiputras' share of corporate equity ownership was 2.4%. Twenty years later this had risen to 20.3%.

The criticism against the NEP is that the Malay elite is seen to have benefited disproportionately, and the Chinese and Indians, the more successful ethnic minorities, feel the playing field is stacked unreasonably against them. At the same time Malaysians, from all ethnic groups, acknowledge that the empowerment focus in the NEP has helped the country to avoid racial turmoil.

2.3.4 The Current Context

The empowerment initiatives described above have all worked well. Nevertheless, the prevailing conditions in South Africa today are substantially different. Globalisation, driven by technological change and economic liberalisation, has reduced a state's ability to dictate change in the world of today. The state is much less powerful in relation to private business or social interests than ever before. This is especially prob-

lematic given the scale of the challenge, to empower South Africa's 38.1 million black people. Not only the fact that it is the majority of the country's population that needs to be empowered makes it problematic, the relative starting points are more unfavourable than the other empowerment groups experienced.

3 THE CONSTITUTIONAL GROUND FOR BLACK ECONOMIC EMPOWERMENT

Introduction

In South Africa's new constitution, *Constitution of the Republic of South Africa*, equality is defined as one of the cornerstones of the democracy in the country. At the same time, the constitution provides for affirmative action measures to be taken. This can be seen as incompatible. However, according to the framers of the constitution, affirmative action shall not be viewed as a derogation from the right to equality, rather it shall be viewed as a means to achieve equality and as part of the right to equality.²⁷

In this chapter we will present the constitutional ground for the affirmative action part of black economic empowerment.

3.1 The Constitution of the Republic of South Africa

The Constitution of the Republic of South Africa was adopted in May 1996 and entered into effect in February 1997.

The beginning of the preamble of the Constitution reads as follows: "We, the people of South Africa, Recognise the injustices of our past; Honour those who have suffered for justice and freedom in our land; Respect those who have worked to build and develop our country; and Believe that South Africa belongs to all who live in it, united in our diversity." The preamble continues by stating that the Constitution has been adopted by the people so as to "...[h]eal the divisions of the past and establish a society based on democratic values, social justice and fundamental human rights;" and to "[i]mprove the quality of life of all citizens and free the potential of each person..."

The Constitution is declared in the explanatory memorandum to "... represent the collective wisdom of the South African people..."

²⁷ Madala, T.H., Affirmative Action – A South African Perspective, SMU Law Review, Vol. 52, No 4, Fall 1999, p 1542

The equality section of the Bill of Rights in the Constitution makes a specific provision for the implementation of affirmative action programmes. After having stated that “[e]veryone is equal before the law and has the right to equal protection and benefit of the law ...”²⁸ it continues with “[e]quality includes the full and equal enjoyment of all rights and freedoms. To promote the achievements of equality, legislative and other measures designed to protect or advance persons, or categories of persons, disadvantaged by unfair discrimination may be taken.”²⁹ Through this the Constitution authorises measures to be taken which are designed to promote the achievement of equality.

Affirmative action is also sanctioned in the Constitution’s chapter on Public Administration, as it states that “*Public administration must be broadly representative of the South African people, with employment and personnel management practices based on ability, objectivity, fairness, and the need to redress the imbalances of the past to achieve broad representation.*”³⁰ (emphasis added). By stating that the administration must be broadly representative of the South African people, it is indirectly stating that affirmative action shall take place. This is further emphasised by the fairness criteria and the explicit wording that the need to redress the imbalances of the past shall be taken into account in employment and personnel management practices in the public administration.

In the Equality section discrimination is prohibited. No one, including the state, may “unfairly discriminate directly or indirectly against anyone on one or more grounds, including race, gender, sex, pregnancy, marital status, ethnic or social origin, colour, sexual orientation, age, disability, religion, conscience, belief, culture, language and birth.”³¹ This protection against unfair discrimination is modified in that discrimination on one or more of the grounds listed “... is unfair unless it is established that the discrimination is fair.”³² This means that although the criteria listed in terms of non-discrimination in the Constitution are far more inclusive than in many modern nations, discrimination on fair grounds is in principle permissible.³³

²⁸ Constitution of the Republic of South Africa, chapter 2 section 9 (1)

²⁹ Constitution of the Republic of South Africa, chapter 2 section 9 (2)

³⁰ Constitution of the Republic of South Africa, chapter 10 section 195 (1) i

³¹ Constitution of the Republic of South Africa, chapter 2 section 9 (3-4)

³² Constitution of the Republic of South Africa, chapter 2 section 9 (5)

³³ Tummula, Krishna K., Policy of Preference: Lessons from India, the United states and South Africa, Public Administration Review, Nov/Dec99

Thus, the question of the legality of affirmative action in South Africa is answered. Yet, certain questions remain, such as to what degree either law or private-sector programmes may be undertaken without conflicting with the Constitution's core principle of equality. The requirement that discrimination shall be formally determined to be "fair" in order to be permissible may mean that no affirmative action programme in South Africa will be Constitutional without receiving a fairly explicit judicial imprimatur. Therefore, the contours of South African affirmative action jurisprudence may not become clear for some time.³⁴

4 GOVERNMENT POLICY PROGRAMMES

Introduction

In this chapter two major government policy programmes are presented: RDP, a socio-economic policy framework, and GEAR, a macroeconomic strategy. Together these two programmes constitute the base for the black economic empowerment process. To be acquainted with the basic features of these programmes is important for the understanding of black economic empowerment.

4.1 The Reconstruction and Development Programme (RDP)

The *Reconstruction and Development Programme* (RDP) constituted the election manifesto of the African National Congress (ANC) for the elections in 1994.³⁵ It was the result of consultation within the ANC, its Alliance partners and other mass organisations.³⁶ After the election it was adopted and supported by all political parties in the Government of National Unity and the parliament, and it was implemented through the RDP White Paper in September 1994.³⁷

The RDP is an integrated, coherent socio-economic policy framework, which seeks to mobilise all the people and resources of South Africa towards the final eradication of the results of apartheid, the building of a democratic, non-racial and non-sexist future. The programme is a vision for the fundamental transformation of the country. It integrates growth, development, reconstruction, redistribution and reconciliation into a unified programme.³⁸

³⁴ Ford, *Challenges and Dilemmas of Racial and Ethnic Identity*, p 1968f

³⁵ NALEDI, draft document - The evolution of "Black Economic Empowerment" in South Africa, p 9

³⁶ The Reconstruction and Development Programme – A Policy Framework, preface

³⁷ RDP White Paper, Discussion Document, September 1994, preface 0.2

³⁸ RDP White Paper, 1.1.1 + 1.3.6

There are six basic principles of the RDP that shall ensure a coherent programme. The first is that of an integrated and sustainable programme, in order to overcome the legacy of apartheid. The second principle is that the programme must be a people-driven process. Peace and security for all, nation-building, the linking of reconstruction and development and democratisation of South Africa are the other ones.³⁹ In one sentence it can be presented as: “An *integrated programme*, based on *people*, that *provides peace and security for all* and *builds the nation, links reconstruction and development* and deepens *democracy* ...”⁴⁰

All the proposals, strategies and policy programmes contained in the RDP are grouped into five key programmes:

- **Meeting Basic Needs** of people, such as jobs, land, housing, water, electricity, telecommunications, transport, a clean and healthy environment, nutrition, health care and social welfare.⁴¹
- **Developing Human Resources** through education in formal institutions, at workplaces, homes, public work programmes, youth programmes and in rural areas. Arts and culture programmes as well as access to sport and recreation are also treated within this key programme.⁴²
- **Building the Economy.** This programme deals with linking reconstruction and development. Topics such as industry, trade and commerce, resource-based industries, upgrading infrastructure, labour and worker rights and issues regarding Southern Africa are being dealt with in this key programme.⁴³ Racial and gender inequalities in ownership, employment and skills are addressed as serious weaknesses in the economy.⁴⁴
- **Democratising the State and Society.** This key programme sets out the role for the Constitution and Bill of Rights, of national, provincial and local government, the administration of justice, the public sector, parastatals, the police and security forces, social movements and NGOs.⁴⁵
- **Implementing the RDP.** This programme deals with the implementation and co-ordination of the RDP and the establishment of effective RDP structures, as well as development of a programme to finance the RDP.⁴⁶

³⁹ RDP White Paper, 1.3.2–1.3.7

⁴⁰ The Reconstruction and Development Programme – A Policy Framework, 1994, 1.3.8

⁴¹ The Reconstruction and Development Programme, 1.4.2

⁴² The Reconstruction and Development Programme, 1.4.4-5 + 8-9

⁴³ The Reconstruction and Development Programme, 1.4.18

⁴⁴ The Reconstruction and Development Programme, 1.4.13

⁴⁵ The Reconstruction and Development Programme, 1.4.20

⁴⁶ The Reconstruction and Development Programme, 1.4.21 + 23

The RDP white paper from 1994, dealing with implementation questions, states that it is essential that the existing ownership patterns become less concentrated. The participation in the economy needs to increase, become more racially inclusive and small, medium and micro enterprises must account for a larger part of the economic activity.⁴⁷ Therefore, the government sets out to, together with the private sector and NGOs, to determine appropriate support policies for small and medium-sized enterprises.⁴⁸

The RDP is to be financed through the RDP Fund.⁴⁹ Resources are drawn from savings by the departments, international and domestic grant aid, interest earned from the investments of money standing to the credit of the fund, sale of state assets and from other sources, such as revenue from lotteries and gambling.⁵⁰

4.2 Growth, Employment and Redistribution – A Macroeconomic Strategy

Growth, Employment and Redistribution (GEAR) is a macroeconomic strategy launched by the government in 1996. It is a strategy for rebuilding and restructuring the economy, built on the goals set forth in the RDP programme.⁵¹ The GEAR strategy has somewhat displaced the RDP programme's economic role.

Central for the programme is to increase the economic growth, in order to reverse the unemployment crisis, provide resources for the expansion in social service delivery and for progress toward an equitable distribution of income and wealth. The strategy points out that transformation towards a competitive outward-oriented economy is required for a sustained growth on a higher level. The GEAR strategy set out a growth rate of six percent per annum and job creation of 400,000 per annum by the year of 2000.⁵²

The core elements of the GEAR strategy are:

- budget reform to strengthen the redistributive thrust of expenditure;
- fiscal reform aimed at reducing the size of the government's deficit, counter inflation and free resources for investment;
- a monetary policy to keep the real effective exchange rate stable at a competitive level and to prevent a resurgence of inflation;

⁴⁷ RDP White Paper, 3.1.4

⁴⁸ RDP White Paper, 3.10.1

⁴⁹ Established in terms of the RDP Fund Act of 1994

⁵⁰ RDP White Paper, 2.3.1-6

⁵¹ Growth, Employment and Redistribution – A Macroeconomic Strategy, June 1996, 1.1

⁵² Growth, Employment and Redistribution, 1.2-3

- gradual relaxation of exchange controls and a reduction in tariffs to contain input prices and facilitate industrial restructuring;
- an industrial policy with tax incentives to stimulate new investment in competitive and labour absorbing projects, a flexibility within the collective bargaining system and a strengthened levy system to fund training;
- speeding up the restructuring of state assets, in order to optimise investment resources and address service deficiencies and backlogs by an expansionary infrastructure programme; and
- an expansion of trade and investment flows in Southern Africa.⁵³

A key element in the government's strategy for employment creation and income generation is the promotion of small, medium and micro enterprises (SMMEs). Various programmes and institutions have been established to give effect to this strategy.⁵⁴ The GEAR strategy seeks to give clear directions to the economic course of South Africa and aims to build a competitive fast-growing economy.⁵⁵

The GEAR policy has come under a flood of criticism. Some say that South Africa needs 'a change of GEAR', while others are calling on the government to scrap the GEAR policy since it has failed in what it set out to achieve, namely to bring economic growth and create jobs.⁵⁶

The government's policies will not be described further, nor analysed in this Thesis.

5 GOVERNMENT TOOLS TO DRIVE EMPOWERMENT

Introduction

This chapter aims at presenting different state initiatives that have introduced an empowerment component in the course of business. We will concentrate on the government's usage of its buying power in order to promote black economic empowerment (BEE). The government's empowerment activities through licenses, privatisation and public-private partnership will be dealt with briefly, just to give the reader an introduction and to help to place the phenomena in the context. The chapter begins with describing the multi-faceted approach that characterises the government's empowerment efforts.

⁵³ Growth, Employment and Redistribution, 1.4

⁵⁴ Growth, Employment and Redistribution, 5.4

⁵⁵ Growth, Employment and Redistribution, 10

⁵⁶ Stop-go for GEAR? Enterprise, November 2000

5.1 Government's Definition on Black Economic Empowerment

For a company dealing with state entities in the course of its business, it is an essential but difficult task to elucidate the government's approach to black economic empowerment. Whereas there should not be any obscurity about the government's objectives with the transformation process overall, the varying emphasis put on empowerment aspects in different situations can be perplexing.

In the absence of a BEE-blueprint stating the essence of black economic empowerment, government departments and state entities have developed their own empowerment conducts. This implies differing empowerment policies between state departments, governments and agencies on local, provincial and national level. Empowerment requirements are also enforced with varying emphasis depending on the procedure in question. This means that the empowerment obligations differ between, for instance, a licence application at a local authority and a tender procedure at state level.

To ensure that the government's approach to black economic empowerment finds homogeneous expressions, legislation has recently been passed for instance in the procurement area. However, until uniform procedures are established and followed throughout the public sector, it will be difficult to determine unambiguously what aspects of empowerment are considered most relevant in doing business with public entities.

Generally, the elements that are most frequently looked at are equity ownership, management representation, skills development and training as well as small business and community support. Usually, bidders for any government contracts have to show that they have considered empowerment in all these aspects.⁵⁷

5.2 Preferential Procurement

5.2.1 Background

The government – at national, provincial and local level – is estimated to procure goods and services at a value of R110 billion each year.⁵⁸ The procurement budgets of state owned enterprises are substantial as well, amounting to between R40 and R60 billion.⁵⁹

⁵⁷ BusinessMap, Empowerment Guidelines, p 10

⁵⁸ Ramaphosa says black economic empowerment has failed, *Business Day*, 13 September 2000

⁵⁹ Ministry of Public Enterprises, *An Accelerated Agenda Towards the Restructuring of State Owned Enterprises: Policy Framework*, 2000, p 73

In order to take a part of these resources by closing government or parastatal deals, it is crucial for companies to understand the procurement system and policies as well as the inducements behind them.

It is not a new phenomenon that the government of South Africa utilises its extensive buying power to promote political, social and economic objectives. In the late 40's, as the National Party came to power, the public tendering system was made use of to advance Afrikaners' social and economic position.⁶⁰ In addition, a kind of preferential procurement took place during the time of international sanctions, as the tender conditions allowed a 10% premium for local manufacturers.⁶¹

After the democratic elections in 1994, there was an urgent need for procurement strategies that would reflect the objectives stated in the Reconstruction and Development Programme (RDP).⁶² Subsequently, an interim "10-Point Plan"⁶³ on public sector procurement was introduced in early 1996. The foremost aim of the plan was to improve small, medium and micro enterprises' (SMMEs) access to state tenders, for example by establishing Tender Advice Centres, simplifying the tender documents and dividing larger contracts into smaller ones.⁶⁴

To implement the 10-Point Plan and to especially promote SMMEs owned by black people or women, a price preference system was developed for contracts under R2 millions. According to the evaluation formula, a tender could be awarded up to 88 of total 100 points for the price. Remaining 12 points were awarded based on the equity ownership structure of the bidding company; Up to 10 points could be received if the bidding company was 100% owned by black people (1 point at 10% ownership etc) and similarly up to 2 points could be received based on the equity owned by women. Thus, the price premium for a tendering company entirely owned by black women was up to 13.64% (12/88).⁶⁵ With other words, such a company could present a tender scoring 76 points for the price and still be competitive with a company scoring 88, the maximum points, for their price.

