

Chapter Seven: Code 500 – Measurement of the Preferential Procurement Element of Broad-Based Black Economic Empowerment

Statement 500 – The General Principles for Measuring Preferential Procurement

Introduction

The Preferential Procurement element of the Generic Scorecard aims to address certain key issues surrounding supplier opportunities for BEE compliant enterprises, Qualifying Small Enterprises and Exempted Micro Enterprises as well as black-owned enterprises. These issues include:

- **Preferential Procurement is used to drive transformation throughout the economy by encouraging procurement only from suppliers that are compliant with the B-BBEE scorecard:**
 - There is a market tendency to interpret B-BBEE compliance as only having ownership by black people without looking at the level of compliance with other B-BBEE requirements. This has resulted in a number of sham transactions/'fronting' activities being entered into in a scramble to meet this compliance requirement.
 - Enterprises are encouraged to procure from those entities that have a good B-BBEE contribution level based on their performance on the scorecard. A supplier that has a very good B-BBEE contribution level is likely to be chosen as a preferred supplier as compared to his peers as they will give the enterprise they are providing goods and services to a good scoring on their own scorecard as well.

- **Incentive to procure from Qualifying Small Enterprises and Exempted Micro enterprises.**

Statement 500 has a specific indicator for the recognition of BEE procurement spend from , Qualifying Small Enterprises (QSE's) and Exempted Micro Enterprises (EME's) by allocating specific scorecard points to procurement from these entities exclusively.

The Preferential Procurement Scorecard

Criteria	Weighting points	Compliance targets	
		Years 0-5	Years 6-10
B-BBEE Procurement Spend from all suppliers based on the B-BBEE Procurement Recognition Level as a percentage of Total Measured Procurement Spend	12	50%	70%



B-BBEE Procurement Spend from Qualifying Small Enterprises or Exempted Micro-Enterprises based on the applicable B-BBEE Procurement Recognition Level as a percentage of Total Procurement Spend	3	10%	15%
B-BBEE Procurement Spend from any of the following Suppliers as a percentage of Total Measured Procurement Spend			
Suppliers that are 50% black owned; and	3	9%	12%
Suppliers that are 30% black women owned	2	6%	8%

The Preferential Procurement scorecard offers B-BBEE procurement recognition from three categories of B-BBEE compliant suppliers. These are summarized in the table below:

BEE COMPLIANT SUPPLIERS WHICH WILL ENJOY PREFERENTIAL PROCUREMENT RECOGNITION	
BENEFICIARY CATEGORY	DESCRIPTION OF BENEFICIARY
<p style="text-align: center;">(A) BEE COMPLIANT SUPPLIERS Based on BEE contribution level</p>	<p>Includes all BEE compliant companies:</p> <ul style="list-style-type: none"> • Of any size; • With 30% or more on the Generic or QSE scorecards; and/or • EMEs
<p style="text-align: center;">(B) QSE & EME SUPPLIERS Based on BEE contribution level</p>	<p>Includes:</p> <ul style="list-style-type: none"> • QSE's – proportional representation based on their score on the QSE scorecard to be applied; • EME's – proportional representation based on their deemed Level 4 status and Level 3 status if they are 50% black owned or 50% black women owned;
<p style="text-align: center;">(C) 50% BLACK-OWNED COMPANIES & 30% BLACK WOMEN OWNED COMPANIES Based purely on ownership status</p>	<p>Includes BEE compliant companies:</p> <ul style="list-style-type: none"> • Large entities; • QSEs; and • EMEs that are • 50% black owned or 30% black women owned

BEE Procurement Recognition Levels

For ease of reference, the BEE Procurement recognition levels as contained in Code 000 have been reproduced below. Note that Exempted Micro Enterprises obtain an automatic, deemed Level 4 Contributor Status (100% BEE procurement recognition).

BEE Status	Qualification	BEE procurement recognition level
Level One Contributor	≥100 points on the Generic/ QSE Scorecard	135%
Level Two Contributor	≥85 but <100 points on the Generic/ QSE Scorecard	125%
Level Three Contributor	≥75 but <85 on the Generic/ QSE Scorecard	110%
Level Four Contributor	≥65 but <75 on the Generic/ QSE Scorecard	100%
Level Five Contributor	≥55 but <65 on the Generic/ QSE Scorecard	80%



Level Six Contributor	≥45 but <55 on the Generic/ QSE Scorecard	60%
Level Seven Contributor	≥40 but <45 on the Generic/ QSE Scorecard	50%
Level Eight Contributor	≥30 but <40 on the Generic/ QSE Scorecard	10%
Non Compliant Contributor	<30 on the Generic/ QSE Scorecard	0%

