

HOW DOES GAZETTE #44591

IMPACT THE OWNERSHIP SCORECARD?

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In terms of the B-BBEE Act, on 18th May 2021 a Practice Note under Gazette #44591 was published by the Minister of Trade, Industry & Competition. The gazette outlines the rules for claiming Discretionary Collective Enterprises. The purpose is to clarify the interpretation of how Ownership by Discretionary Collective Enterprises (Collective Enterprises) is measured on a B-BBEE Scorecard. These include Broad-Based Schemes (BBOs), Employee Share Ownership Programmes (ESOPs), Trade Unions, Investment Holding Companies that are BBOs, Not for Profit Companies (NPCs), Co-operatives and Trusts that should align with the Codes of Good Practice (Codes).

Ownership for Collective Enterprises has been a topic of hot debate amongst regulators, those operating in the B-BBEE space and the organisations implementing Ownership structures that use Collective Enterprises as a vehicle. Essentially, the debate surrounding Ownership structures incorporating Collective Enterprises began in May 2015, with the publishing of Gazette Notice 396, which was subsequently repealed. The notice disallowed Collective Enterprises from using an Ownership vehicle as most did not meet the three core elements of the Ownership scorecard, namely Voting Rights, Economic Interest and Net Value. Of particular concern for Collective Enterprises is that they can compromise Participants or Beneficiaries. Therefore, the clarity from this Practice Note is welcome, as beforehand interpretations centred around the requirements of the Ownership Scorecard by referring to various pieces of legislation. The objective of publishing the Practice Note was to create a point of reference for measuring Ownership structures, taking into account the “substance over legal form” principle.

There are many Participants or Beneficiaries attached to Collective Enterprises. However, there must only be one point of reference. Collective Enterprises are managed by a ‘fiduciary’. Such a person or organisation acts on behalf of Participants or Beneficiaries. Their role is to put the beneficiary’s best interest before their own, with a duty to preserve good faith and trust. Being a ‘fiduciary’ thus requires being bound both legally and ethically to act in another’s best interest. The Practice Note facilitates the objectives of B-BBEE as outlined in paragraph 2 of the B-BBEE Act (The Act) as Amended:

- (a) Promoting economic transformation to enable meaningful participation of ‘Black’ People in the economy;
- (b) Achieving a substantial change in the racial composition of ownership and management structures and the skilled occupations of existing and new businesses;
- (c) Increasing the extent to which communities, workers, co-operatives, and other collective enterprises own and manage existing as well as new businesses. The aim is to expand such access to economic activities, infrastructure and skills training;
- (d) Increasing the extent to which ‘Black’ Women own and manage existing and new businesses, as well as increasing their access to economic activities, infrastructure and skills training;
- (e) Promoting investment programmes that lead to broad-based meaningful participation in the economy by ‘Black’ People to achieve sustainable development and general prosperity;
- (f) Empowering rural and local communities by enabling access to economic activities, land, infrastructure, ownership and skills; and
- (g) Promoting access to finance to support B-BBEE.



The Rules for BBOs, ESOPs and Trusts are contained in Statement 100 of the Codes. However, in terms of the Codes, a 'defined class of natural person' satisfies collective identification. Herein it determines that the Collective Enterprise's constitution must define the Participants or Beneficiaries and the proportion of their claim to receive distributions.

Paragraph 3.1.1 in Statement 100 of the Codes states that: "An Entity receives points for participation by 'Black' People in its rights of Ownership, using the Ownership Scorecard. 'Black' People may hold their rights of Ownership in a Measured Entity as direct Participants or as Participants through some form of entity such as:

- 3.1.1.1 A Company as defined in the Companies Act of 2008, as Amended;
- 3.1.1.2 A Close Corporation;
- 3.1.1.3 A Co-operative;
- 3.1.1.4 A Trust;
- 3.1.1.5 A Broad-based Ownership Scheme;
- 3.1.1.6 An Employee Share Ownership Programme;
- 3.1.1.7 A partnership or other association of natural persons; and
- 3.1.1.8 Any form of a juristic person recognised under South African law."

The Codes expressly recognise that 'Black' People are entitled to participate in organisations' Ownership structures indirectly. The Practice Note emphasises the validity of Collective Enterprises, amongst others, as valid vehicles for furthering B-BBEE. In particular, the interest of that interposing vehicle - whether a Collective Enterprise or otherwise - should in some lawful manner be capable of being attributed to 'Black' Persons under paragraph 3.3.1, considering the Flow-Through Principle that features in Statement 100 of the Codes, which states:

"As a general principle, when measuring the rights of Ownership of any category of 'Black' People in a Measured Entity, only rights held by natural persons are relevant. If the rights of Ownership of 'Black' People pass through a juristic person, then the rights of Ownership of 'Black' People in that juristic person must be measurable. This principle applies across every tier of Ownership in a multi-tiered chain of Ownership until that chain ends with a 'Black' person holding Rights of Ownership."

Discretionary Powers

The Practice Note highlights discretionary powers afforded to a 'fiduciary' that are critical for ensuring meaningful benefit to a 'defined class of natural persons'.

What is a 'defined class of natural persons'?

It is a collection of Participants or Beneficiaries chosen on predetermined criteria. An example is ABC Traders creating an Ownership vehicle that supports a bursary scheme. The Beneficiary criteria of this Collective Enterprise is that all Participants or Beneficiaries must be women who are 'Black' Students that matriculated in Gauteng Province. The fixed percentage of the proportion of distribution of the claim is '100%'.