⁶⁰ Naledi, Policy Bulletin, Vol. 2., No 4, November 1999, p 5

⁶¹ BusinessMap, Empowerment Guidelines, p 11

⁶² van Niekerk, Tristan A., Enabling Legislation for SMME (Small, Medium and Micro Enterprise) Development: Defining the Participants and Administering the Rules in an Affirmative Public Sector Procurement Programme, 1998, p 10

⁶³ Procurement Task Team: An Initiative of the Ministries of Finance and Public Works Interim Strategies: Public Sector Procurement Reform in South Africa: A 10-Point Plan, November 1995

⁶⁴ Naledi, Policy Bulletin, p 5

⁶⁵ Naledi, Policy Bulletin, p 5

With the adoption of the new Constitution in 1996, the constitutional ground for preferential procurement was laid. The section on procurement starts with stating that “[w]hen an organ of state ... contracts for goods or services, it must do so in accordance with a system which is fair, equitable, transparent, competitive and cost-effective”.⁶⁶

According to the same section, this does not prevent an organ of state from implementing a procurement policy that provides for

“a. categories of preference in the allocation of contracts; and
b. the protection or advancement of persons, or categories of persons, disadvantaged by unfair discrimination.”⁶⁷

This is in line with the equality clause in the Constitution’s Bill of Rights, by which measures may be taken to promote equality.⁶⁸

To enable an unsuccessful tenderer to verify that his constitutional rights to equal treatment have been observed during the tender evaluation, the Appeal Court has ruled that all public bodies, including parastatals, have a constitutional duty to provide reasons for their decisions.⁶⁹

The Constitution sets out that national legislation must provide a framework in which the preferential procurement policy may be implemented.⁷⁰

The process towards a legislative framework started in April 1997 with the *Green Paper on Public Sector Procurement Reform in South Africa*. In this extensive discussion document, the government clearly manifests its determination to use its purchasing power to attain specific socio-economic objectives.⁷¹

5.2.2 The New Procurement System

After a strongly delayed legislation process, the *Preferential Procurement Policy Framework Act* (Framework Act) was finally passed in February 2000 to give effect on the Constitution, by providing a framework in which an organ of state must determine and implement its own preferential procurement policy.

⁶⁶ Constitution of the Republic of South Africa, chapter 13, section 217 (1)

⁶⁷ Constitution of the Republic of South Africa, chapter 13, section 217 (2)

⁶⁸ Constitution of the Republic of South Africa, chapter 2, section 9 (2)

⁶⁹ Transnet gets wake-up call on tenders, *Business Day*, 15 November 2000

⁷⁰ Constitution of the Republic of South Africa, chapter 13, section 217 (3)

⁷¹ *Green Paper on Public Sector Procurement Reform in South Africa - An initiative of the Ministry of Finance and the Ministry of Public Works*, April 1997, chapter 1

Similar to the former 10-Point Plan, the Framework Act propounds a preference point system to be followed. For contracts with a Rand value above a prescribed threshold, up to 10 points may be allocated for ‘specific goals’, whilst up to 90 points can be granted based on the price. For contracts equal to or below the threshold value, specific goals can score up to 20 out of 100 points.⁷² Thus, the smaller contracts can be granted more points for specific goals in order to promote the SMME sector.

According to the Framework Act, the specific goals may include

- “(i) contracting with persons, or categories of persons, historically disadvantaged by unfair discrimination on the basis of race, gender or disability;
- (ii) implementing the programmes of the Reconstruction and Development Programme ...”⁷³

The invitation to submit a tender must clearly specify any specific goal for which points may be awarded in the procurement process in question.⁷⁴ Further, a specific goal must be measurable, quantifiable and monitored for compliance in order to be adequate for preference point allocation.⁷⁵

The Minister of Finance may exempt an organ of state from any or all the provisions of the Framework Act if it should be of importance for national security or in the public interest. The provisions of the Framework Act may also be deviated from if the likely tenderers are international suppliers.⁷⁶

Due to its general character, the Framework Act does not define neither the concept of historically disadvantaged persons nor how their participation in the contracts should more precisely be evaluated. Further, the settlement of the crucial threshold value is left for later regulation.⁷⁷

To give substance to the Framework Act⁷⁸, *Draft Regulations of the Preferential Procurement Policy Framework Act* (Draft Regulations) were released by the Department of State Expenditure⁷⁹ in June 2000. The Draft Regulations apply to all organs

⁷² Preferential Procurement Policy Framework Act, No 5, 2000, (Framework Act), chapter 2, sections 1 (a) + 1 (b) i-ii

⁷³ Framework Act, chapter 2, section 1 (d) i-ii.

⁷⁴ Framework Act, chapter 2, section 1 (e)

⁷⁵ Framework Act, chapter 2, section 2

⁷⁶ Framework Act, chapter 3, sections (a)-(c)

⁷⁷ Framework Act, chapter 5, section 1

⁷⁸ Also called a “disgraceful piece of slipshod work”, Empowerment: wrong message, Finance Week, 4 February 2000

⁷⁹ Now included in The National Treasury together with the former Department of Finance

of state, and forbid the application of any preference system not in compliance with the Framework Act, the Draft Regulations or other legislation.⁸⁰

The threshold value referred to in the Framework Act is specified in the Draft Regulations to be R2 million. To calculate the price points for a contract with a Rand value equal to or below 2 million, the following formula must be used:

Preference Point System 80/20:⁸¹

$$80 \times \left[1 - \frac{P_t - P_{\min}}{P_{\min}} \right]$$

Where P_t = Rand value of tender under consideration
 P_{\min} = Rand value of lowest acceptable tender

Consequently, the formula for calculating the price points for a contract with a Rand value above 2 million is:

Preference Point System 90/10:⁸²

$$90 \times \left[1 - \frac{P_t - P_{\min}}{P_{\min}} \right]$$

The invitation to submit a tender must stipulate which of these two preference point systems will be applied to that specific tender. This implies thorough planning and pre-calculation by the organs of state before each tender procedure. All the tenders are to be evaluated after the preference point system indicated in the tender document, irrespective of whether some of the received tenders have a value that should imply for the application of the other preference point system. Should all the received tenders fall within the system not indicated, i.e. have a value equal to or below R2 million where the 90/10 preference point system is stipulated, or consequently a value above R2 million when stipulating the 80/20 preference point system, the tender must be cancelled and re-invited with the appropriate preference point system

⁸⁰ Preferential Procurement Policy Framework Act, No. 5, 2000:Draft Regulations, (Draft Regulations), section 2
⁸¹ Draft Regulations, section 5 (1)
⁸² Draft Regulations, section 5 (2)

indicated.⁸³

For the purpose of determining preference points, the Draft Regulations define Historically Disadvantaged Individuals (HDIs) as including all South African citizens,

- “1. who had no franchise in national elections prior to the introduction of the 1983 and 1993 constitutions;⁸⁴
2. women; or
3. disabled persons.”⁸⁵

Equity ownership by these HDIs may entitle for preference points calculated by the formula

$$\text{NOP} \times \frac{\text{EP}}{100}$$

Where NOP = the maximum points awarded for equity ownership by HDIs

EP = the percentage of equity ownership by HDIs within the enterprise.⁸⁶

However, preference points are not granted for mere ownership of shares, without control and active involvement in the company’s management and daily business operations proportional to the degree of ownership. A change in the degree of ownership after the closing date of the tender results in the withdrawal of the preference points. Subsequently, a public company cannot score preference points for HDI-ownership, due to the changing shareholder structure in such companies.⁸⁷

As stipulated in the Framework Act, the specific goals that may entitle to preference points also include implementing programmes outlined in the government’s socio-economic policy framework RDP, the Reconstruction and Development Programme. This reference to the RDP goals seems to make the scope for attaining preference points very broad. Surprisingly, the Draft Regulations do not put forward any principles to be used when allocating preference points for the promotion of RDP-objectives.

⁸³ Draft Regulations, section 5

⁸⁴ The 1993 constitution was a interim constitution, negotiated principally between the then-governing National Party leader F.W. de Klerk and Nelson Mandela

⁸⁵ Draft Regulations, section 1

⁸⁶ Draft Regulations, section 7 (2) (d)

⁸⁷ Draft Regulations, section 7 (2) (b)

Although the current procurement system is blamed for placing too much emphasis on price, most of the procurement contracts cannot be secured solely with price points. White companies have had to acclimatise to the new procurement regulations. In order to be competitive, they have entered partnerships with HDI-owned companies or changed their ownership profile by bringing in black shareholders. These have either been employees or people unrelated to the company. Larger companies have also launched various social responsibility programmes, often with employee training and community support elements, in order to show commitment to the empowerment process.

The Draft Regulations provide a formula for calculating preference points, when they are claimed for on the basis of partnership with companies owned by HDIs. The principle is that each partner's own preference points are taken into account to the same degree that they will execute the contract. This means that a joint venture between a 100% white male owned company and a 50% HDI-owned company, where the HDI-company delivers 60% of the contract value, could score 3 preference points within the 90/10 preference point system (10p x 50% x 60%).⁸⁸

The government's procurement procedures have until recently been administered by a system headed by a national State Tender Board and nine provincial boards. At the time of writing, there are plans to abolish the tender boards. A major reason for this is that they have been found to be archaic, cumbersome and prone to corruption.⁸⁹ In some provinces, the tender boards are already replaced by procurement committees within the provincial departments.⁹⁰

5.2.3 Problems Connected to Procurement

The high amount of state expenditures together with the emphasis put on equity ownership by HDIs make affirmative procurement one of the government's most powerful tools to promote black economic empowerment. At the same time, the economical values involved have made abuse of the system lucrative, thus hampering the empowerment effects.

Due to institutional weaknesses and insufficient monitoring of performance by the government, the procurement system has left scope for companies to evade the requirements of substantial involvement by the historically disadvantaged persons.

⁸⁸ Draft Regulations, section 7 (4)

⁸⁹ The tender trap, Business Day, 1 March 2001

⁹⁰ Free State acts to improve tendering, Business Day, 10 May 2001

Thus, contracts have been won by registering black persons (during the 10-Point Plan preferably black women, since that scored two additional preference points) as owners in white companies, or setting up a black-owned company to tender on behalf of the white company, which would then be subcontracted to perform the contract obligations. Further, black persons have seen their opportunity to profit by posing as 'empowerment' partners during a tender procedure and then leaving the scene.⁹¹ These kinds of token conducts have raised concepts called window-dressing, fronting, mobile black executives, rent-a-black, rent-a-face etc. The reasons for these conducts vary, but the common denominator for companies to create an artificial empowerment profile can be said to be the wish to qualify for government contracts. The phenomenon is usually associated with procurement procedures, but can also take place for instance within affirmative action.

The government has been blamed for encouraging window-dressing by focusing on requirements on HDI-ownership without ensuring that the compliance is adequately monitored. The Draft Regulations now state that an organ of state may require, at any time in the tendering process, a bidder to verify its claims for preference points.⁹² It is questionable whether this will be sufficient to address the problem, which has given rise to negative connotations to the empowerment process in its entirety.

5.2.4 Procurement by State Owned Enterprises

State Owned Enterprises (SOEs) are not regarded as organs of state, wherefore the Framework Act and the Draft Regulations do not formally apply to them. However, the government, in its shareholder capacity, raises requirements that the SOEs' procurement procedures shall comply with the described legislation all the same.⁹³

SOEs, especially the 'Big Four' parastatals Eskom (electricity), Telkom (telecommunication), Transnet (transport) and Denel (defence industry) are known to be committed promoters of black economic empowerment. For instance, the power group Eskom doubled its spending on BEE initiatives in year 2000 to R1.9 billion, mainly through its procurement policies.⁹⁴

To eliminate fronting and tokenism, these companies have introduced firm practises to monitor their BEE contracts. Eskom completes a thorough screening every time a company takes part in a tender procedure, regardless of its earlier contracts with

⁹¹ Black Faces for Hire, Enterprise, February 1998

⁹² Draft Regulations, section 6.3

⁹³ Policy Framework for the Restructuring of SOEs, p 73f

⁹⁴ Eskom boosts empowerment, Business Day, 17 April 2001

Eskom. Should token practises be disclosed, the company is disqualified as a tenderer and summoned to appear before a disciplinary committee. Transnet seeks to secure genuine participation from a BEE-company by requiring shareholder certificates and interviews with the bidding company and its possible partners. Moreover, contracts are closely monitored, and where a part of a contract has been subcontracted to small businesses, their progress is followed up.⁹⁵

To an increasing extent, SOEs pay attention to their suppliers' procurement procedures and require empowerment elements in their purchase policies. This means that the sphere that is affected by the parastatals' affirmative procurement practises is becoming wider.

5.3 Licenses and quotas

In sectors such as broadcasting, telecommunication, gaming and fishing, the government is enforcing empowerment by incorporating empowerment obligations in the requirements for licenses and quotas necessary for operation in the field. The bidders for such licenses and quotas are partly evaluated by their ability to meet empowerment requirements, relating to levels of ownership by black groups as well as non-equity-related empowerment factors, such as employment equity and training.

To give an example, the South African Telecommunications Regulatory Authority, Satra⁹⁶, applied following evaluation criteria and weightings when the third mobile network licence was announced in 1999:⁹⁷

- Empowerment 25%
- Technical 13%
- Business plan and implementation strategy 44%
- Universal Service 11%
- Impact on industry and consumers 7%

The scope of the empowerment element was wide, requiring the bidders to give evidence of, among others, ownership by historically disadvantaged groups, job creation, affirmative action and training commitments as well as community and social responsibility programmes. Due to the importance given to empowerment aspects and the high investments required for the licence, expectations on the empowerment ef-

⁹⁵ BEE that works, Enterprise, June 2000
⁹⁶ Today the Independent Communications Authority of South Africa, Icasa
⁹⁷ BusinessMap, Empowerment Guidelines, p 22

fect were high.⁹⁸

These requirements were seen as difficult to manage and critics have called the licence affair a 'beauty contest' not based on facts. Suspicions of irregularities and government intervention in the process have attracted much attention in the media and the outcome was contested by a court process.

Beyond the third mobile network licence affair, there have been a number of flaws abating license requirements of delivering good empowerment results. Particularly in the field of fishing where quotas are allocated, we have been told that the empowerment requirements are often dealt with in a way hardly corresponding with government's good intentions; Black SMMEs who have qualified for a quota have sold their fishing rights further to an established fishing company, thus ruling out the chance for skills transfer and job creation. Such conduct, known as 'paper quota' system,⁹⁹ impedes empowerment from happening and needs to be addressed if the requirements are to be kept.

5.4 Restructuring and Privatisation of State Owned Enterprises

The reconstruction of State Owned Enterprises (SOEs) has been an important issue on the government's agenda ever since the elections in 1994. The SOEs inherited by the new government were in many cases not equipped for delivering service to all South African citizens.