- Companies are recognised for additional points based on the status table above
- Customers (public and private sector) will prefer to interact and procure from companies with higher BEE status (for their own recognition)
- Exempted Micro Enterprises qualify for a promotion to the next BEE Recognition level if the enterprise is:
 - more than 50% owned by black people
 - more than 50% owned by black women

Key measurement principles

2.Enhanced Recognition for Procurement from the Measured Entity’s Enterprise Development Beneficiaries

A Measured Entity will enjoy enhanced recognition for procurement spend from any company which is also simultaneously one of its enterprise development beneficiaries. This will be at a multiple of 1.2 – see example below:



ENHANCED RECOGNITION FOR SPEND ON ENTERPRISE DEVELOPMENT BENEFICIARIES

For example:

If Rand spend on Company A which is also an enterprise development beneficiary equals R100,000:
= R100,000 X 1.2
= R120,000

To calculate Preferential Procurement Spend (Company A is an EME in this example but the beneficiary need not necessarily be an EME)

= Rand spend (taking into account enhanced recognition) X BEE procurement recognition level
= R120,000 X 100% (EME = deemed Level 4 Contributor = 100% BEE recognition level)
= R120,000

3. Enhanced Recognition for Procurement from Value-Adding Suppliers

A Measured Entity will enjoy enhanced recognition for procurement spend from any company which is also a Value Adding Supplier. This will be at a multiple of 1.25

REWARDING VALUE-ADDING SUPPLIERS WHICH PRODUCE LOCALLY

Value-Adding Suppliers beneficiate or add value to raw materials and tend to manufacture and produce locally, rather than relying too heavily on imports in most cases. The objective of this enhanced recognition is to encourage local production.

NB: Value-adding suppliers still need to meet the Preferential Procurement scorecard requirements for any procurement spend on such suppliers to be recognised for B-BBEE scoring purposes.

Example

ENHANCED RECOGNITION FOR SPEND ON VALUE ADDING SUPPLIERS

For example:

If Rand spend on Company A which is also a value adding supplier equals R100,000:
= R100,000 X 1.25
= R125,000

Company A is a level 5 contributor

To calculate Preferential Procurement Spend

= Rand spend (taking into account enhanced recognition) X BEE procurement recognition level
= R125,000 X 80% (Level 5 Contributor = 80% BEE recognition level)
= R100,000

Note

Had Company A not been a value adding supplier the company procuring goods and services from Company A would claim preferential procurement points based on the following calculated amount:

= Rand spend X BEE procurement recognition level
= R100,000 X 80%
= R80,000



4.Enhanced Recognition for Black Owned Professional Service Providers and Entrepreneurs

A Measured Entity will enjoy enhanced recognition for procurement from Professional Services Providers and Entrepreneurs who are black owned. It must be noted that it is the intention of this Code to encourage procurement from such service providers who have a shareholding in excess of 50% and that such services are in the professional and consulting arenas of service provision. It is also the intention of the code to encourage the use of local service providers and it is therefore assumed that such black owned service providers and entrepreneurs will incur a majority of the costs related to this service provision locally. A non-exhaustive list of examples of such service providers is detailed below.

Professional and Consulting Services shall mean:-

Accounting and Auditing
Actuarial Sciences
Advertising Marketing
Any other professional and consulting services
Architectural services
Asset/Fund Management Services
Corporate Finance related services
Engineering services (all kinds of engineering disciplines)
Financial Advisory Services
HR Consulting Services
Information Technology Services and Consulting
Legal Services (including all legal related services)
Management Consulting Services
Medical Services
Quantity Surveying
Real Estate Appraisers
Real Estate Brokers and Salespersons
Real Estate Developers
Real Estate Managers
Recruitment Services
Scientists
Strategic Consultants
Tax Services
Town Planning Services
Training and Development
Transaction Advisory Services



TOTAL MEASURED PROCUREMENT SPEND (TMPS)		
	SPEND ITEM (included in TMPS save for any exceptions outlined in the adjacent column)	EXCEPTIONS (may be permissibly excluded from TMPS)
1.	Cost of sales	No exceptions
2.	Operational expenditure	No exceptions
3.	Capital expenditure	No exceptions
4.	Public sector procurement – from Schedule 2(e.g. Eskom) & 3(e.g. SITA) listed organs of state & public entities as per the Public Finance Management Act (PFMA)	Procurement from Schedule 1 organs of state & public entities is excluded from Total Measured Procurement Spend, unless the procurement is from a local government entity acting as a reseller
5.	Monopolistic procurement	No exceptions
6.	Third-party procurement (not pass-through, third party procurement)	Pass through third party procurement where the Measured Entity may be acting as an agent in normal business practices. In other words procurement spend which may pass through an agent (the Measured Entity) but which is not recorded as an expense in the entity's financial statements but is recorded in the third party's financial statements. For example: a travel agent buying on behalf of a third party
7.	Labour brokers & independent contractors	No exceptions
8.	Pension & medical aid contributions	Exclude capital investment portion only
9.	Trade commissions	No exceptions
10.	Empowerment related expenditure	The following empowerment related expenditure is excluded from TMPS: <ul style="list-style-type: none"> • Investments in or loans to an Associated Enterprise (as defined in Statement 102) • Investments, loans or donations which qualify for enterprise development and socio-economic development recognition under Codes 600 and 700
11.	Imports	Several exceptions – see box below
12.	Intra-group procurement	Exceptions as per the guideline on Complex Structures and Transactions