A 'fiduciary' year on year identifies 'a defined class of natural person' then distributes funds according to the criteria. They have a vested right to receive bursaries from the ABC Traders bursary scheme.

However, not all women who are 'Black' Students matriculated in Gauteng. Therefore, women who are 'Black' Students who matriculated in KwaZulu Natal fall outside ABC Traders' 'defined class of natural person' and do not qualify for receiving any benefit from the ABC Traders bursary scheme. A 'fiduciary' may not award an ABC Traders bursary to any individual falling outside the 'defined class of natural person'.

Is a single-purpose empowerment structure claimable?

Single-purpose Collective Enterprises that contribute towards education, development or community upliftment, such as BBOs or Trusts, are accepted. However, each must be recognised in a chain of Ownership. Therefore, ABC Traders claiming these points must link to the 'Black' Participants or Beneficiaries housed in their single-purpose Collective Enterprise.

Such single-purpose empowerment structures, although used in South Africa to address B-BBEE, are used in businesses globally to address socio-economic challenges in their own country of origin.

Can ABC Traders incorporate 'minors' - children under 18 - in their 'defined class of natural persons'?

The Practice Note states that only 'Black' People who are Participants may attract recognition on the Ownership Scorecard; the Codes place no restrictions on the nature of Participants or Beneficiaries. Without steering from the message of this statement, 'minors' are not restricted Participants or Beneficiaries, whether as part of a 'defined class of natural persons' or individually. The National Youth Development Agency Act, no.54 of 2008, published as Gazette #31780, defines a Youth as a person aged between 14 and 35 that qualifies under Designated Groups.

As per the Children's Act 38 of 2005, a "child" means a person under 18. Therefore, when entering into Ownership transactions that incorporate Youth between 14 and 17 years old, legislation to protect their interest must be taken into account. Other Acts that should be taken into consideration when dealing with people aged between 14 and 17 are:

- > The Financial Intelligence Centre Act (No. 38 of 2001) (FICA);
- > The Companies Act 71 of 2008; and
- > The Labour Relations Act 66 of 1996.

The purpose of each piece of legislation, as mentioned, is aimed at guarding the welfare of those it benefits and protects, whilst affording economic opportunities. It is, therefore, vital that organisations do not enter blindly into Ownership transactions with Youth who fall under the protection of the Children's Act.

What is the Economic Interest entitlement of a Participant or Beneficiary of a Collective Enterprise?

The Practice Note clarifies that dividend distribution may be in the form of cash or kind. Distribution for the type of Collective Enterprise chosen by ABC Traders more often than not sees dividend distribution paid in kind. The reason, in this case, is that ABC Traders will directly pay for the development of skills, education or training on behalf of its Participants or Beneficiaries. Otherwise, ABC Traders may choose to facilitate access to funding through social funding, community interventions or developments that will benefit Participants or Beneficiaries who fall within the 'defined class of natural persons'.

Economic Interest is the right to receive dividend payments or similar rights instead of the distribution itself. So, if ABC Traders distributes in a monetary form or in kind, the 'defined natural class of persons' does not in any way detract from the Economic Interest points that ABC Traders is entitled to claim. Furthermore, it has no bearing on any Economic Interest claimable in the Codes, whether there is a tangible distribution or not. The primary factor determining whether a dividend is declared or distributed is solvency and liquidity, which directly relate to ABC Traders or its Collective Enterprise. Therefore, ABC Traders or their Collective Enterprise may not be penalised if it did not distribute dividends in any particular year. However, any earnings retained, thus not distributed for whatever reason to the 'defined class of natural person', may not under any circumstances be distributed to any other party.

What are the Reporting Requirements of a Collective Enterprise?

Clause 4 of the Practice Note clarifies Reporting Requirements when an organisation is obligated to report their B-BBEE compliance to the B-BBEE Commission.

Section 13(G) of The Act, read with the Regulations and related forms, inform this obligation.

Section 13(G) of the Act states:

"Reporting

(1) All spheres of government, public entities and organs of state must report on their compliance with B-BBEE in their audited annual financial statements and annual reports required under the Public Finance Management Act, 1999 (Act No. 1 of 1999).

(2) All public companies listed on the Johannesburg Stock Exchange must provide to the Commission, in such manner as may be prescribed, a report on their compliance with B-BBEE.

(3) All Sectoral Education and Training Authorities contemplated in the Skills Development Act, 1998 (Act No. 97 of 1998), must report on skills development spending and programmes to the Commission."

Consequently, a Collective Enterprise with one or more other juristic vehicles in its chain of Ownership cannot report on 'Black' Participants or Beneficiaries in terms of classification, for example their 'number', their 'province' or their 'age', to name but a few. This results from a 'defined class of natural person' not being distinguished in these categories. In such cases, an organisation must report on 'Black' People's participation only, thus not including other categories, unless, however, a competent person cannot distinguish between them or the Code criteria for measurement do not request such verification.

Notwithstanding, it must report in line with the information the Collective Enterprise presents as evidence. In the case of ABC Traders, an information breakdown could include per province with a further breakdown requirement of demographics, or other relevant information, even if it is not verified.

If ABC Traders is not able to produce verified information, it is not compelled to do so. Therefore, under these circumstances, ABC Traders may not be considered non-compliant as per the requirements of Annexure 100 B-D in Statement 100.

However, it is essential to bear in mind that no unverified information can be included as evidence when measuring against the Ownership Scorecard. Information reported needs to be based on verified information by a SANAS Accredited B-BBEE Rating Agency, taking the requirements of the Protection of Personal Information Act into consideration (see page 12).