The restructuring of SOEs, often referred to with the narrower term privatisation, is used by the government as an arena where to enforce its empowerment objectives. However, the government's ambition to implement empowerment elements into restructuring deals have varied during the last years depending on the strategic nature of the assets to be restructured. Where non-core assets have been at stake, the empowerment requirements have been considerable and the bidders have usually had to find black equity partners in order to qualify for the deal. Whereas when assets with strategic dimension or important public service function has been concerned, government's concern has been to find foreign, financially strong Strategic Equity Partners (SEPs) with high technology resources and expertise in the field.¹⁰⁰ The focus on the Strategic Equity Partner's ability to meet the objectives of the specific asset and to ensure a highly professional delivery has put empowerment requirements low

⁹⁸ BusinessMap, Empowerment Guidelines, p 22

⁹⁹ BusinessMap, Empowerment Guidelines, p 24

¹⁰⁰ BusinessMap, Empowerment Guidelines, p 26

down on the priority list. For example, when the government initiated the search for an SEP into the state telecommunications company Telkom in 1995, there was a fear that a strong emphasis on empowerment aspects would affect the value of Telkom adversely. The government therefore did not require the bidders to bring an empowerment partner into the deal.¹⁰¹

The government's different approaches to enforce empowerment requirements in restructuring of the SOEs have been criticised. The lack of empowerment effect in some deals where the government has offered stakes to both Strategic Equity Partners and empowerment investors has been criticised as well. For example, when selling 20% of The Airports Company of South Africa (ACSA) to Aeroporti di Roma in 1998, another 10% stake was directed to empowerment investors. Hindered by the high prices that foreign bidders offered and the difficulties to finance the acquisition, only 4.2% of the shares were transferred to black owners.¹⁰²

The idea of selling out state assets without any positive empowerment effects emanating from it was politically inconceivable. Therefore, the establishment of a trust was initiated to secure that black equity ownership is an outcome of privatisation of any State Owned Enterprise.

5.4.1 National Empowerment Fund Trust

The National Empowerment Fund (NEF) Trust was established in 1998 by the *National Empowerment Fund Act (No 105, 1998)*. The Act states that the aim of the NEF Trust is to redress the inequalities brought about by apartheid. This shall be done through promotion and facilitation of ownership of income generating assets to historically disadvantaged persons (HDPs). The HDPs are defined as those persons or categories of persons, who prior to the new democratic dispensation, marked by the adoption and coming into force of the Constitution of the Republic of South Africa in 1996, were disadvantaged by unfair discrimination on the basis of their race. This definition also includes juristic persons or associations owned and controlled by such persons.¹⁰³

Beyond providing historically disadvantaged persons with the opportunity to become direct or indirect owners of SOEs, the Trust's objectives are, among others, to encourage and promote saving, investments and meaningful economic participation by peo-

¹⁰¹ BusinessMap 1999, p 79

¹⁰² Policy Framework for the Restructuring of SOEs, p 65

¹⁰³ National Empowerment Fund Act, No 105, 1998, section 1 (f)

ple in this target group. Furthermore, the NEF Trust promotes and supports business ventures pioneered and run by historically disadvantaged persons and promotes the universal understanding of equity ownership among the HDPs.

To meet these objectives, the NEF Trust is entitled to acquire shares in SOEs that are being restructured, at a discount of up to 20%.¹⁰⁴ Up to the late year 2000, the Trust had received shares with a nominal value of about R2 billion, most of the value represented by a 10% stake deriving from the Telkom restructuring in 1997. As the restructuring process of SOEs proceeds, the Trust may earmark up to 10% of the shares in each SOE. This represents a nominal value of between R10-20 billion.¹⁰⁵

The assets in the Trust will be distributed to the beneficiaries through three different investment vehicles:

An **investment trust** will market affordable investment units, including both SOE-shares and other investments. The trust has a dual purpose: it provides ordinary people with the chance to be shareowners, and educates them to understand the mechanisms of an equity market.¹⁰⁶

A **portfolio trust** will be set to hold the shares until they can be sold to HDPs seeking a direct shareholding in these SOEs.¹⁰⁷

To encourage entrepreneurship and to address the scarce access to financing, an **equity management fund** is prepared for providing HDPs with venture capital. The fund aims to take into account the HDPs' special conditions that have a historical basis, and does thus, for example, not require extensive business records from the loan applicants.¹⁰⁸

The start-up phase for the NEF Trust has been long, and it was not until in April 2001 that the first CEO of the fund was appointed.¹⁰⁹ Therefore, it is too early to judge whether the NEF Trust will become "... one of the most significant investment entities in the South African financial markets ..."¹¹⁰ as envisaged by the government.

¹⁰⁴ BusinessMap, Empowerment Guidelines, p 37

¹⁰⁵ Policy Framework for the Restructuring of SOEs, p 68

¹⁰⁶ Dr Themba Mhlongo, Chief Director: Industry & Technology Strategy, Department of Trade and Industry, interview 28 November 2000

¹⁰⁷ Policy Framework for the Restructuring of SOEs, p 69

¹⁰⁸ Dr Themba Mhlongo, Chief Director: Industry & Technology Strategy, Department of Trade and Industry, interview 28 November 2000

¹⁰⁹ Government appoints first CEO of empowerment fund, Business Day, 6 April 2001

¹¹⁰ Policy Framework for the Restructuring of SOEs, p 68

5.4.2 Restructuring as a BEE-Tool Today

Government's current approach to the restructuring of the SOEs is presented in a Policy Framework¹¹¹ from August year 2000. The benefits of the restructuring process are believed to be distributed more effectively through new, creative and diverse empowerment strategies. Hence, the Policy Framework proposes a multi-dimensional approach to empowerment through three kinds of empowerment elements in the SOE restructuring processes:

- The **NEF Trust's role** as a tool to broaden ownership is emphasised. It is expected to play an important role in promoting empowerment options by providing different kinds of equity schemes for those previously excluded from mainstream economic participation. Guidance shall be sought from international experiences of collective investment vehicles, in order to avoid the problems in existing empowerment-related financial engineering.¹¹²
- While increasing ownership of SOEs remains a crucial element of empowerment, the government is also enforcing **operational empowerment** to ensure that a broader part of the HDPs is reached by the empowerment strategies. Operational empowerment implies for a wide range of active participation in industries affected by the SOE restructuring, from access to training and skills development to improving entrepreneurial opportunities through outsourcing, partnerships, affirmative procurement and access to financing.¹¹³
- Finally, **Employee Share Ownership Plans** (ESOPs) and **community trusts** (such as producer and consumer co-operatives and non-profit organisations) are being considered as alternative empowerment tools in the restructuring process.¹¹⁴

5.5 Public-Private Partnerships

Public-Private Partnerships (PPP) has been generated from the recognition that the government alone cannot meet South Africa's increasing development challenges. In order to generate economic growth, provide infrastructure and deliver services, the government needs to complement its capacity with the private sector's strengths and

¹¹¹ Ministry of Public Enterprises, An accelerated Agenda Towards the Restructuring of State Owned Enterprises: Policy Framework (Policy Framework for the Restructuring of SOEs)

¹¹² Policy Framework for the Restructuring of SOEs, p 87

¹¹³ Policy Framework for the Restructuring of SOEs, p 72-73

¹¹⁴ Policy Framework for the Restructuring of SOEs, p 87

abilities.¹¹⁵

The government's PPP policy is manifested in three key documents:

- *Strategic Framework for Delivering Public Services through Public-Private Partnerships*
- *Treasury Regulations*¹¹⁶
- *Guidelines for Public-Private Partnership*¹¹⁷

Due to the wide range of PPP variations and the fact that PPP arrangements were practised before the regulative framework emerged, there has been some confusion regarding what constitutes PPPs. Treasury Regulations now define PPP as a contractual arrangement whereby a private party performs a departmental function for a specified time against remuneration together with a substantial transfer of risk to the private party.¹¹⁸

The nature of services or functions that different departments perform in public interest is diverse. Therefore, a PPP arrangement can relate to everything from a 1-year facility maintenance service contract to a 30-years concession, where the contractor manages, operates, maintains and invests in a new airport, road etc. Common to PPPs of different character is a substantial transfer of risk to the private party, enabling the department to shift its focus from providing the service to managing the contract with the service provider.¹¹⁹

The way in which empowerment specifically shall be emphasised within the scope of a PPP cannot be concluded from the policy framework. However, in practise a PPP project often involves empowerment requirements, which a potential service provider has to meet in order to win the contract. The required empowerment elements again depend on the nature of the contract. For example, in construction industry, emphasis is typically placed on employment and training involving the local communities.¹²⁰

PPPs contribution as an empowerment deliverer is still to be shown. Without regulated empowerment requirements, though, the government's interest of delivering cost effective and efficient service to communities might take precedence over sometimes contradictory empowerment ambitions.

¹¹⁵ Department of Finance, *Guidelines for Public-Private Partnership*, April 2000, p i

¹¹⁶ National Treasury: *Treasury Regulations for departments, constitutional institutions, public entities, Parliament and provincial legislatures*, May 2000

¹¹⁷ Department of Finance, *Guidelines for Public-Private Partnership*, April 2000

¹¹⁸ *Guidelines for Public-Private Partnership*, p 5

¹¹⁹ *Guidelines for Public-Private Partnership*, p 5-6

¹²⁰ BusinessMap, *Empowerment Guidelines*, p 30

6 THE FINANCING OBSTACLE

Introduction

The government's focus on delivering empowerment, especially through its procurement and licence practises, gave a strong impetus for partnerships between black companies, who wanted to take part in the mainstream operations, and white companies, seeking to adjust their company status to the new requirements. The emergence of such partnerships through ordinary market practises was restrained due to the black partners' lack of access to capital.

In this chapter, we will describe the broadly applied solution to this problem, the so-called Special Purpose Vehicle. After discussing new approaches to finance empowerment deals, the chapter will be concluded with a short introduction to the government's financing initiatives aiming to address the problem.

6.1 Financing of Empowerment Deals

A major obstacle facing the early BEE-initiatives attempting to transfer ownership into black hands was the lack of access to capital by the black population. In the climate where established businesses felt pressure to support black business initiatives, various creative solutions were found.

Particularly during the first years of empowerment, artificial control tools such as convoluted pyramid company structures and the issuance of so-called N-shares occurred. By issuing low-voting N-shares to investors, owners of an empowerment company could raise capital without diluting their own control over the company. These methods ensured the appearance of black control that did not always reflect economic realities.¹²¹

Black investors, without the financial means needed, were offered to buy shares in white companies that were seeking to change their ownership profile. Financial institutions, such as investment bankers, retirement funds and insurance companies, facilitated the ownership transformation process by starting to provide various finan-

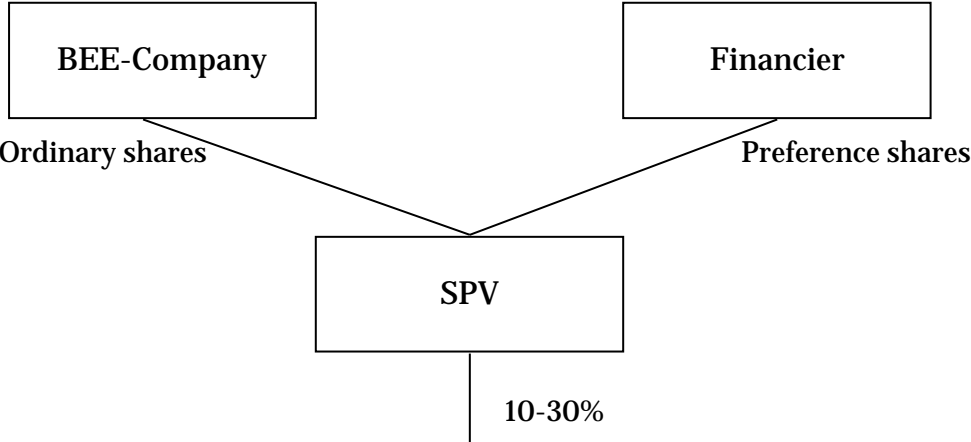
¹²¹ BEE – quest for more workable models, Enterprise, October 1999

cial instruments, of which the Special Purpose Vehicle (SPV) would become most favoured.¹²²

6.2 SPV – Special Purpose Vehicle

An SPV is a special purpose company established by a ‘BEE-company’, with the purpose to facilitate the purchase of an equity stake in a ‘target company’. There is no unambiguous legal definition of what constitutes a BEE-company (also referred to as an empowerment company). Therefore, the level and form of involvement by black persons required for an empowerment status vary from case to case. The target company can either be a company listed on JSE Securities Exchange SA or a private company, interested in selling an equity stake to a black partner.¹²³ The impetus behind this interest is often the target company’s eagerness to appear politically progressive and to qualify for government contracts that put requirements on the bidder’s empowerment status. Hence, the shares in the target company are not seldom offered at a 10-20 % discount of the current market price.¹²⁴ The incentive for a financier to become involved in the empowerment deal is, apart from being regarded as politically correct, to get access to large stakes (usually 10-30%) in coveted companies, not available without partnership with a black company.¹²⁵

The BEE-company raises the required means to fund the deal partly through a loan from the financiers, partly by issuing preference shares in the SPV to them. The BEE-company holds 100% of the ordinary shares in the SPV and therefore controls the votes.¹²⁶



¹²² Between 1996 and 1998, SPVs were by far the most favoured financing structure, accounting for 52% of black economic ownership, BEE Commission Draft Discussion Document, 2000, p 45, <http://www.beecom.org.za> 2000-10-08

¹²³ BEE Commission, Draft Discussion Document, p 45

¹²⁴ Easy street looks like a dead end, Newsweek, 12 June 1999

¹²⁵ BusinessMap 2000, p 35

¹²⁶ “Asian Tigers” did it, so can we... , Enterprise, July 2000

| |
|----------------|
| Target Company |
|----------------|

The preference shares are redeemable in three to five years. In the meantime, the preference shares entitle the financier to a determined dividend rate from the SPV, normally expressed as a percentage (usually 60-65%) of the prime lending rate.¹²⁷ Any equity performance achieved over and above this dividend rate is shared between the BEE-company and the financier. The SPV financing structure places most of the economic benefit on the financier as the owner of the preference shares. However, as all the funding comes from the financier, he assumes all the downside risk as well.¹²⁸

The terms of an SPV vary from case to case, but the basic philosophy behind the structure is the belief that the target company's earning potential and share price will increase due to the achievement of an empowerment status and the black group's participation. The structure relies on a bullish market with rising share values and low interest rates, enabling the BEE-company to repay the borrowed funds by selling a part of its shares as the term of the SPV becomes due.

6.2.1 The Effect of the Market Crisis in 1998

During the first two-three years, the positive market expectations were generally met and the SPV seemed to be a real success story for all the parties involved. However, due to the crisis on the Asian market in 1998, the market turned bearish and the interest rates shot up. The dividends from the target company became insufficient to serve the dividend rate, which led to that the payments due were added to the loan capital. This happened at a time when many preference shares were about to be redeemed. If the BEE-company could not raise cash elsewhere, it had to relinquish a portion or even all of its shares in the SPV to the financier in order to settle the debt.¹²⁹ In several cases, the BEE-companies were not able to meet their financial obligations, thus losing the newly acquired assets as well as causing substantial losses for the financiers.¹³⁰

6.2.2 Critique on the Model

¹²⁷ Oiling the financial wheels of black empowerment, Financial Mail, 13 November 1998

¹²⁸ "Asian Tigers" did it, so can we... , Enterprise, July 2000

¹²⁹ BusinessMap 1999, p 13

¹³⁰ BEE Commission, Draft Discussion Document, p 46

SPV as a mechanism to finance black companies' share acquisitions has met harsh criticism after the market crisis in 1998. It has been called financial engineering, not resulting in real, sustainable empowerment due to evident weaknesses in the structure. Some of the weaknesses are:

- The black company's ownership in the underlying investment is based on debt. Even in the best-case market scenarios, the model implies that the black company would have to give up a part of its ownership in order to meet the financial requirements at the end of the term. This has resulted in that several BEE-companies have exited an SPV with no or strongly diluted ownership in the underlying investment. Consequently, the structure does not contribute to real transfer of ownership to black hands.¹³¹
- As a result of the SPV being 'one step away' from the target company's daily operations and that the ownership stake seldom exceeds 20 percent, the BEE-group's ownership is limited to one or few board seats. Therefore, it is said that the ownership does not give the black group a chance to a meaningful influence on the executive and operational level in the target company.¹³²
- The participation in an SPV does not require any risk-taking from the black company. With everything to gain, black companies have been eager to close as many SPV deals as there are. This has resulted in BEE-groups acquiring corporate interests in various sectors, lacking the strategic and operational focus normally required from an ownership portfolio and with little attention to adding value to the investments.¹³³
- The SPV structure separates control from the economical risk, thus not reflecting fundamental business principles.
- The incentives behind the target company to find a black partner have in a number of cases been to get a politically correct ownership structure and to secure further government contracts. This has negatively affected the interest to carefully choose the right empowerment group as a partner and to support skills transfer during the partnership.

