



Construction Industry Development Board
Pretoria - Head Office
Tel: 012 482 7200
Fraudline: 0800 11 24 32
Call Centre: 0860 103 353
E-mail: cidb@cidb.org.za

CONSTRUCTION PROCUREMENT

BEST PRACTICE GUIDELINE # B1

Formulating and implementing preferential procurement policies

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Note: The purpose of this Practice Guide is to present a range of policy options and implementation methodologies that may be pursued in the formulation of preferential procurement policies that are consistent with the provisions of the South African regulatory regime. This practice guide as such introduces the thinking behind preferential procurement policies, the manner in which such policies are implemented internationally and the constraints to implementation within South Africa. It interprets the Preferential Procurement Policy Framework Act and related regulations, identifies the methods by which preferences may be applied, provides guidelines as to how preferential procurement policies may be formulated to satisfy legislative requirements and contains examples of preferential procurement policies that are drafted in accordance with this practice guide. It also describes the relationship between the Preferential Procurement Policy Framework Act and the Broad-Based Black Economic Empowerment Act.

Practice Guide # B2, *Methods and Procedures for Implementing Preferential Procurement Policies*, provides a range of uniform methods and procedures for implementing a wide range of policy themes in a consistent manner and is intended for those responsible for implementing preferential procurement policies in a uniform manner.

This practice guide is intended for those responsible for formulating preferential procurement policies and those wishing to implement preferential procurement policies outside of the provisions of Practice Guide # B2.

1 Introduction

1.1 The use of procurement as an instrument of policy

Procurement may be regarded as the process that creates, manages and fulfils contracts relating to:

- the provision of supplies, services or engineering and construction works;
- the disposal of property;
- the hiring of anything; and
- the acquisition or granting of any rights and concessions.

A preferential procurement policy is a procurement policy that promotes objectives additional to those associated with the immediate objective of the procurement itself. The procurement of supplies, services and engineering and construction works has been used internationally to support a number of socio-economic or political (secondary) objectives including:

- the stimulation of economic activity;
- the protection of national industry against foreign competition;
- improving the competitiveness of certain industrial sectors;
- remedying regional disparities; and
- achieving certain more directly social policy functions such as the fostering of the creation of jobs, the promotion of fair labour conditions and the use of local labour, the prohibition of discrimination against minority groups, the improvement of environmental quality, the encouragement of

equality of opportunity between men and women, and the promotion of the increased utilization of the disabled in employment.

Historically, procurement has been used in South Africa to promote local content in goods, the manufacture of goods in designated industrial zones and quality in terms of national standards (SABS mark). In the last decade, it has been used to promote a number of broad socio-economic objectives relating to race, gender, disability, job creation and poverty alleviation.

1.2 Methods by which preferential procurement policies may be implemented

Procurement can be used to support socio-economic policies using the approaches described in Table 1. For example, in the United States, reservation schemes and supply side schemes are used to ensure market share of small business enterprises and minority business enterprises. Recent legislation in Botswana (Republic of Botswana, 2001) makes provision for both reservation and preferencing schemes to promote citizen contractors i.e companies that are wholly owned by Botswanan citizens. In South Africa, the Department of Trade and Industry operates in terms of a cabinet memorandum, an indirect scheme (Industrial Participation Programme) whereby successful tenderers on certain high value contracts are required to participate in the South African economy to the extent that the total of all commercial / industrial activity (subject to the Department's crediting criteria) equals or exceeds 30% of the imported content within a period of 7 years.

Table 1: Generic schemes for using procurement to attain socio-economic objectives

Scheme type	Description
Reservation	Contracts or portions thereof are reserved for contractors who satisfy certain prescribed criteria e.g. contractors who: <ul style="list-style-type: none"> • are owned, managed and controlled by a target population group; • are classified as being a small business enterprise; • have equity ownership by companies with prescribed characteristics; or • are joint ventures between non-targeted and targeted joint ventures.
Preferencing	Although all contractors who are qualified to undertake the contract are eligible to tender, tender evaluation points are granted to those contractors who satisfy prescribed criteria or who undertake to attain specific goals in the performance of the contract.
Indirect	Procurement strategies and requirements are used to promote policy objectives by constraining the manner in which the procurement is delivered or by being used to generate offsets in parallel to the procurement eg specifications require that work associated with the contract is undertaken in a manner that supports policy objectives or offsets whereby undertakings such as the provision of bursaries, participation in an economy, the provisions of community centres etc that are unrelated to the procurement itself are, in order to secure the contract, committed to.
Supply side	Supply side measures are provided to targeted enterprises to overcome barriers to competing for tenders or for participating in procurements within the supply chain, eg access to bridging finance and / or securities, mentorship, capacitation workshops etc.

The Public Procurement Research Group, which is based at Nottingham University in the United Kingdom, has identified 9 basic methods to implement preferential procurement policies. Table 2 describes these methods and classifies them in terms of the scheme types presented in Table 1.