Exclusions from Total Measured Procurement Spend -

Permissible exclusions from Total Measured Procurement Spend are strictly defined in Statement 500. For ease of reference, the exclusions from total procurement which have already been outlined above in that they are exceptions from specific inclusions, are repeated below:

- Taxation
- Public sector procurement (schedule 1 entities as per the PFMA)
- Salaries, wages and emoluments
- Pass-through third-party procurement (where no entries relating to this procurement appear in the books of the Measured Entity)



- Empowerment related procurement associated with investments, loans or donations to Associated Enterprises or enterprise development beneficiaries

IMPORTS – PERMISSIBLE EXCLUSIONS FROM TOTAL MEASURED PROCUREMENT SPEND

- imported capital goods or components for value-added production in South Africa provided that:
 - there is no existing local production of such goods or components
 - importing such capital goods or components promotes further value-added production within South Africa
- imported goods and services if there is no local production of such goods or services including instances where:
 - the imported goods or services carry a brand different to the locally produced goods or services
 - where the imported goods or services have different technical specifications to those produced locally.

CALCULATING A MEASURED ENTITY'S PREFERENTIAL PROCUREMENT SPEND:

Below is an example to illustrate the calculation of a hypothetical company's preferential procurement score. Please note that this example assumes that Measured Entity X procures only from 4 suppliers over a twelve month period – a highly simplified example for explanatory purposes only.

Measured Entity X's annual procurement spend is as follows:

Supplier Company	BEE Score	Level Contributor Status	BEE Procurement Recognition	Procurement Rand Spend with Supplier	Enhanced Recognition	BEE Spend	Beneficiary category
Company A (measured as per Generic Scorecard)	62%	5	80%	R10,000,000	Value Adding Enterprise (1.25)	R10,000,000	(A)
Company B (measured as per the QSE Scorecard)	82%	3	110%	R250,000	Enterprise Development Beneficiary (1.2)	R330,000	(A) (B)
Company C	29%	Non-	Black women	R2,000,000	Black women	R2,000,000	(C)



(30% black women owned measured as per generic scorecard)		compliant	owned therefore 100% recognition		owned entity therefore no enhanced recognition		
Company D (measured as per the generic scorecard)	28%	Non-compliant	0%	R14,000	Value Adding Enterprise (no enhanced recognition as non compliant)	R0	

Step 1: Calculation of Rand Value of BEE Spend:

Company A:

= Procurement Rand Spend X BEE Procurement Recognition Percentage X Enhanced Recognition Multiple (where applicable)
 = R10,000,000 X 80% X 1.25
 = R10,000,000

Although Company A's BEE score is below 65% and the Measured Entity therefore cannot recognize 20% of the R10 million they spend on Company A, the enhanced recognition which Company A enjoys owing to its status as a Value Adding Enterprise, means that there is effectively recognition of the full R10 million spend for BEE procurement purposes

Company B:

= Procurement Rand Spend X BEE Procurement Recognition Percentage X Enhanced Recognition Multiple (where applicable)
 = R250,000 X 110% X 1.2
 = R330,000

Company C:

=R2,000,000

The full R2,000,000 is recognized as procurement is from a company that is more than 30% owned by black women

Note: Had company C been an enterprise development beneficiary of the Measured Entity or a Value-Adding Company, the Measured Entity's R2million spend on Company C would have been multiplied by 1.25 or 1.2 effectively. Since it is neither, however, there is no calculation since



Company C falls into the third scorecard category which sets a compliance target of 9% (in the first 5 years) for spend on any enterprise which is 50% black owned (as per the definition) and a 6% target (in the first 5 years) for spend on any enterprise which is 30% black women owned (as per the definition), regardless of its score on any broad-based scorecard and therefore without the application of the proportional recognition system for BEE procurement.

Company D:

= R0

Although Company D is a Value Adding Enterprise, it does not meet any of the Preferential Procurement Scorecard requirements for recognition and can therefore not enjoy any enhanced recognition.