¹³¹ BEE Commission, Draft Discussion Document, p 47

¹³² BEE Commission, Draft Discussion Document, p, 48

¹³³ BusinessMap 2000, p 11

- The success of an SPV mechanism relies on absolute rather than relative performance of the target company. The performance is not benchmarked on earnings or share price compared to its peers on the market, but on the target company's absolute share price performance.¹³⁴

Today, these inherent weaknesses in the SPV model seem obvious and it is easy to criticise the financial institutions for initiating the SPVs and similar artificial funding mechanisms that do not help the black companies to create a sustainable capital base of their own. Still, the financial institutions' role in black economic empowerment has been important, BusinessMap¹³⁵ argues in its annual report on black empowerment. They enabled the 'capitalist without capital' to become a part of the corporate establishment and to take the first steps towards a balanced ownership structure in SA.¹³⁶ Even if it has been recognised that this ownership transfer seldom was sustainable, there has been successful empowerment deals financed through SPVs as well. However, the turbulent market situation in late 1998 made the shortcomings connected with the SPV model visible, and since then this financing method has become less popular. Still, the key question on how to finance empowerment deals remains.

6.2.3 New Approaches

During the past two years, financial institutions have had to reconsider their role in the empowerment process and come up with new working financing solutions. According to BusinessMap, two different directions can be recognised having emerged from the finance crisis.¹³⁷

Reworking the SPV-Model

The first type of response has aimed to rework the traditional financing mechanisms such as the SPVs. It is believed that these kinds of funding arrangements have not yet played out their role, but that they need to be adjusted in order to prevent the negative consequences from reoccurring. One initiative has been to create a secondary market for the SPVs, thus alleviating the reduced liquidity for the financier during the SPV contract. There have been indications that this can become a viable option for both financiers and the empowerment companies.¹³⁸

¹³⁴ "Asian Tigers" did it, so can we... , Enterprise, July 2000

¹³⁵ BusinessMap is a prominent research and consultancy company, with Black Economic Empowerment as one of its areas of focus. For more information, see <http://www.businessmap.co.za>

¹³⁶ BusinessMap 1999, p 7

¹³⁷ BusinessMap 2000, p 35

¹³⁸ BusinessMap 2000, p 35

Another major flaw in the SPV structure was the askew risk allocation on the financier alone. It is argued that in order to ensure the BEE-company's interest in active participation as a shareholder, there should be something more to loose than just the BEE-company's time invested. Subsequently, financiers have started to require some financial input from the BEE-company into the SPV-deal. The input can be of limited importance as security for the loan, but significant enough for the BEE-company to ensure that proper business principles are brought in to the deal. It has also been initiated that a BEE-company's involvement in various SPVs should not continue to be ring-fenced, meaning that assets in one SPV in the future shall be able to be claimed for debts accrued in another SPV.¹³⁹

Financiers are also searching for ways of passing some of the risks onto the target company, for example by demanding the target company to guarantee the financing offered to the BEE-company. This is believed to strengthen the target company's involvement in the process, especially when it comes to choosing the right empowerment partner and to clarify its objectives with the deal.¹⁴⁰ However, the target companies' participation must be designed in a way that respects the section 38 of the Companies Act, which prohibits a company to financially assist the purchase of shares in the company itself.¹⁴¹

Creating New Solutions

The second direction can be described as a new approach towards financing empowerment deals. It emphasises sustainable long-term deals between sound companies, whose contributions are clearly defined and measured before entering the partnership.¹⁴² Investments in passive holding companies belong to the history according to this approach. Access to financial means is only given to those black companies that demonstrate strong strategic focus, commitment for operational involvement in their investment and preparedness to share the risks.¹⁴³ Further, financiers' interest is increasingly drawn towards BEE-companies that have emerged by building an operational business from the ground, instead of having acted merely as an investment holding company without an operational track record.¹⁴⁴ The financiers also insist on sophisticated corporate governance in the BEE-company. They require de-

¹³⁹ BusinessMap 1999, p 8

¹⁴⁰ BEE Commission, BEEC Black Economic Empowerment project, Draft Report, June 1999, p 286

¹⁴¹ This issue is discussed in a university coursework "The Financing of Black Economic Empowerment – the SPV Funding Model and Section 38 of the Companies Act", by Samuel Gumede, 2000

¹⁴² BusinessMap 2000, p 36

¹⁴³ BusinessMap 2000, p 35

¹⁴⁴ BusinessMap 1999, p 8

veloped reporting mechanisms, appropriate information disclosure and remuneration based on performance. These issues were often neglected during the first eager years of empowerment.¹⁴⁵

Regardless of whether financial institutions prefer funding instruments based on a modified type of SPV or new solutions, their current approach can be described as emphasising the integration of sound business principles with empowerment deals.

We believe that the new approach to support empowerment deals is to be welcomed. It will probably be successful in correcting the asymmetrical risk-return profile and remuneration not linked to performance, characteristic for the early financing models and rule out the possibilities to easy gains without any risk and active involvement. However, the first years of empowerment have not yet changed the historical fact that there is scarcely any accumulated black capital available to back new business initiatives. If the black peoples' different conditions are ignored when granting financial help, the entry barriers into the economic sphere can become too high for new black business initiatives.

6.3 Government Financing Initiatives

The scarcity of black capital was early recognised by the government to choke the empowerment process. To address this issue and as a part of its national strategy to promote the SMME-sector, government introduced new institutions with the aim to increase black entrepreneurs' access to financing:

Khula Enterprise Finance was established in 1996. Its main objective is to provide loans to SMMEs through a network of financial retailers. These are banks, non-governmental organisations (NGOs) and provincial development corporations. Other products consist of credit guarantees to secure SMMEs loans, and granting of seed loan and capacity building for new financial retailers.¹⁴⁶

Ntsika Enterprise Promotion Agency was established by the Department of Trade and Industry (DTI) in 1995. Through support, managerial development and programme funding, it aims to increase local and provincial SMME Service Providers' ability to deliver non-financial support to SMMEs.¹⁴⁷

¹⁴⁵ BusinessMap 2000, p 12

¹⁴⁶ <http://www.khula.org.za> 2001-06-11

¹⁴⁷ <http://www.ntsika.org.za> 2001-06-11

Industrial Development Corporation (IDC) was originally established in 1940 as a state owned corporation. Its mission is to promote industrial development through a wide range of financing facilities for new and existing projects.¹⁴⁸ It has been restructured to serve government's empowerment objectives and is now, among others, providing financial help to emerging entrepreneurs in the industrial businesses through its Entrepreneurial Finance programme.¹⁴⁹

To give black entrepreneurs access to capital is also one of the objectives of government's major initiative **National Empowerment Fund (NEF)**.¹⁵⁰

7 THE DIFFERENT PHASES OF EMPOWERMENT

Introduction

In the last years, a dynamic empowerment process has taken place, in which it is possible to distinguish different phases with their own, characteristic features. It is not feasible to unambiguously define the nature and duration of an empowerment phase. Whereas some people are debating the fourth, or even the fifth generation of empowerment, the majority holds the view that the empowerment process is today shifting over to its third major phase. In this chapter, our aim is to give the reader a general picture of the most characteristic features in the two empowerment waves up to present, whereas the future prospects are discussed in chapter 11.

7.1 The First Phase of Empowerment

To understand the early years of empowerment, you have to be acquainted with the general atmosphere in South Africa after the first democratic elections in 1994. The new government was committed to deliver wealth to the neglected majority of the population. The corporate sector was eager to show acceptance to the new order, wishing to thereby prevent turbulent development in the economic sector. Without a framework stating the objectives of the transformation process, empowerment initiatives emerged from both private and public actors in a non co-ordinated and confused manner.

The first phase of empowerment was characterised by a deal making frenzy. Focus was on acquisition rather than the creation of wealth. Artificial financing structures, such as Special Purpose Vehicles, SPVs, paved the way for black equity ownership in

¹⁴⁸ NALEDI, draft document - The evolution of "Black Economic Empowerment" in South Africa, p 22

¹⁴⁹ <http://www.idc.co.za> 2001-06-11

white companies, playing the politically correct game and looking for an empowerment label to meet the new requirements for government contracts.

The SPV-structures encouraged black consortia to participate in a sophisticated form of gambling, where the risk to loose was entirely placed on the financiers. To enhance the prospects to win, black companies started to run over each other to secure as many SPV-deals as possible. In many cases, this implied lack of focus and passive ownership of shares with no operational participation. The 'blackness' behind an empowerment company was in many cases questionable. Tempted by the discounted access that empowerment companies had to white-owned companies looking for an empowerment partner, the label of black control could be created through excessive divergence in voting rights or complex pyramid structures.¹⁵¹ It was not exceptional either to exercise pure window-dressing to secure the 'empowerment' status of a company.

The strong focus on equity transactions limited the empowerment effect to a small group of black people, a group that was already better off economically than the average black South African. Therefore, the designation 'enrichment process' has said to more correctly illustrate the character of the first phase of empowerment.

Between July 1996 and July 1998, the market capitalisation of black-controlled firms on the JSE Securities Exchange rose from R7 billion to R67.8 billion, corresponding to a rise from 0.7% to 6% of the JSE market capitalisation.¹⁵² The celebration of black companies' success on the JSE was interrupted by the market crisis in late 1998. Share prices went down dramatically, the collapse of the Rand sent interest rates up and the lack of substance behind ownership based on debt was revealed. Political correctness went out of the window as the structural weaknesses of the early empowerment deals were exposed and revised the attitude to the SPV-structure as an appropriate empowerment tool.¹⁵³

7.2 The Second Phase of Empowerment

Lessons from the market crisis revealed that there are no short cuts to genuine empowerment. It gave an impetus to redefine the concept of black economic

¹⁵⁰ The fund has been discussed earlier in chapter 5.4, Restructuring and Privatisation of State Owned Enterprises

¹⁵¹ BEE – quest for more workable models, Enterprise, October 1999

¹⁵² BusinessMap, Empowerment Discussion Paper - An eye on the future, 20 September 1999

¹⁵³ BEE – quest for more workable models, Enterprise, October 1999

empowerment and gradually led to the present phase, called the second phase of empowerment, where there is emphasis on active and committed operational involvement instead of mere equity ownership.

After the first impatient wave, second generation empowerment can be described as a slower, but a more meaningful transformation process aimed to give empowerment companies a substantial and permanent role in the economy. Operational control, adding value and internal affirmative action policies are the keywords in this phase of empowerment.

Many black empowerment companies have been structured as unfocused investment holding companies. This was overlooked by the market during the first years, since partnership with black empowerment companies brought access to government tenders and privatised assets. This has now changed. With an increasing number of empowerment companies, 'blackness' does not provide an edge anymore. To be of interest, black empowerment companies have to be focused, add value to their investment and have a good reputation.¹⁵⁴ As Jakes Gerwel, former adviser to South Africa's former president Nelson Mandela has expressed it, "[b]lack empowerment companies are no longer 'just black cherries that can be picked and put on top of something'..."¹⁵⁵

Financial institutions are increasingly talking of a bottom-up approach and are losing interest to finance unfocused empowerment conglomerates.¹⁵⁶ Thus, the new empowerment companies concentrate increasingly on start-up operations and practise direct control of investments and subsidiaries. Subsequently, the first-generation empowerment companies have been forced to show clear focus by selling off non-core investments in order to be attractive to investors.¹⁵⁷

During the first years, which were dominated by SPV-structures, financial institutions took on a disproportionate amount of risk and reward compared to their empowerment partners. As the lack of capital remains a serious obstacle to empowerment deals, SPV-like financing solutions still exist to some extent. Nevertheless, a more appropriate allocation of risk and rewards is seen as crucial.¹⁵⁸

¹⁵⁴ Time to take stock, Financial Mail, 4 June 1999

¹⁵⁵ Empowerment companies no longer there for the picking', Business Day, 9 May 2000

¹⁵⁶ Falling black control on the JSE matters, Business Day, 22 March 2000

¹⁵⁷ BEE's unsung heroes, Enterprise, June 2000

¹⁵⁸ Falling black control on the JSE matters, Business Day, 22 March 2000

During the first phase of empowerment, the presence on JSE Securities Exchange was seen as the ruling measure of success or failure of empowerment companies. It is still an important benchmark of empowerment, but there is a growing realisation that formal control does not necessarily bring true empowerment. The emphasis is shifting from passive investment companies towards full-time involvement at operational level, where value adding and skills transfer can take place. Thus, the equity control on the stock exchange is no longer seen as 'the Holy Grail of empowerment'.¹⁵⁹

An increasing number of successful empowerment transactions involving unlisted companies have contributed to shift the focus away from the JSE, as well. The stock exchange is still a potent and very visible symbol of economic power though, and the process of black empowerment will not be complete until there is substantial black ownership of JSE-listed shares.¹⁶⁰

Ownership of shares, either in listed or unlisted companies, is no longer perceived to be the only and most appropriate deliverer of sustainable empowerment. The second phase of empowerment has seen the apartheid attitude 'big is beautiful' fade, and there is an increasing emphasis on the promotion of SMMEs and empowerment on grass-root level. It is now believed that job creation, skills transfer and broad-based true empowerment must come from the small, entrepreneurial companies.¹⁶¹

8 BLACK ECONOMIC EMPOWERMENT COMMISSION

Introduction

Since its establishment, the Black Economic Empowerment Commission (BEE Commission) has drawn a great deal of attention in the South African media. In most cases where the state of black economic empowerment has been discussed, reference has been made to the Commission and its ongoing research in the field. The BEE Commission has recently completed its work. The Commission's recommendations are likely to have an influence on the government's future empowerment efforts, as well as affect the public debate on the subject. Therefore, it is important to be acquainted with the BEE Commission and the major conclusions of its research work.