Typically the concerns raised by the international community revolve around the risk of the following occurring when implementing a preferential procurement policy:

- loss of economy and inefficiency in procurement;
- the exclusion of certain eligible tenderers from competing for tenders;
- a reduction in competition;
- unfair and inequitable treatment of contractors;
- lack of integrity or fairness;
- lack of transparency in procurement procedures; and
- failure to achieve socio-economic objectives through procurement .

Risks associated with a programme of procurement can be minimized should the implementation methodology that has the least negative impact be adopted and this methodology be implemented within a well defined framework.

A qualitative risk assessment on the implementation of a preferential procurement policy which has objectives that can be realised by creating a demand for services and supplies from, or to secure the participation of, targeted enterprises and targeted labour, using the first eight methods listed in Table 2 has been conducted in South Africa. The study, which was based on the assumption that the implementation method under consideration is managed and implemented in a manner so as to achieve the most favourable outcomes, indicated that preferencing schemes (methods 5 (preferencing at the short listing stage) and 6 (award criteria)), whilst not guaranteeing that socio-economic objectives will be met, is the method that is most likely not to compromise immediate / primary procurement objectives if appropriately managed. The analysis furthermore indicates that method 3 (contractual conditions), method 7 (product / description specification), and method 8 (design of procurement to benefit particular contractors) have the potential under certain circumstances to satisfy primary objectives while method 1 (set asides), method 2 (qualification criteria), and method 4 (offering back) are most likely to compromise such objectives.

Table 2: Methods used to implement preferential procurement policies

Scheme type	Methods		Actions associated with the method
Reservation	#1	Set asides	Allow only enterprises that have prescribed characteristics to compete for the contracts or portions thereof, which have been reserved for their exclusive execution.
	#2	Qualification criteria	Exclude firms that cannot meet a specified requirement, or norm, relating to the policy objective from participation in contracts other than those provided for in the law.
	#3	Contractual conditions	Make policy objectives a contractual condition eg a fixed percentage of work must be subcontracted out to enterprises that have prescribed characteristics or a joint venture must be entered into.
	#4	Offering back	Offer tenderers that satisfy criteria relating to policy objectives an opportunity to undertake the whole or part of the contract if that tenderer is prepared to match the price and quality of the best tender received.
Preferencing	#5	Preferences at the short listing stage	Limit the number of suppliers / service providers who are invited to tender on the basis of qualifications and give a weighting to policy objectives along with the usual commercial criteria, such as quality, at the shortlisting stage.
	#6	Award criteria (tender evaluation criteria)	Give a weighting to policy objectives along with the usual commercial criteria, such as price and quality, at the award stage.
Indirect	#7	Product/service specification	State requirements in product or service specifications eg by specifying labour-based construction methods.
	#8	Design of specifications, contract conditions and procurement processes to benefit particular contractors	Design specifications and/or set contract terms to facilitate participation by targeted groups of suppliers.
Supply side	#9	General assistance	Provide support for targeted groups to compete for business, without giving these parties any favourable treatment in the actual procurement.

2 The South African legislative framework for preferencing

2.1 An overview

Section 217 of the Constitution of the Republic of South Africa (Act 108 of 1996) establishes the immediate and broad secondary procurement objectives in South Africa as indicated in Table 3. (See also Best Practice Guide #A2, *Applying the prescripts of the CIDB in the Public Sector*).

Table 3: Public procurement objectives in South Africa

Objective	Reference
Primary Procurement system is to be fair, equitable, transparent, competitive and cost effective.	Section 217 (1)
Secondary Procurement policy may provide for: categories of preference in the allocation of contracts; and the protection or advancement of persons, or categories of persons, disadvantaged by unfair discrimination.	Section 217 (2)

The policy for the “good governance” aspects of procurement captured in Section 217 (1) establishes a comprehensive framework for procurement that is consistent with international norms and standards. Section 217(2) establishes South Africa’s preferential procurement policy in that it provides for a preferencing scheme and measures to be taken to protect or advance persons disadvantaged by unfair discrimination.

Section 217(3) of the Constitution of the Republic of South Africa (Act 108 of 1996) establishes the manner in which South Africa’s preferential procurement policy is to be implemented. Section 217 (3) of the Second Amendment Act (Act 61 of 2001) requires that national legislation must prescribe a framework within which the preferential procurement policy must be implemented.

The Preferential Procurement Policy Framework Act (Act 5 of 2000) was promulgated in response to this constitutional imperative. Accordingly, all organs of state must determine their preferential procurement policy and exercise a preference in accordance with the provisions of the Preferential Procurement Policy Framework Act.

The Act makes use of award criteria (i.e. the allocation of tender evaluation points in the evaluation of offers) to implement the nation’s preferential procurement policy i.e. the method most compatible with the primary procurement objectives embedded in the constitution and the method that is potentially acceptable to the international community and to foreign investors.

