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BLACK ECONOMIC EMPOWERMENT

New construction sector code could replay the Mining Charter debacle

Radical last-minute changes could have unintended effects on built environment professionals and companies, writes Deon Oberholzer

08 FEBRUARY 2018 - 05:55 DEON OBERHOLZER

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The Construction Sector Code was finally gazetted in December – just two weeks before the building industry holiday. At least the timing of this was better than the repeal of the old one in 2016, just days before the financial year-end of most companies.

Comparing the final document to the draft reveals that most of it was left unchanged, but there are a few earthquakes set to shake some well-constructed black economic empowerment (BEE) strategies to their foundations. Some of the last-minute changes could have a significant effect on the industry, and the look and feel of those changes bear the hallmarks of one or more highly influential lobby groups or agents with a radical agenda pushing amendments through without proper consultation. Anyone up for another Mining Charter extravaganza?

What follows are points I noted in my review:

• Multinational BEP ownership. BEP refers to built environment professionals such as consulting engineers, architects and other professional service providers in the construction industry, and the news is dire for multinational BEPs. They should apparently please just leave the country, as it appears internationally owned consulting firms will no longer be considered for government contracts in SA. If you do not want to exit completely, then sell the business to your black executives. If they cannot afford it, close the door on your way out.

The South African National Roads Agency Limited (Sanral) published its draft procurement policies late in 2017, noting that it would only do business with companies that had 51% BEE ownership. The amended Construction Sector Codes set out a new and highly controversial disqualifier for BEPs — that only half of a BEE shareholding would count if the business was not more than 50% owned by the company's own South African executives.

So, by combining these two, an internationally owned BEP is automatically disqualified. There will be pushback on this, but it might not be particularly vocal or legal. The industry works predominantly on tenders for big projects, and we all know that if you make too much noise your tender submission may just fall off the back of the truck on the way to the tender committee.

• Procurement from black-owned designated group suppliers. First the definition of who qualifies: a "black designated group supplier" is defined as "a company that is at least 51% owned by black people who are unemployed, youth, persons with disabilities, living in rural areas and/or military veterans".

Because many BEPs subcontract work to other BEP specialists, I somehow doubt that the incidence of designated BEPs is 10 times as high as the incidence of designated suppliers of anything else, but there it is: BEPs have to source 20% of all their procurement from this tiny sector of the economy. The equivalent for everyone else in terms of the BEE codes and the sector codes is only 2%.

• The last bone of contention is the treatment of employees who are foreign nationals. Counter to all the definitions and determinations that secure the rights and obligations of legally employed foreign nationals, according to the last-minute changes to the code foreign employees are no longer recognised as employees, even if they are in a formal employment relationship. Their salaries are now part of "procurement". This is a really weird addition that happens to be entirely counterproductive. I assume the idea might have been to incentivise construction companies to employ more South African citizens, but to create a set of rules that are so easily circumvented is a clear indication that this was not thought through or put out for comment.

If you do have any foreigners working for you, simply get them to become freelance consultants. They merely need an invoice and a sworn affidavit and, presto, you are now dealing with level four exempted micro-enterprises with 100% procurement recognition, a nice reduced skills development target and less pressure on management transformation.

I cannot figure out how this promotes real transformation. Prior to this we had a compounding BEE benefit, especially on the skills development element. The skills targets were recognised for spending on black staff only, but the target was based on total salaries. The exclusion of international salaries simply serves to reduce this target.

• One of the few highlights of the final draft of the Construction Sector Codes is that the role of the Construction Sector Council (CSC) has been strengthened to an executive authority with the mandate to monitor transformation in the sector. With ANC president Cyril Ramaphosa having built his election platform on a commitment to root out government corruption and state capture, we can expect an equally hard push to get rid of corruption and fraud in business. The new codes confirm that the broad-based BEE commissioner and the CSC will most certainly form a close working relationship to take aim at BEE fronting.

The CSC was the result of a most thorough and comprehensive process of industry participation. The code is generally well drafted and most of its unique requirements are specific to the industry and included for the right reasons, such as the inclusion of construction material suppliers and the intense focus on construction industry professionals.

However, the last-minute changes were not properly communicated, not tested and, in many instances, will most likely lead to unintended consequences that will not improve transformation in this critical sector of our economy. We all know what happens if you add extra floors on top of a building as an afterthought. Apart from a few sensible tweaks, most of these changes to the code fall into the afterthought category.

• February is upon us. Construction companies with a February year-end have but a few weeks to get their houses in order or risk being out in the wilderness for a year. Companies should remember that the measurement periods may now only be the actual financial year of the entity, so if you miss this year, the next window to do something is a year away.

Construction companies would be well advised to steer clear of any form of fronting. As mentioned, the push against corruption will surely – after the widespread and ongoing reporting on the activities of KPMG, McKinsey, SAP, Steinhoff and others – be expanded to include businesses of all sizes.

The new government, whoever it may include, will be obliged to carry out a visible "witch hunt" among those who feel they can flout the rules because others do.

For those with a February year-end, if you think you can relax until a later date, you're in for a rude awakening. And there is likely to be an even ruder awakening for those who think they can blame government corruption for dodgy practices or non-compliance with sector codes.

• *Oberholzer is CEO of Gestalt Growth Strategies.*