8.1 The Establishment of the BEE Commission

¹⁵⁹ Falling black control on the JSE matters, Business Day, 22 March 2000

¹⁶⁰ Falling black control on the JSE matters, Business Day, 22 March 2000

¹⁶¹ BEE's unsung heroes, Enterprise, June 2000,

The establishment of the Black Economic Empowerment Commission was initiated in November 1997 at a conference held by the Black Management Forum (BMF), an independent non-governmental organisation supporting the development of managerial leadership and transforming of organisations.¹⁶² On the conference, concerns were raised about the weaknesses and inadequacies in the BEE process. It was recognised that the empowerment process had been left to be conceptualised, controlled and driven by the private sector, from which the black people and women still were essentially excluded.¹⁶³

The BEE Commission was formally established in May 1998 by the Black Business Council, an umbrella body representing 12 black business organisations, whereof BMF is one. The mandate given to the Commission was to investigate the success of the BEE progress thus far, to identify possible barriers in the process and to make recommendations for the future.¹⁶⁴

Thus, the objectives set by the BEE Commission were:

- “To gain insight into the BEE process through empirical research and to make observations on the pace and results of BEE initiatives during the 1990’s.
- To reach conclusions on the obstacles to meaningful participation of black people in the economy.
- To develop a powerful case for an accelerated National BEE Strategy and to make recommendations on policies and instruments required to guide a sustainable strategy.
- To develop benchmarks and guidelines to monitor the implementation of the National BEE Strategy.”¹⁶⁵

The BEE Commission’s work has been headed by Cyril Ramaphosa, who was ANC’s chief negotiator with the former South African regime when the apartheid rule was ended. He was thereafter elected chairman of the Constitutional Assembly, which delivered South Africa’s new Constitution in 1996. Ramaphosa, by many expected to succeed Nelson Mandela to head the ANC, left the political arena for private sector in 1996, and is today a prominent businessman.¹⁶⁶

¹⁶² http://www.bmfonline.co.za/vision_and_mission2.htm 2001-06-07

¹⁶³ Executive Summary Report of the BEE Commission, http://www.bmfonline.co.za/bee_rep.htm 2001-06-07

¹⁶⁴ Mbeki stresses empowerment report deadline, Business Day, 22 November, 1999

¹⁶⁵ BEE Commission, Draft Discussion Document, p 2

¹⁶⁶ Govt denies Ramaphosa investigation, The Mail & Guardian, 1 September 2000

After conducting extensive research and consultations with stakeholders and experts from different sectors, the BEE Commission released a discussion document that was debated at the National Consultative Conference in September 2000. The BEE Commission's final report was handed over to President Mbeki in April 2001.¹⁶⁷

8.2 The BEE Commission's definition of BEE

The fundamental concept that formed the base for the BEE Commission's research work was that a substantial increase of the levels of black participation in the economy is indispensable in order to attain growth.¹⁶⁸ The Commission's definition on what constitutes black economic empowerment is:

- "It is an integrated and coherent socio-economic process.
- It is located within the context of the country's national transformation programme, the RDP.
- It is aimed at redressing the imbalances of the past by seeking to substantially and equitably transfer and confer the ownership, management and control of South Africa's financial and economic resources to the majority of its citizens.
- It seeks to ensure broader and meaningful participation in the economy by black people in order to achieve sustainable development and prosperity."¹⁶⁹

Accordingly, the BEE Commission argues that BEE should be broadly viewed, including among others:

- job creation
- rural development
- urban renewal
- poverty alleviation
- specific measures to empower black women
- skills and management development
- education
- meaningful ownership
- access to finance for households and for conducting business.¹⁷⁰

In its research the BEE Commission states, that seven years after the implementation of a transformation programme, which aims at fundamentally changing South Af-

¹⁶⁷ At the time of writing, the final report is yet to be released on the Commissions homepage <http://www.beecom.org.za>

¹⁶⁸ <http://www.bmfonline.co.za/ramaphosa.htm> 2001-04-27

¹⁶⁹ Executive Summary Report, http://www.bmfonline.co.za/bee_rep.htm 2001-06-07

¹⁷⁰ Executive Summary Report, http://www.bmfonline.co.za/bee_rep.htm 2001-06-07

rica's political, economic and social landscape, the country's economic growth performance remains weak. The BEE Commission emphasises that structural distortions in the economy, as well as ingrained racism across all sectors of the society, preserve the marginalisation of the black majority. The subsequent result is high levels of unemployment and one of the most unequal distributions of income in the world.¹⁷¹

In order to break out of this cycle of underdevelopment and to launch the country onto a course of economic growth, the BEE Commission calls for a fundamental shift in the approach from all sectors of society. It argues for an adoption of a coherent and Integrated National BEE Strategy as a national imperative.¹⁷²

The purpose with an Integrated National BEE Strategy would be to create a coordinated set of guidelines and regulations that manifest the priorities and targets for the economic transformation process and the different stakeholders' roles and obligations within this process.¹⁷³

According to BEE Commission, the moral and political legitimacy for implementing such an Integrated BEE Strategy is to be found in the former legacies of colonialism, apartheid and the deliberate disempowerment of the majority of South Africa's population.¹⁷⁴

8.3 The BEE Commission's recommendations¹⁷⁵

The BEE Commission proposes the Integrated National BEE Strategy to include the following key components:

- A **National black economic empowerment Act**, which would define BEE and set uniform guidelines against which the public and private sector can measure their performance and use when implementing BEE. In order to address market failures and to transform existing government institutions, the BEE Act should also provide for the establishment of
 - A permanent **National Empowerment Commission** within the office of the President of South Africa
 - A **National Procurement Agency** aimed at transforming the procurement environment in the public as well as in the private sector

¹⁷¹ Executive Summary Report, http://www.bmfonline.co.za/bee_rep.htm 2001-06-07

¹⁷² BEE Commission, Draft Discussion Document, p 9ff

¹⁷³ Executive Summary Report, http://www.bmfonline.co.za/bee_rep.htm 2001-06-07

¹⁷⁴ Executive Summary Report, http://www.bmfonline.co.za/bee_rep.htm 2001-06-07

¹⁷⁵ Executive Summary Report, http://www.bmfonline.co.za/bee_rep.htm 2001-06-07

- A **National Empowerment Funding Agency** with the aim to rationalise existing government funding initiatives (for instance Khula and Ntsika) and increase the access to capital among black entrepreneurs
- A **Rural Development Agency** to raise funds for land acquisition and rural infrastructure development
- **Uniform definitions to determine a company's empowerment status** to be applied by the public and private sector. For instance, within affirmative procurement practises a company's BEE-rating would determine the awarding of set-asides and price preferences:
 - A **'black company'** is 50.1% owned and managed by black people. Rating for accreditation purposes: A, allowing the company to qualify for set-asides and a 15% price preference.
 - A **'black empowered company'** is 25.1% owned and managed by black people. Rating: B, allowing it to qualify for set-asides and a 10% price preference.
 - A **'black influenced company'** is 5-25% owned and managed by black people. Rating: C, price preference 5%.
 - An **'engendered company'** is one with 30% representation of black women within the black ownership and management portion. This gives an additional 5% price preference, for example an 'engendered black company' is entitled to 20% price preference, an 'engendered empowered company' to 15% etc.
- Government, labour and business should reach an agreement on an **Investment for Growth Accord** describing the parties' obligations to invest in areas of national priority and thereby increase the country's fixed investment levels and promote economic growth. For example, Government Employees Pension Fund should invest 10% of its assets in productive investments within areas of national priority. Obligations to invest a certain percentage of the total assets should also be imposed on the financial sector, particularly life and retirement companies.
- A **Commercial Equity Act** to facilitate de-racialisation of business practises and ownership
- An **Empowerment Framework for Public Sector Restructuring** defining principles to be followed in the restructuring process
- An **Integrated Human Resources Development Strategy**.

8.4 Critique on the BEE Commission and its recommendations

As earlier described, the BEE Commission was established with the task to define black economic empowerment and make recommendations for the future empowerment process. After the commission's work has been considerably delayed, it has been criticised to let the urgent issue of empowerment slip away from the national agenda. The slow delivery of the awaited results have been described as taking on 'biblical proportions'¹⁷⁶ and raised speculations on whether the delay has been caused by some commissioners in order to serve their own agendas.¹⁷⁷

As the final report was released in April year 2001, its compromising and unspecified nature seems to have been a disappointment for those awaiting clear and tangible guidelines for the future development of BEE. It has also been stated that more than two-thirds of the BEE Commission's proposals are already in various stages of implementation.¹⁷⁸ This has probably been caused by the fact that the government has not been represented in the Commission.

However, the report is clear on calling for a strong and intervening government to drive the empowerment process through the promulgation of the BEE law and creation of several new institutions. The government has objected to this excessive reliance on state delivery and means that black economic empowerment can only advance through co-operation between government, business and labour.¹⁷⁹ Some of the BEE Commission's comprehensive proposals for new laws and special structures for BEE have also been questioned. The government has argued that many of the issues raised can be addressed within the existing legislative and institutional framework if they are given time to prove their ability to deliver empowerment.¹⁸⁰

In its final report, the Commission urges the private sector to recognise its collective responsibility to assist government in the empowerment process. Yet, the Commission's strong emphasis on the government's active role can give an opposite effect, as it can be used as an excuse by the established (white) business, not to take an active part in the transformation process.

The BEE Commission's proposal for fixed investment levels (also known as prescribed asset requirements), forcing institutional investors to hold a certain percent-

¹⁷⁶ Panel tussles with an issue blurred by lack of definition, Financial Mail, 17 March 2000

¹⁷⁷ Delays no good for SA, Business Day, 19 February 2001

¹⁷⁸ Delay in report threatens black empowerment, Business Day, 26 March 2001

¹⁷⁹ Erwin urges black business to lead empowerment initiative, Business Day, 29 September 2000

¹⁸⁰ Submission deadline too early, some claim, Business Day, 9 October 2000

age of their assets in designated empowerment investments, is seen as the most controversial recommendation. Even if the requirement for fixed investment levels is planned to be limited to 5-7 years, it is regarded as a major state intervention in an area that should be left to the market mechanisms. The fear is that it will distort the relationship between risk and return and lead to misallocation of scarce resources.¹⁸¹ Furthermore, there is a question on who would decide what qualifies as 'productive investment' within areas of national priority.¹⁸²

The BEE Commission has been criticised to not have dealt with the lack of skills among black people. It has been argued that this issue should be considered before placing comprehensive requirements on businesses, in order to avoid that they will resort to token conducts that characterised the first years of empowerment.¹⁸³

The BEE Commission's goal to become a permanent, statutory body is also questioned. Placed within the bureaucracy of a statutory commission, black economic empowerment would risk becoming an issue outside the mainstream.¹⁸⁴

9 LABOUR LAWS

Introduction

As a result of apartheid and other discriminatory laws and practices, there are disparities in employment, occupation and income, which create a pronounced disadvantage for certain categories of people. According to the government's point of view, this status cannot be redressed simply by repealing discriminatory laws. Consequently, they have sought to influence the workplace through a variety of legislative means.¹⁸⁵ Below we offer a presentation, as well as some critique, of these laws.

9.1 Employment Equity Act (No 55 of 1998)

The purpose of the *Employment Equity Act* is to achieve equity in the workplace by promoting equal opportunity and fair treatment in employment. Affirmative action measures are implemented to redress disadvantages in employment experienced by, so-called, designated groups. The objective of the Act is to ensure equitable representation in all occupational categories and levels in the South African workforce.¹⁸⁶

¹⁸¹ Persuasion, not prescribed assets, Business Day, 15 August 2000

¹⁸² Black advancement, Business Day, 15 September 2000

¹⁸³ Hat-trick needed, Financial Mail, 29 September 2000

¹⁸⁴ More flesh needed, Business Day, 28 March 2000

¹⁸⁵ Employment Equity Act, No 55, 1998, preamble

¹⁸⁶ Employment Equity Act, chapter 1 section 2

The Act requires so called designated employers, discussed below, to implement affirmative action measures for people from designated groups. Designated groups are defined as ‘black people’ (which in this Act is used as a generic term for Africans, Coloureds and Indians), women and people with disabilities.¹⁸⁷

The Act puts certain requirements, such as the anti-discrimination clauses, to all employers. Other clauses, more specifically the affirmative action clauses, only apply to the so-called designated employers, except where otherwise is provided. Therefore, it is necessary to clarify what constitutes a designated employer. For the purpose of this Act, designated employers are defined as employers employing 50 or more employees. Employers employing fewer than 50 employees, but with a total annual turnover equal to or exceeding the applicable annual turnover of a ‘small business’, in terms of a schedule in the Act, are designated as well. The annual turnover threshold of a small business, according to the schedule, range from R2 million in the Agricultural sector to R25 million in the sector of Wholesale Trade, Commercial Agents and Allied Services. An employer can also be a designated employer by being bound by a collective agreement, which appoints it as a designated employer in terms of the Employment Equity Act. All municipalities and organs of state, with a few exceptions, are also considered to be designated employers.¹⁸⁸

An employee is defined as any person, other than an independent contractor, who works for another person and who receives, or is entitled to receive, any remuneration and, in any manner, assists in carrying on or conducting the business of an employer.¹⁸⁹ If a person’s services have been procured for, or are provided to a client by a temporary employment service, for a indefinite duration or for a period of three months or longer, that person is deemed to be an employee of that client as well.¹⁹⁰

The Act can be divided into two main areas; (1) prohibition of discrimination in employment and (2) implementation of Affirmative Action measures.

9.1.1 Prohibition of Unfair Discrimination

All employers are required to take steps to promote equal opportunity in the workplace. This shall be done by eliminating unfair discrimination in all employment poli-

¹⁸⁷ Employment Equity Act, chapter 1 section 1

¹⁸⁸ Employment Equity Act, chapter 1 section 1

¹⁸⁹ Employment Equity Act, chapter 1 section 1

¹⁹⁰ Employment Equity Act, chapter 6 section 57

cies and practices.¹⁹¹ The definition of employment policy or practice, given in the first chapter of the Act, is extensive:

“Employment policy or practice includes, but is not limited to--

- a. recruitment procedures, advertising and selection criteria;
- b. appointments and the appointment process;
- c. job classification and grading;
- d. remuneration, employment benefits and terms and conditions of employment;
- e. job assignments;
- f. the working environment and facilities;
- g. training and development;
- h. performance evaluation systems;
- i. promotion;
- j. transfer;
- k. demotion;
- l. disciplinary measures other than dismissal; and
- m. dismissal.”¹⁹²

Further, the Act prohibits unfair discrimination. No person may unfairly “discriminate, directly or indirectly, against an employee, in any employment policy or practice, on one or more grounds, including race, gender, sex, pregnancy, marital status, family responsibility, ethnic or social origin, colour, sexual orientation, age, disability, religion, HIV status, conscience, belief, political opinion, culture, language and birth.”¹⁹³ Harassment of an employee is judged as unfair discrimination as well. All these protective regulations also apply to applicants for employment.¹⁹⁴

The Employment Equity Act prohibits unfair discrimination. This can seem to contradict with the affirmative action measures that are imposed by the Act. To avoid this to become an issue, the Act states that measures taken in pursuit of affirmative action do not constitute unfair discrimination.¹⁹⁵

9.1.2 Affirmative Action

Every designated employee must implement affirmative action measures for people from designated groups in order to achieve employment equity. An employer that is

¹⁹¹ Employment Equity Act, chapter 2 section 5

¹⁹² Employment Equity Act, chapter 1 section 1

¹⁹³ Employment Equity Act, chapter 2 section 6

¹⁹⁴ Employment Equity Act, chapter 2 section 3 + 9

not a designated employer may notify the Director-General of the Department of Labour, that it intends to voluntarily comply with the Act as if it were a designated employer.¹⁹⁶

Affirmative action measures are defined as “measures designed to ensure that suitably qualified people from designated groups have equal employment opportunities and are equally represented in all occupational categories and levels in the workforce of designated employer.”¹⁹⁷

Section 15 (2) is one of the most central ones in the Act, it reads as follows:

“Affirmative action measures implemented by a designated employer must include--

- a. measures to identify and eliminate employment barriers, including unfair discrimination, which adversely affect people from designated groups;
- b. measures designed to further diversity in the workplace based on equal dignity and respect for all people;
- c. making reasonable accommodation for people from designated groups in order to ensure that they enjoy equal opportunities and are equitably represented in the workforce of a designated employer;
- d. subject to subsection (3), measures to--
 - i. ensure the equitable representation of suitably qualified people from designated groups in all occupational categories and levels in the workforce; and
 - ii. retain and develop people from designated groups and to implement appropriate training measures ...”