Step 2: Calculate Total Measured Procurement Spend

Assume that all procurement spend in this example is listed above and that there are therefore no exclusions. Total Measured Procurement Spend is therefore equal to total procurement in this instance:

$$\begin{aligned}
 &= \sum \text{Total Rand Spend of Companies A, B, C, D} \\
 &= R10,000,000 + R250,000 + R2,000,000 + R14,000,000 \\
 &= R26, 250,000
 \end{aligned}$$

Step 3: Calculate Scores for Each of the Three Indicators

Beneficiary Category (A)

$$\begin{aligned}
 &= \text{BEE procurement spend from all suppliers as a percentage of Total Measured Procurement Spend} \\
 &= (\sum \text{BEE procurement} / \text{Total Measured Procurement Spend}) / \text{target} \times \text{weighting} \\
 &= (R10,000,000 + R330,000) / R26,250,000 / 50\% \times 12 \\
 &= (R10,330,000 / R26,250,000) / 50\% \times 12 \\
 &= 0.39 / 50\% \times 12 \\
 &= 0.787 \times 12 \\
 &= 9.4 \text{ points (out of a maximum total of 12)}
 \end{aligned}$$

The Measured Entity's BEE Procurement Percentage is 39% against a target of 50% which means the entity will enjoy 78% of the 12 weighting points allocated to this Beneficiary Category, i.e. 9.4 points.

(Note: Because company C is non-compliant with the scorecard it will not be taken into consideration in the calculation of Beneficiary Category (A); If however it had obtained a compliance level the extent of its compliance would have been used to determine the amount attributable from Company C towards this Beneficiary Category level)

Beneficiary Category (B)



= BEE procurement spend from QSE's & EME's as a percentage of Total Measured Procurement Spend

= $(\sum \text{QSE/EME BEE procurement} / \text{Total Measured Procurement Spend}) / \text{target} \times \text{weighting}$

= $(R330,000 / R26,250,000) / 10\% \times 3$

= $0.0125 / 10\% \times 3$

= 0.125×3

= 0.4 points (out of a maximum total of 3)

The Measured Entity's BEE Procurement Percentage is 1.25% against a target of 10%, which means the entity will enjoy 12.5% of the 3 weighting points allocated to this Beneficiary Category, i.e. 0.4 points



Beneficiary Category (C)

= BEE procurement spend from a 30% Black Women Owned supplier as a percentage of Total Measured Procurement Spend

= (BEE Procurement from 30% Black Women Owned supplier/Total Measured Procurement Spend)/target X weighting

= (R2,000,000 / R26,250,000) /10% X 2

= 0.076/ 10% X 2

= 0.76 X2

= 1.5 points (out of a maximum total of 2)

The Measured Entity's BEE Procurement Percentage is 7.6% against a target of 10% which means the entity will enjoy 76% of the weighting points allocated to this Beneficiary Category, i.e. 1.5 points

Step 4: Sum points for each Beneficiary Category to reach a score for Preferential Procurement

= Score for Beneficiary Category (A) + score for Beneficiary Category (B) + score for Beneficiary Category (C)

= 9.4 + 0.4 + 1.5

= 11.3 (out of a maximum total of 20)

The Measured Entity scores 11.3 points out of 20. It is however, possible for entities to score more than 20 points through procurement from BEE compliant suppliers with more than 65points on the scorecard (BEE procurement recognition of 110% - 135%) and/or through procurement from their own enterprise development beneficiaries and/or BEE compliant Value-Adding Suppliers

Analysis

Note that Beneficiary Category (A) on the Preferential Procurement scorecard includes procurement spend from EME's, QSE's. It may also include procurement spend from 50% Black Owned and 30% Black Women Owned companies, BUT only if they score 30% or more on a broad-based scorecard, since this indicator applies the proportional BEE procurement recognition levels.

Beneficiary Category B specifically targets procurement spend from EME's and QSE's and scores Measured Entity's only on this aspect of their procurement, to encourage procurement from small, medium and micro entities. Procurement from such entities will therefore ensure that a Measured Entity scores points on both Beneficiary Category (A) and Beneficiary Category (B), whereas procuring only from larger entities will mean that no points will be scored on Beneficiary Category (B).

Beneficiary Category (C) specifically targets procurement spend from 50% Black Owned and 30% Black Women Owned companies, rewarding only black ownership regardless of the entities scoring



on the scorecard. This is to ensure that the objective of increasing the number of black owned and controlled and black women owned and controlled entities is achieved while the other Beneficiary Categories cater for non-black owned and controlled entities and non-black women owned and controlled entities.