An important clarification regarding the measures referred to in subsection (2) (d) above is that they include preferential treatment and numerical goals, but exclude quotas.¹⁹⁸

Further, nothing in the section above, section 15, “requires a designated employer to take any decision concerning an employment policy or practice that would establish an absolute barrier to the prospective or continued employment or advancement of people who are not from designated groups.”¹⁹⁹

¹⁹⁵ Employment Equity Act, chapter 2 section 6 (2a)

¹⁹⁶ Employment Equity Act, chapter 3 section 13-14

¹⁹⁷ Employment Equity Act, chapter 3 section 15

¹⁹⁸ Employment Equity Act, chapter 3 section 15 (3)

¹⁹⁹ Employment Equity Act, chapter 3 section 15 (4)

In addition to the factors stated in section 15, the following aspects are taken into account when determining whether a designated employer is implementing employment equity in compliance with the Employment Equity Act:

- “a. The extent to which suitably qualified people from and amongst the different designated groups [black people, women and people with disabilities] are equitably represented within each occupation category and level in that employer’s workforce in relation to the--
 - i. demographic profile of the national and regional economically active population;
 - ii. pool of suitably qualified people from designated groups from which the employer may reasonably be expected to promote or appoint employees;
 - iii. economic and financial factors relevant to the sector in which the employer operates;
 - iv. present and anticipated economic and financial circumstances of the employer; and
 - v. the number of present and planned vacancies that exist in the various categories and levels, and the employer’s labour turnover;
- b. progress made in implementing employment equity by other designated employers operating under comparable circumstances and within the same sector;
- c. reasonable efforts made by a designated employer to implement its employment equity plan;
- d. the extent to which the designated employer has made progress in eliminating employment barriers that adversely affect people from designated groups; and
- e. any other prescribed factor.”²⁰⁰

For the purpose of the Act, it is stated that a person may be suitably qualified for a job as a result of that person’s formal qualifications, prior learning, relevant experience or capacity to acquire, within a reasonable time, the ability to do the job. When determining whether a person is suitably qualified, the employer must determine whether the person has the ability to do the job in terms of any one of, or any combination of these factors. In making this decision, an employer may not discriminate against a person solely on the ground of a person’s lack of relevant experience.²⁰¹

The affirmative action measures shall ensure that suitably qualified people from designated groups have equal employment opportunities and are equitably represented

²⁰⁰ Employment Equity Act, chapter 5 section 42

in all occupational categories in the workforce. For this purpose designated employers must conduct analysis of employment barriers, which adversely affect people from designated groups. This shall be done in consultation with all their employees, through their trade union, or, in the absence of a union, with representatives nominated by the employees. Employment barriers can for instance be found in employment policies, practices, procedures or in the work environment. In order to determine the degree of under-representation of people from designated groups in various occupational categories and levels, this analysis of employment barriers must include a profile of the designated employer's workforce within each occupational category and level.²⁰²

9.1.3 Employment Equity Plan

One of the tools used for achieving equity on the labour market is the employment equity plan that all designated employers must prepare and implement. The employment equity plan is meant to secure reasonable progress towards employment equity in the employer's workforce.

The plan shall be prepared in consultation with the employees, in the same manner as described above. Implementation of the employment equity plan shall be discussed, as well as an annual report on the progress made in the implementation of this plan. The report shall include a statement on the remuneration and benefits received in each occupational category and level of the employer's workforce. The report is to be sent to the Director-General of the Department of Labour, and public companies must publish a summary of the report in their annual financial report.²⁰³

The equity plan must state the objectives to be achieved and what affirmative action measures that are to be implemented by the employer for each year of the plan. If under-representation of people from designated groups has been identified by the analysis, numeric goals, a timetable and the strategies to achieve equitable representation shall be stated. The plan shall also include a timetable for achievement of goals and objectives other than numeric goals.²⁰⁴

The plan shall state procedures and responsible persons to monitor and evaluate both the implementation of the plan and whether reasonable progress is being made towards implementing employment equity. The internal procedures to resolve any dis-

²⁰¹ Employment Equity Act, chapter 3 section 20 (3-5)

²⁰² Employment Equity Act, chapter 3 section 16,17,19

²⁰³ Employment Equity Act, chapter 3 section 16-17 + 20-22 + 27

²⁰⁴ Employment Equity Act, chapter 3 section 20

putes regarding the plan shall also be stated. The duration of each Equity plan should be for a period of no less than a year and no longer than five years.²⁰⁵

All employers, not only the designated ones, have a duty to display a notice informing its employees of the provisions of the Employment Equity Act. The designated employers must also display the most recent report submitted to the Director-General of the Department of Labour.²⁰⁶

9.1.4 Enforcement

A Commission for Employment Equity, with representatives of various interests such as labour, business etc, is established by the Act. Among other functions, the Commission is to advise the Minister of Labour regarding the issuance of codes of good practice, regulations, policies and other matter concerning this Act.²⁰⁷

Labour Inspectors have authority to enter, question and inspect any workplace or any other place where an employer carries on business or keeps employment records. If the inspectors have reasonable grounds to believe that the employer has failed to comply with the Act, they can request a written undertaking from a designated employer. If the employer refuses to make this written undertaking, or fails to comply with it, the Labour Inspectors may issue a compliance order. Should the designated employer not follow the compliance order, the Director-General may apply to the Labour Court to make it an order of the court.²⁰⁸

The Director-General may also conduct a review to determine whether an employer is complying with the Act. In doing so, he can request the employer to submit different records and request a meeting with an employer, employee or trade union. Failure to comply with requests or recommendations by the Director-Generals can be referred to the Labour Court.²⁰⁹

Disputes concerning unfair discrimination shall be referred to CCMA, the Commission for Conciliation, Mediation and Arbitration. If the dispute remains unsolved after conciliation, any of the parties in the dispute may refer it to the Labour Court for adjudication. The dispute may also be solved through arbitration if the parties are consent.²¹⁰ If the Labour Court decides that an employer has unfairly discriminated

²⁰⁵ Employment Equity Act, chapter 3 section 20

²⁰⁶ Employment Equity Act, chapter 3 section 25

²⁰⁷ Employment Equity Act, chapter 4 section 28-30

²⁰⁸ Employment Equity Act, chapter 4 section 35-37 (1+6)

²⁰⁹ Employment Equity Act, chapter 4 section 43 + 45

²¹⁰ Employment Equity Act, chapter 2 section 10 (2+6)

against an employee, the Court may make any appropriate order that it finds just and equitable. This may include payment of compensation and damages by the employer to the employee, an order to the employer to take steps to prevent the same unfair discrimination or a similar practice occurring in the future or directing an employer who is not a designated employer to comply with the Act as if the employer was designated.²¹¹

The burden of proof is placed on the employer, who has to justify any action that is alleged to be unfair discrimination.²¹²

The Labour Court has power to, among other sanctions, award compensation and damages in any circumstances contemplated in the Act, order compliance and impose fines for contravention of certain provisions of the Act.²¹³ The fines range from R500 000 for the first contravention to R900 000 for four previous contraventions in respect of the same provision within three years.²¹⁴

Critique on the Law

The Employment Equity Act are by some critics regarded as a “... new version of statutory discrimination ...”²¹⁵ The Act has been accused of re-introducing the abominated principles used by the former ruling nationalist party government, such as job reservation, re-introduction of racial classification and discrimination on a massive scale.²¹⁶

Critics against the affirmative action aspect of the Employment Equity Act have claimed that the Act will lower standards on the workforce. This criticism is opposed by others who mean that the Act does not oblige any employer to appoint anyone who is not suitably qualified, and standards will therefore not be lowered by affirmative action. Throughout the Act the term ‘suitable qualified people’ is used to describe an applicant’s suitability for the job. The term is thoroughly explained in the Act, as previously described, and the essence of it is that an employer may not turn an applicant down solely on the ground that he or she lacks formal qualification for the job. If a person has the ability to do or learn to do the job, then he or she shall be taken for qualified.

²¹¹ Employment Equity Act, chapter 5 section 50 (2)

²¹² Employment Equity Act, chapter 2 section 11

²¹³ Employment Equity Act, chapter 5 section 50 (1)

²¹⁴ Employment Equity Act, schedule 1

²¹⁵ Affirmative action - Renaissance rules, OK?, Finance Week, 18 August 2000

²¹⁶ Sibiyi storms out of forum after address, Business Day, 1 November 2000

From this the conclusion can be made that employers will not have to employ people that are not qualified to do the job, but they might have to employ job applicants that are not the most merited ones in order to meet the objectives in their employment equity plan. From the perspective that the most merited ones might be passed in order to achieve equitable representation in the workforce, standards can be seen as lowered.

Another argument from critics against affirmative action is that the Act introduces quotas, fixed targets and keeps focus on race. This criticism can be dismissed as the Act explicitly excludes quotas to be used. Nor does the law require fixed targets. Each workplace sets its own targets, after consultation with employees and trade unions. When targets are set the circumstances of each workplace must be taken into account, together with the demographic profile, pool of suitable qualified people, economic circumstances of the employer etc. (Please see above for further information). In this the Act allows for flexibility.

It is true that Affirmative Action keeps focus on race, but the negative aspect of this is generally considered to be outweighed by the great need for affirmative action. It can also be noted that affirmative action includes all but white non-handicapped men, approximately 7% of the population.²¹⁷

9.2 Skills Development Act (No 97 of 1998)

The *Skills Development Act* provides an institutional framework to devise and implement national, sector and workplace strategies to develop and improve the skills of the South African workforce.²¹⁸

The purpose of the Act is to increase the levels of investment in education and training of the labour force, to improve the employment prospects of persons previously disadvantaged by unfair discrimination and to redress the disadvantages through training and education. Employers shall be encouraged to use the workplace as an active learning environment, to provide the employees with the opportunities to acquire new skills, to provide opportunities for new entrants to the labour market to gain work experience and to employ persons who find it difficult to find employment.²¹⁹

²¹⁷ The high percentage (93%) that is included in the target group for Affirmative Action can initially make one wonder why it is needed. From another point of view, the fact that Affirmative Action measures are taken to promote 93% of the population shows the strong domination by the rest.

²¹⁸ Skills Development Act, No 97, 1998, preamble

²¹⁹ Skills Development Act, chapter 1 section 2

The definition of an employee in this Act is the same as in the Employment Equity Act. A worker is defined as an employee, an unemployed person or a work-seeker.²²⁰

The Act establishes the National Skills Authority and the National Skills Fund and provides for the establishment of Sector Education and Training Authorities (SETAs).

The functions of the National Skills Authority are, among others, to advise the Minister of Labour (the Minister) on regulations to be made, to liaise with SETA on different skills development policies and strategies, to conduct investigations and report on the progress made in the implementation of the national skills development strategy. Members of the Authority are appointed by the Minister to represent interests from labour, business, the community and development interests as well as the State.²²¹

There are several Sector Education and Training Authorities, 24 at the moment.²²² They are set up for specific economic sectors, determined by the education and training needs of employers and employees in similar categories of businesses. The potential for coherent occupational structures and career planning as well as the financial and organisational ability of the proposed sector to support a SETA are other issues taken into consideration.²²³

The function of a SETA is to develop and implement a Sector Skills Plan by establishing learnerships, approve workplace skills plans, allocate grants to employees, employers and education and training providers, and monitor education and training in the sector. Furthermore, they are to collect and disburse the Skills Development Levies (described below) in their sector. The SETAs are to liaise with the National Skills Authority and report to the Director-General of Labour. Every SETA consists of representatives from labour, employers and relevant government departments and might also include other interested parties if the Minister of Labour considers it appropriate.²²⁴

Employers may develop a Skills Programme for their workforce and can thereafter apply to their SETA for a grant or the Director-General of Labour for a subsidy. A Skills Programme is defined as a programme that is occupationally based, will constitute a credit towards a qualification registered in terms of the National Qualification Framework when completed, uses training provider accredited by a body con-

²²⁰ Skills Development Act, chapter 1 section 1

²²¹ Skills Development Act, chapter 2 section 5-6

²²² <http://www.labour.gov.za> 2001-05-20

²²³ Skills Development Act, chapter 3 section 9

templated in the South African Qualifications Authority Act or complies with the prescribed requirements.²²⁵

9.2.1 Enforcement

For monitoring and enforcement of the Act, Labour Inspectors have authority to conduct inspections, enter workplaces and any other place where an employer carries on business or keeps employment records, require information disclosure, copy records, issue compliance orders etc. Permissible fines that may be imposed for failure to comply with the Act, not involving underpayment, range from R100 to R500 per employee, depending on whether there are previous failures to comply with the same provision within 3 years.²²⁶

The Labour Court has jurisdiction in respect of matters arising from the Act. It constitutes an offence to obstruct or attempt to influence improperly a person who is performing a function in terms of the Act, to obtain or attempt to obtain any prescribed documents by means of fraud, false pretences or by submitting a false or forged prescribed document, or to knowingly furnish false information. The penalty for a person convicted of an offence ranges from fines to imprisonment for a period not exceeding one year.²²⁷

9.3 Skills Development Levies Act (No 9 of 1999)

The *Skills Development Levies Act* provides for the imposition of a skills development levy on employers. All employers with very few exceptions must pay this levy. For instance, if the total amount of remuneration paid or payable by an employer to all its employees does not exceed R250 000 during the following 12 months and that the employer is not required to apply for registration as an employer according to the Income Tax Act, then the levy does not have to be paid. Religious or charitable institutions do not have to pay the levy, either. The levy is 1% of the leviable amount, by which is meant the total amount of remuneration, paid or payable, or deemed to be paid or payable, by an employer to its employees during every month. Pension, superannuation allowance, retiring allowance etc shall not be included in the leviable amount.²²⁸

²²⁴ Skills Development Act, chapter 3 section 10-11

²²⁵ Skills Development Act, chapter 5 section 20

²²⁶ Skills Development Act, chapter 8 section 32

²²⁷ Skills Development Act, chapter 8 section 31, 33-34

²²⁸ Skills Development Levy Act, No 9, 1999, chapter 1 section 3-4

Every employer who is liable to pay the levy must register for the payment of the levy with the Commissioner for the South African Revenue Service and indicate within which Sector Education and Training Authority the employer is to be classified.²²⁹ The collected levies, penalties and interests are paid into the National Revenue Fund. 20% of the collected amount is allocated in the National Skills Found, established by the Skills Development Act, and the rest, 80%, is distributed to the relevant SETAs that the employers have indicated on the registration form.²³⁰ The money in the fund is to be used in projects identified in the National Skills Development Strategy as national priorities.²³¹

If the skills development levy is not paid in due time, a penalty of 10 per cent of the unpaid amount is payable in addition to interest.²³²

Similar to the Employment Equity Act, Labour Inspectors are used to monitor and enforce the compliance with the Act. They may, without warrant or notice, enter any workplace or other place, which is not a home, where an employer carries on business or keeps any records. By consent of the owner or occupier, or by a warrant, the inspectors may enter a home and any other place as well. The Labour Inspectors may require persons to disclose information under oath or affirmation, inspect and take copies of any document of interest regarding this Act, require producing of documents and perform any other prescribed function necessary for collection of the levy. They may issue compliance orders as well.²³³

Any person who fails to apply for registration, pay the levy, knowingly furnishes false information, or fails to submit or deliver documents, disclose information, attend and give information, hinders or obstructs any person in carrying out his or her functions in terms of the Act, commits an offence. A fine or imprisonment for a period not exceeding one year is the sanction on conviction. The burden of proof that the information supplied by the employer in statements is accurate is put on the employer.²³⁴

9.3.1 Disbursement of Grants

The intention of the Skills Development Act and Skills Development Levy is to stimulate skills development by enabling employers to reclaim some expenditure on

²²⁹ Skills Development Levy Act, chapter 1 section 5

²³⁰ Skills Development Levy Act, chapter 1 section 8

²³¹ Skills Development Act, chapter 7 section 27-28

²³² Skills Development Levy Act, chapter 1 section 12

²³³ Skills Development Levy Act, chapter 2 section 15-17 + 19

²³⁴ Skills Development Levy Act, chapter 3 section 20 + 21

skills development initiatives. The disbursement of grants is proportional to the levy that has been paid by the employer.²³⁵ There are several levels of grants, with different requirements to be fulfilled. The relevant SETA has further information on this.

A SETA may also pay a grant towards the cost of a learnership, and pay an allowance to learners at workplaces.²³⁶

10 CONCLUSIVE REFLECTIONS

Introduction

In this chapter we will describe and analyse some attitudes and problems connected to black economic empowerment. Focus will be on affirmative action, window-dressing and skill shortage.

10.1 General Aspects

The optimists of BEE claim that there has never been such a speedy transfer of economic assets from one racial group to another in the history of world economy. At the same time, pessimists claim that black economic empowerment seems more like a sham. One black businessman has described it as a huge con job: “The financial institutions have only leased these assets to us. They will soon be coming back to reclaim possession of what is theirs.”²³⁷

Economic growth, or the lack thereof, is often discussed at the same time as black economic empowerment. Some argue that economic growth will be achieved only if government policies regarding affirmative action, general redress and equality are repealed and if, by extension, business is allowed to pursue profit without hindrance. Others argue that it will be achieved only if the previously marginalised persons are roped into the mainstream and redistribution of wealth is taking place. There are many aspects to both these opinions. What one must keep in mind is that affirmative action, and other legislation that is criticised, are there to change the economic complexion of the country and deepen the democracy, by ensuring that black people take part in creating the country’s growth and shaping its future.²³⁸ Hence, the question is not only whether empowerment generates growth more than growth would deliver

²³⁵ What employers need to know about the Skills Development Levy, leaflet from Department of Labour

²³⁶ Regulations concerning the Registration of Intended Learnerships and Learnership Agreements, section 3 (6)(b)i,ii, issued in terms of Section 36 of the Skills Development Act

²³⁷ Still Not Happening, Financial Mail, 24 September, 1999

²³⁸ In search of a common economic foundation, Business Day, 8 November 2000

empowerment. It is a question of democracy, getting rid of the yoke of apartheid and of fulfilling the expectations that was created by the election manifesto and the new democratic order.

The efficient functioning of the market in South Africa is described to be distorted by racism, which remains fundamentally ingrained across all sectors of the society. Out of this perspective, black economic empowerment is believed to be necessary in order to create a non-racist, efficiently functioning market.²³⁹

The government of South Africa regards black economic empowerment not only as an instrument to achieve empowerment for the historically disadvantaged individuals (HDIs), but also as a tool to integrate the South African society into the surrounding global environment. To be competitive on the international market, it is not feasible to have the majority of the population outside the economy. Human capital and entrepreneurship are crucial for a country's competitiveness, especially in the new economy. Out of this aspect, empowerment is not only a matter of equity, it is a matter of South Africa's survival in the global context.²⁴⁰

Critics often take the view that black economic empowerment has resulted in black enrichment instead of empowerment. Enrichment has and is certainly taking place, which is why black economic empowerment sometimes is said to be working only in favour of those who wants to be 'filthy rich' and do not care about the rest of the society. This view is opposed by others arguing that despite the flaws, which were mostly connected to the first generation of empowerment, black success stories have had an important psychological role for the black community. The success of some black businessmen have inspired the rest of the black population and dispelled the illusion that business success is a whites' phenomenon only.²⁴¹

The instant achievers have served as role models in this evolution. You have to start somewhere. Total dismissal of black economic empowerment because a few people have enriched themselves in the beginning of the process is harsh. Black economic empowerment aims at changing the conditions for living for the big masses in South Africa, which is a process that needs time to give result.

²³⁹ BEE moves to phase two, *Enterprise*, October 2000

²⁴⁰ Dr Themba Mhlongo, Chief Director: Industry & Technology Strategy, Department of Trade and Industry, interview 28 November 2000

²⁴¹ TIPS Annual Forum "Growth and Investment in South Africa", Johannesburg, 21 September 1999, Panel - National economic empowerment, <http://www.tips.org.za/events/proceedings/bee.html> 2001-07-11

You have to bear in mind that the first few years after the democratic elections were coloured by private companies eager to attain a politically correct ownership structure. These first empowerment operations had no regulatory guidance from the government side. For example, it took a long time before the government issued clear empowerment criteria for the procurement procedures that the companies could follow. Thus, the empowerment that took place during the first years was not controlled by the government and can therefore not be taken as evidence of that the government's empowerment endeavours only work for the few.

The past years can be seen as a learning period for the government. The South African government is regarded as good at creating policies but not as good at implementing them. They need to walk the talk, as someone has expressed it. The government has received heavy criticism for the lack of monitoring of its various programmes. To evaluate the effect, or lack thereof, of different programmes and initiatives is almost impossible due to the lack of adequate statistics.

The informal sector in the country is large. This is caused by the inherited apartheid system and creates several problems for the new government. Many people are not in the registers, they have no permanent address and they earn too little money to pay tax. The tax base in South Africa is only about 30 percent.

One problem in the new South Africa is the so called 'expectation problem' - the growing disillusionment and anger of the millions of Africans who expected that their problems would vanish once political freedom was achieved and the apartheid system was defeated. For this group of people the process has been too slow. At the same time, the change has been perceived to be too fast and is seen as a threat by those who were previously advantaged.²⁴² White people have fears and black people have expectations. This puts the government in a very tough position. The black population constitutes the majority of voters, whereas the white population represents most of the economic power in the country. In order to succeed both as a government and with black economic empowerment, the government needs support from the whole population. The government has a difficult role in trying to balance the different interests. It is essential that the capacity of the whites remains in South Africa, as well as it is essential that those previously disadvantaged are advanced as quickly as possible. Therefore, the government, and the corporate world, have to find a way to advance the disadvantaged, seemingly at no cost to the advantaged. This needs to be

²⁴² The impact of black economic empowerment initiatives, Accountancy and Finance Update, August 1997

done in a time period during which the disadvantaged will not lose patience, but at the same time at a rate that will retain tolerance among the advantaged. South Africa's future may be determined by how well this balancing act is handled by the government.²⁴³

Political freedom for all South Africans was gained by the first democratic elections in 1994. Black economic empowerment aims at achieving economical freedom. The government is believed to have underestimated the challenging process from political freedom to economical freedom.

Black economic empowerment is an enormous task for the government to take on. One has to keep in mind that the previous government provided for only 13 percent of the population and the present government provides for 100 percent of the population. The nature of the South African economy has been described as “[i]t is premised on the view, and has been for the last 100 years, that a modern industrial economy can be run effectively by 5 percent of the population for the benefit and advancement of 12.8 percent of the population while ignoring the other 87 percent.”²⁴⁴

While the income gap between whites and blacks has narrowed, there is now a growing gap between the earnings of high- and low-income black people. Thereby, the political debate has increasingly changed from being a race issue to a class issue.

Legislation created in order to achieve black economic empowerment keeps the focus on race. Some people, who mean that it constitutes reverse racism and is based on the same methods as the abolished apartheid system, see this as negative. Nevertheless, to remedy a racial issue, the same tools need to be used if results are to be achieved within a reasonable time. A system that recognises the history for what it is, is needed in order to correct it. There are huge inequalities in South Africa, due to its racist history. It would be naive to say that all groups of people are on the same level now that the statutory discrimination has been repealed.

The government implements black economic empowerment legislation and policies with the ambition to create a non-racial society. To address a problem through legislative measures may have the opposite effect than was intended, though. The problem becomes more of a legislative issue, which can dampen the public debate. By setting legal requirements on a certain level, there is also a risk for a minimum approach. If

²⁴³ CDE debate 19 May 1998, Affirmative action: Is South Africa heading down a route which many African Americans are rethinking? <http://www.cde.org.za/debates/debate10.asp> 2001-07-11

²⁴⁴ Qunta, Christine in: SA not ready for the global stage, says the BMF, The Star, 25 October 2000

the law says x percent, x percent is what will be performed and nothing more. Pressure, as well as incentives, through legislation is the only feasible option to secure results in certain areas. If the accomplishment of black empowerment would be left to the market, the process would be too slow. It is wishful thinking to believe that the market would make a speedy correction of itself out of moral beliefs or a sense of social responsibility.

South Africa's history of apartheid is still close by. People, both black and white, have practically lived their whole lives segregated and under different conditions and possibilities. It takes a lot of courage and willingness to re-evaluate your view of the world that you have been fostered into. Time is needed - perceptions and mind-sets could need generations to change.

10.2 Affirmative Action

In South Africa, affirmative action takes place in what once was the most structured racist society in the world, now in the process of deracialisation. This makes the character of affirmative action in South Africa unique compared to affirmative action that has taken place elsewhere. Rather than aiming to create opportunities for a minority, as it is usually used for, affirmative action in South Africa aims at transforming an economy that for many years barred the majority of the population from any meaningful role.

Affirmative action is resented by some of the beneficiaries of the previously legislated advantages. They consider it to be reverse racial discrimination, contradicting the ANC promise of colour-blind non-racialism. While the ANC government views more equitable representation through affirmative action policies as a precondition for successful nation-building, opponents perceive the policy of affirmative action as undermining national reconciliation.²⁴⁵

White young people of today sometimes claim that they have to bear the burden of the historical wrongs against the black population. The purpose of affirmative action is not to punish those who were privileged in the apartheid system, but to admit that many people are wrongfully excluded from several areas in the society due to suppression and denial of equal opportunities in the past. Affirmative action is a way to address and come to terms with this in an active way. The fact is that almost all white people, regardless their attitude to racism, benefited from the institutional racism

²⁴⁵ Adam, Kanya, Affirmative Action and Popular Perceptions: The Case of South Africa, Society, Jan/Feb 2000

that was practised in South Africa. White South Africans need to accept that racism was not eradicated by the new dispensation, that it still is embedded in the country's society and needs to be addressed.²⁴⁶ It is easy to hold the view that bygones should be bygones if you are from the privileged group.

During the first phase of empowerment parallel positions were created; Black people, without the qualifications needed, were recruited to managerial positions, while white people continued to run the business. This was done to open doors for government contracts or to score public relations points. The use of parallel positions has led to the misconception that affirmative action is about putting incompetent black people in positions they cannot handle. This kind of conduct does not constitute true affirmative action. The essence of affirmative action is to recognise the people who have suitable ability and training, and assist them in gaining positions in business life that they were previously denied.²⁴⁷

A negative effect of affirmative action may be that it could lead to a perception of entitlement among the previously disadvantaged. They do not see that they still have to shape their own future, rather they expect the new system to deliver it to them. This creates a lot of frustration. Another downside is that affirmative action is said to stigmatise the beneficiaries of affirmative action, by implying that they cannot compete on equal basis. People in the affirmative action category may come to question their value and wonder if they succeeded on their own merit, or whether their sex or race explains their success. The assumption of being a product of affirmative action is likely to be applied to all blacks that have attained positions, whether it would be with or without the aid of affirmative action.²⁴⁸

In the interviews we conducted in South Africa, we raised the issue of whether affirmative action measures should have a so-called sunset clause, limiting the time for using affirmative action. Its termination could either be set by a timeframe or be linked to the achievements of certain goals. Most people we met reject this idea, whereas some people think that it might be good in that the government would have to play with open cards regarding its full objectives. The latter group thinks that the introduction of a sunset clause could slow down the brain-drain from South Africa and to a certain extent open for a more foreseeable political situation. At the same time, if the new government in 1994 would have introduced for example an employ-

²⁴⁶ Racism, confidence and the economy, Finance Week, 8 September 2000

²⁴⁷ Hell for Blacks Too? Financial Mail, 21 February 1997

²⁴⁸ Adam, Kanya, Affirmative Action and Popular Perceptions: The Case of South Africa

ment equity programme with a sunset clause, stating certain levels that had to be achieved within a specific time period, most white South Africans are believed to have protested and moved away. As it happened, the process allowed changes to slowly sink into peoples' minds over time. Subsequently, most white South Africans have come to accept the affirmative action process.

An introduction of a sunset clause is knowingly not on the government's agenda today, but it can be interesting to speculate on the effect such a clause would have on the process. The need for a time frame has to be based on the assumption that affirmative action seriously affects the possibilities for white persons, though.

10.3 Window-Dressing

Window-dressing, fronting and rent-a-black, are all definitions of the same kind of conduct, namely when black business-people are lending their faces and fronting for white businesses. They are invited at equity level to give the company an artificial black empowerment profile. This creates a lot of problems. Most often the black shareholder does not get involved at operational level. The business is still run by white managers, which means that there is no managerial skills transfer to blacks. The biggest damage is made as companies that practice window-dressing compete with real black empowerment companies under the empowerment banner. The black entrepreneurs, who most often are operating under tougher conditions than the white businesses, are the big losers.²⁴⁹ It is completely undermining the affirmative procurement policies and other empowerment ambitions designed to develop black operational capacity and economic growth.

10.3.1 Why do Companies Practise Window-Dressing?

When you look into the reasons why companies practise window-dressing, many explanations are given. One is that empowerment is seen as a pure cost. Money decides and window-dressing will therefore happen as long as you can get away with it. Another reason is lack of time. There is time pressure to make the management level look good. Sometimes window-dressing is said to occur because it is hard to find professional black people.

Those who oppose these arguments mean that window-dressing is an evidence of white companies attempts to exploit and circumvent empowerment regulations out of reluctance to transfer economical power to black people. From this perspective, pure

²⁴⁹ Black Empowerment Engine Not in GEAR, Financial Mail, 13 November 1998

racism is the ground. The argument that professional blacks are hard to find is countered by the argument that companies do not look in the right places. Companies are blamed for lacking dedication and for not putting efforts in to find suitable qualified people as affirmative action employees. The thinking is believed to be more of 'we need a black face, lets get it over and done with'. There is also a suspicion that companies willingly employ incompetent black people to prove that affirmative action does not work.

The focus on equity ownership during the first phase of empowerment made window-dressing a lucrative and relatively easy way to acquire the needed empowerment status. In today's South Africa window-dressing will become expensive in the long run, at least if the company is labour intense. The new labour legislation puts a growing number of requirements on companies to employ historically disadvantaged individuals. Meeting these requirements by creating parallel positions is costly.

Window-dressing would not exist without black people willing to participate in that kind of conduct. The reasons for their participation are several. One of the major reasons is, of course, the common human desire for fast and easy money. Added to this, many of the so-called historically disadvantaged individuals feel entitlement. They have been excluded and deprived for so long and cannot wait to get wealthy. The ones that have got a job may be exposed to huge financial pressure from the extended families and feel responsibility to take care of them.

Historically disadvantaged individuals that have acted as front figures have been discredited and accused of being disloyal to the rest of the community. To refer to moral obligation as a reason not to participate in window-dressing is naive. It takes a lot to turn lucrative offers down. If there are business opportunities, most people would take them. One can also wonder why the black peoples' business operations should be more steered by moral obligations than others'.

10.3.2 Governments Role in Window-Dressing

The government can partly be blamed for the window-dressing that has occurred. Organisations that are created in a certain system will reflect the opportunities provided by the institutional framework in that system. If piracy is rewarded, then piratical organisations will come into existence.²⁵⁰ The practice of window-dressing and alike conducts has been possible since the government's monitoring of empowerment is weak. The intention is there, and some state entities' monitoring practices are better

than others'. Still, there is room for companies to have a superficial empowerment profile.²⁵¹ Trade and Industry Minister Alec Erwin has admitted that the government has not been sufficiently well organised and co-ordinated to ensure a systematic implementation of the programmes for affirmative procurement, and agrees that a great deal of work still has to be done to co-ordinate the various government departments.²⁵²

The government has also been accused for acting hypocritically at times. When acquiring goods and services the government wants the job to be done by an empowerment company, at the same time as they require the job to be done fast and with major resources. As empowerment companies often lack the resources and experiences needed, especially for larger contracts, a white firm, with a subcontract or a joint venture with an empowerment company, is therefore contracted to take full responsibility for the job. Thus, the government is said to exclude the empowerment companies from the bidding scene through its requirements on the bidders' operational capacity.

10.4 Skills Shortage

As a result of the apartheid educational system, the market of well-educated black South Africans is not only small, but also skewed. For example, there is a significant lack of black people with technical degrees. Due to the demand on black professionals, fully trained black people are much more expensive than their white counterparts. The very active headhunting industry creates problems for companies that put time and money into training staff.²⁵³

This affects the government as well. South Africa's Finance Minister Trevor Manuel has claimed that black professionals are pricing themselves out of the economy and that the government finds it difficult to deliver services because the skills needed from black people are unaffordable.²⁵⁴

The so-called epidemic of job-hopping by blacks is not only caused by headhunting, some argue. Many black people are said not to leave because of a better offer but out of frustration. Colleagues that are afraid of interacting with them, feelings of alienation, distrust in their ability, difficulties to reach their full potential or to advance

²⁵⁰ BEE the missing factor, Enterprise, June 2000

²⁵¹ BusinessMap, Empowerment Guidelines, p 5f

²⁵² Corporate empowerment review, Business Day, 11 May 2000

²⁵³ The Price of the Black Skills Shortage, Head-hunters on the Prowl, Financial Mail, 21 February 1997

²⁵⁴ Empowerment body want policies revised, Business Day, 02 October 2000

within their organisation are issues that are far more often said to be the reason for job hopping.²⁵⁵

The skills shortage is also caused by 'brain drain'. Many well-educated white people have left the country in the last years. Statistics are poor and therefore different numbers and reasons for the brain drain are presented. Many white people are said to have left out of fear for what would follow after the political changes in the country in 1994. The high crime rate, declining standards and services and the turbulence in the educational system are other reasons given. Some are said to leave for the sake of their children - they do not believe that they will have a good future in South Africa.

Some people think that white South Africans leave due to racism. The individualistic culture among western people is also said to be the reason for white South Africans to leave. Furthermore, white people are believed to be leaving since they are not getting the same privileges as during the time of apartheid. On the other hand, others argue that brain-drain in South Africa is overplayed and is more of a threat than an event.

When you discuss brain-drain, you have to keep in mind that we live in an increasingly globalised world with mobility of people, capital and technology. It is an international trend that people with globally accepted higher degrees are more mobile than ever before. What is viewed as brain-drain in South Africa can probably partly be explained as a natural consequence of the country's newly acquired acceptance in the world society.

11 FUTURE

Introduction

In this chapter, we will discuss the future prospects of black economic empowerment. The chapter is based on our interviews, debates in the media, as well as our own view on the future course of black economic empowerment.

11.1 The Future of Black Economic Empowerment

There are indications of a shift towards a new phase of empowerment. The waterline between the second and third phase of empowerment may spring from the recently released, long-awaited BEE Commission's report on the present state and future of black economic empowerment.

²⁵⁵ Hell for Blacks Too? Financial Mail, 21 February 1997

Year 2000 saw the value of empowerment deals on the JSE slide back to same levels as in 1996.²⁵⁶ With unemployment among young black South Africans of about 40 percent and the black ownership on JSE estimated at less than 2 percent, it lies near at hand to see black economic empowerment as a failure. Especially when, at the same time, white South Africans, approximately 13 percent of the population, earn 44 percent of the country's net income.²⁵⁷

All sides do not share this view, though. The people decrying the slow advancement of BEE are blamed for seeing the transformation process too narrowly, ignoring the progress made by unlisted companies and the development that has taken place in the rural areas. To use a leading black businessman's words, "BEE has not been a failure. It has been a steep learning curve".²⁵⁸

Irrespective of which standpoint you have, black economic empowerment is becoming an increasingly significant political and economical issue in South Africa today.

Which way empowerment will take in the future is likely to be affected by the conclusions and recommendations made by the BEE Commission. As earlier presented in chapter 8, the BEE Commission advocates an interventionist strategy by the government, and calls for comprehensive legislative measures to accelerate development. Their view is supported by black businesses, which believe that South Africa might go the Zimbabwe route if the right gear for empowerment is not found.²⁵⁹

The government has shown doubt to the BEE Commission's strong reliance on the government to lead the empowerment process. Therefore, we believe that a considerable shift in the government's present role is not likely to follow. The government has a strong belief that the existing legislative framework will prove to be sufficient to serve the future empowerment process given adequate time.

When judging the progress of black economic empowerment up to date and giving suggestions on the appropriate way forward, the complex reality where the first empowerment initiatives were led off must be considered. Several good BEE initiatives came to nothing due to that the economical environment was not structurally geared to accommodate them. At the time, there was no regulatory framework to support and give structure to the process. When the framework started to be built, the

²⁵⁶ Past year gloomy for black empowerment, Business Day, 4 May 2001

²⁵⁷ Ramaphosa warns of backlash on economy, Business Day, 27 March 2001

²⁵⁸ SA launches index to measure black empowerment, Business Day, 16 May 2001

²⁵⁹ Hat-Trick Needed, Financial Mail, 29 September 2000

objectives were not fully clarified, leading to some government strategies fighting each other. It also deserves to be noticed that appropriate statistics still scarcely exists. Thus, the government lacks the basic tool for policy creation and evaluation.

With a newly introduced policy for the restructuring of State Owned Enterprises (SOEs) and legislation for affirmative procurement, these two areas are likely to be additionally emphasised in the future as the major deliverers of empowerment. Therefore, the pressure on the market to enter equity relationships with black companies in order to secure government contracts or ownership in restructured SOEs will continue. This is likely to increase the number of joint ventures and equity transactions between established firms and black companies.

The effect of the affirmative procurement policies will in the future not be limited to companies that deal directly with the state. Companies that have business with the state will be asked to show that their own procurement has a strong affirmative element. These requirements will put pressure on the companies' suppliers to have an appropriate empowerment status in order to secure contracts. As discussed in chapter 5.2.4, this is already the case in several SOEs. Therefore, companies with no direct business contact with the state also have to conform to the state's affirmative procurement regulations.²⁶⁰

In order to uniform and facilitate the evaluation of a company's empowerment status it is possible that the government will carry out the BEE Commission's recommendations on how to define a black, black empowered, black influenced and engendered company. However, the BEE Commission's proposal keeps the focus on equity ownership as a determining factor for a company's empowerment status. It is believed that, in the future, the empowerment status of a company will be determined by the composition of the company board and executive leadership, together with commitments and actions that conform to an empowerment profile, rather than the company's shareholder base.²⁶¹

The decreasing concentration on equity ownership that was seen during the second phase of empowerment is believed to continue. It is argued that the big masses cannot earn their living as shareholders, wherefore the government's focus should be kept in areas where significant results can be achieved, namely education and job creation.

²⁶⁰ BusinessMap, Empowerment Guidelines, p 5

²⁶¹ BEE – quest for more workable models, Enterprise, October 1999

The lack of access to financing is expected to continue to be the major obstacle for empowerment. Financial institutions are blamed for constituting the least transformed sector in South Africa and for not showing enough commitment to the apparently needed transformation of the society. The financial institutions dismiss the criticism with the motivation that they treat applications objectively and that their exposure for international competition hinders them from applying specific criteria for financing of empowerment activities. However objectively an application for a loan may be treated, financiers are asking for earlier business records, experience and securities, requirements that people who have been excluded from the economical sphere until recently hardly can meet. Consequently, the result is based on race and has the effect that it is very hard for black entrepreneurs to be granted financial means.

State driven financing initiatives have been introduced during the years to improve the empowerment companies' scarce access to capital. The results have thus far not fulfilled the expectations, and the government's financing programmes have been blamed for involving too much politics. It is increasingly argued that the private sector's contribution is needed in order to address the problem.

12 RECOMMENDATIONS TO COMPANIES

Introduction

We hope that this Thesis has been successful in conveying the essence of the complex transformation process taking place in South Africa. To make an elaborate study of black economic empowerment in a paper of this extent is not feasible, nor has it been our aim. We trust that the paper has helped to increase the reader's awareness of the importance to have a well thought-out BEE strategy for business operations in South Africa.

In this concluding chapter we will discuss the importance of choosing the right empowerment partner, BEE as a business imperative and transformation within the company.

12.1 The Choice of an Empowerment Partner

For a company operating in South Africa that intends to do business with public entities, an empowerment partner is often needed. The most adapted judicial form for an empowerment partnership must be decided out of every company's own conditions,

depending on the purpose, extent and permanency of the planned business operations in South Africa. Irrespective of the outer form for the collaboration, it is crucial to choose the right empowerment partner in order to be successful in South Africa.

Before entering a partnership with an empowerment company, it is of outmost importance to define for what purpose the collaboration is established, and to clearly express the value that is expected from the empowerment partner. Thereby, it is possible to avoid an inappropriate structure for the partnership and disappointments regarding the levels of involvement, value added and skills transfer.²⁶²

In the debate regarding window-dressing, the argument is often brought forward that it is difficult to find a suitable empowerment partner. This is probably the case in fields involving for instance high technology, whereas in other fields we have been told that the problem relates more to lack of commitment than to non-existence of good empowerment partners. A company looking for an empowerment partner should be conscious of the importance to devote time and resources to the selection process, and not start business relations with the first empowerment company that it gets in contact with.

When granting loans, financial institutions increasingly prefer empowerment companies, which have emerged from the bottom up – in other words, built an operational business as opposed to merely acting as an investment holding company.²⁶³ In our opinion, this approach is also recommendable for companies looking for an empowerment partner. However, when evaluating empowerment companies' experiences and track records, it should be born in mind that all empowerment companies are post-democratic. Companies that usually are classified as start-ups elsewhere can in the South African context be regarded as established ones.

12.2 Black Economic Empowerment – a Business Imperative

As the preceding chapters have aimed to convey, black economic empowerment affects all business operations in South Africa. The pressure to comply with the regulatory framework varies depending on the company size, field of business and the degree of business relations with state entities, as well as how labour intense the business is. The government has come a long way in laying the foundation and building a sustainable structure for the empowerment process to proceed on, and is increasingly challenging the business sector to embrace black economic empowerment.

²⁶² BusinessMap 1999, p 21

A company operating in South Africa decides its own approach in how to deal with BEE regulations and programmes, and thereby the degree of its contribution to the transformation process of the society. Since we do not consider non-compliance and circumvention to be an alternative, we identify the following levels of commitments for a company operating in South Africa:

- Formal and correct compliance with the empowerment regulations
- Active compliance with the empowerment regulations combined with voluntary initiatives, for example compliance with Employment Equity Act without being a so called designated employer (see chapter 9.1)
- To embrace black economic empowerment as a business imperative

The first two approaches are sufficient if the purpose is to comply with the BEE regulations, and to even show commitment to the process by active compliance. Whereas if successful long-term operation in South Africa is a part of a company's objectives, we assert that black economic empowerment should not be seen as a matter of complying with regulations and laws. It should constitute one of the company's core strategies.

12.2.1 Black Economic Empowerment as a Competitive Advantage

Conformity with black economic empowerment requirements will continue to grow in importance in dealings with the government in South Africa, as the government is emphasising black economic empowerment requirements in increasingly more aspects. As BusinessMap puts it; “[t]his presents established white-controlled domestic and foreign businesses with a stark reality; conform or don't bid for state business...”²⁶⁴

Companies who are dependent on contracts with state entities increasingly understand the importance to show commitment to the empowerment process. This cannot be said to be the case among companies with no direct business contact with the government or parastatals.

As discussed earlier in this paper, there are strong signs that the sphere of companies affected by various empowerment requirements is becoming wider. Today these requirements are put on the companies through government initiatives, but in the fu-

²⁶³ BusinessMap 1999, p 8

²⁶⁴ BusinessMap 2000, p 13

ture, we believe the major pressure to embrace black economic empowerment to come from the market.

In the same way as international market forces today can condemn a company for placing operations in countries with poor labour conditions or for neglecting environmental aspects in the course of business, we believe that the ability to demonstrate contribution to the transformation process will become crucial for a company's success in South Africa. Out of this perspective, the pressure will increase on companies to be regarded as socially responsible businesses, by BusinessMap defined as organisations that focus on their operation's impact on their employees and their social and environmental surroundings. This implies emphasis on concepts such as social auditing and social accountability to measure the full empowerment impact of a company's operations.²⁶⁵

Given the present lack of an unambiguous definition on the essence of empowerment and the relatively early state of the transformation process, the awareness of the market is most likely not to be expected in the near future. When the market's awareness has increased, we believe that the value of goodwill, bringing a competitive advantage, will be considerable for companies that can demonstrate a history of firmly established commitment to black economic empowerment. Especially as the future buying power will emerge from people subject to empowerment today.

This competitive advantage is understood by several large companies that have launched different social commitment programmes with elements of social investment through education, employment creation and community support. They also promote small empowerment companies in their own procurement process through affirmative procurement policies and form joint ventures with this category of companies when taking part in public tender procedures.

12.3 Transformation within the Corporation

For a company seeking to develop black economic empowerment into one of its core strategies, the transformation process has to begin within the organisation. A solid starting point in this process is the understanding of the fact that the regulatory requirements on a company's diversity profile can lead to a positive result, if the commitment is there. Instead of being regarded as a legal issue placing a threat of penalty for non-compliance, we believe that true commitment to the essence of black eco-

²⁶⁵ BusinessMap 2000, p 29ff

conomic empowerment should be regarded as a tool to liberate new capacity in the organisation, and therefore is decisive for the company's future relevance on the market.

The transformation of a company is not a process that solely can be lead from the boardrooms. The concept of empowerment, and employment equity as a part of it, has to be understood and supported throughout the organisation in order to reach substance over mere form. It is therefore crucial to create a company culture that embraces and encourages empowerment.

12.3.1 The Importance of a Visionary Leader

The company leader's role in creating the right company culture is indispensable. The CEO, as well as the top management, is to drive and steer the development of empowerment as a central business imperative. Without the leaders' strong and visible commitment to the process, it will not be possible to reach unity behind the company's empowerment objectives throughout the organisation.

Internal resistance to embrace black economic empowerment as a business imperative is mostly found in the middle management. As their lack of enthusiasm can be decisive of how the workforce perceives the process, sincere commitment at the middle manager level is to be ensured. One way to clarify the importance of BEE as the company's business imperative is to integrate links between management remuneration and the performance they show in managing empowerment objectives.

Given the importance of a strong leader to drive the empowerment process within the organisation, it is of outmost importance for a company establishing in South Africa to appoint a visionary leader with a firm commitment to black economic empowerment.

12.3.2 Diversity Management in the Company

As several South African workplaces are becoming more representative of the society, the need for diversity management has been recognised and actively discussed the last year within corporate South Africa. You should be aware of that diversity management is not about combining one white and one black culture within the organisation. There are several black, as well as white, cultures in South Africa that need to learn how to collaborate in the workplace.

In workplaces where diversity management is neglected, the internal transformation process can be restrained due to inherent reluctance to the process. The reluctance is

most often an unconscious reaction, originating in fear for change. Diversity management aims at providing people with skills that enable them to deal with the transformation of their organisation.

Workshops dealing with various related themes are often used as a part of a company's diversity management. Their objective is to increase the knowledge of culture-based peculiarities and thereby diminish scepticism towards values that might not coincide with your own.

By changing the mind-sets, people can start to understand diversity and learn to appreciate and respect it within their own organisation. Therefore, successful diversity management is a vital part in impeding the pace of job-hopping, partly caused by intolerant and uncomfortable workplaces. Other ways to help retain staff is to create job assignments and working environments in a way that will develop and support the individual's performance. Mentorship programmes are useful tools as well.²⁶⁶

The process to develop all aspects of black economic empowerment to be business imperatives requires knowledge and strong commitment. It can be perceived to take a lot of time and resources from the ordinary business operation. You have to keep in mind that economic empowerment of the previously disadvantaged is not about charity. It is an investment. At the end of the day, to broaden the economic base to comprise the society in its entirety makes business sense.

²⁶⁶ Hell for Blacks Too? Financial Mail, 21 February 1997

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Interviews:

Please see Acknowledgements at page 4

All works referred to in the Thesis are South African, unless otherwise indicated.