The one perceived downside to the Act is that the methodology does not ensure that the intended beneficiaries do in fact always benefit directly from the use of procurement as a policy instrument. Target groups are not automatically guaranteed contracts or participation i.e. entitlement is not embedded in the methodology. There is always a risk that the successful tenderer may not be the tenderer that enjoys preferential treatment in terms of the policy or is not the one who offers the highest participation in a contract to target groups. This can be a source of frustration and needs to be overcome by implementing supply side measures to capacitate those for whom the policy is intended, to take advantage of the benefits that are offered.

2.2 Recent practices in South Africa

In recent years, institutions have utilized a number of methods to implement procurement policies and have tended to combine some of the methods listed in Table 2 in an effort to improve policy outcomes. Frequently minimum requirements are established (method #3) and tenderers who fail to satisfy these requirements are excluded from tendering or have their tenders rejected as being “non responsive”. Examples of such practices include the setting of compulsory threshold contract participation goals and

the establishment of eligibility requirements for equity ownership by historically disadvantaged individuals or for joint venture formation. Others apply a hybrid form of the award criteria (method #6) in that points are awarded in respect of specific goals and some functionality points are awarded for "representivity" in respect of staff made available for the execution of the contract. Another common practice, particularly in respect of professional services is to invite tenders only from those who satisfy policy criteria (method #2). These methods, however, fall outside the provisions of the Preferential Procurement Policy Framework Act.

Several institutions, in newspaper advertisements, solicit tenders offers from only designated persons or groups. This practice is in conflict with the Act, which is designed to grant a preference to tenderers who can achieve or satisfy the requisite goals and not to deny those that cannot, the opportunity of tendering.

2.3 The Act in summary

The Preferential Procurement Policy Framework Act requires institutions (organs of state) to determine their preferential procurement policy and to implement it within the framework provided by the Act. The Act requires that a preference point system must be followed viz:

- for contracts with a Rand value above a prescribed amount, a maximum of 10 points may be allocated for specific goals provided that the lowest acceptable tender scores 90 points for price;
- for contracts with a Rand value equal to or below a prescribed amount, a maximum of 20 points may be allocated for specific goals provided that the lowest acceptable tender scores 80 points for price¹;
- any other acceptable tenders which are higher in price must score fewer points on a pro rata basis, calculated on their tender prices in relation to the lowest acceptable tender in accordance with a prescribed formula; and
- the contract must be awarded to the tenderer who scores the highest points unless objective criteria in addition to that pertaining to specific goals justify the award to another tenderer².

The framework provides examples of specific goals in that it states that specific goals **may** include:

- contracting with persons, or categories of persons, historically disadvantaged by unfair discrimination on the basis of race, gender or disability.
- implementing the programme of the Reconstruction and Development Programme as published in Government Gazette no. 16085 dated 23 November 1994.

The framework furthermore requires that:

- any specific goal for which a point maybe awarded, must be clearly specified in the invitation to submit a tender; and
- any goals contemplated must be measurable, quantifiable and monitored for compliance.

It should be noted, however, that the regulations (2001) issued in terms of the Act make provision for the awarding of contracts on the basis of preference, price and functionality (quality).

The regulations issued in terms of the Preferential Procurement Policy Framework Act have, however, several shortcomings. They in some instances go beyond the provisions of the Act and convert the framework provided in the Act into a series of prescriptions. The provisions of regulations 13 and 17 are *ultra vires* and as such may be ignored.³

¹ The current regulations, issued in terms of the Act (2001), makes preferencing optional should the procurement have a value of R30 000 or less and nominates a value of R500 000 as the threshold above which the 10% weighting is to be applied.

² Specific goals and criteria are differing concepts. Accordingly, socio-economic considerations fall outside the scope of objective criteria. Objective criteria relate to compliance with legislative requirements (e.g. tax obligations) and commercial (i.e. on technical, quality, capability and capacity issues.)

³*Ultra vires* literally means "beyond the powers or legal authority". The executive authority can only promulgate regulations that are within the ambit of the Act and cannot override the provisions of the Act.

2.4 The acceptability of other methods to implement preferential procurement policies in South Africa

The Preferential Procurement Policy Framework Act makes provision for the use of only award criteria (method #6) to implement preferential procurement policies. The question that arises is: can any other method be used and under what circumstances?

The Act does not make provision for preferencing at the shortlisting stage. Although this practice is in harmony with the intent of the approach to preferencing in the Act, it is outside the scope of the Act and should therefore be used with extreme caution in the public sector. The Broad Based Black Economic Empowerment Act makes provision for the qualifying contractors on the basis of criteria relating to broad-based black economic empowerment in concession contracts and the sale of state assets. (See section 3 below.)

Reservation schemes, with the exception of contractual conditions (method #3), apart from not being provided for in the Preferential Procurement Policy Framework Act, also violate some of the requirements of the Constitution for procurement to be fair, equitable, competitive and cost effective.

Contractual conditions (method #3), product specifications (method #7) and the design of specifications, contract conditions and procurement processes to benefit particular contractors (method #8) can be used should it be satisfactorily demonstrated that the procurement remains fair, equitable, transparent, cost effective and competitive. (See clause 4.8 and annex G of SANS 10396, *Implementing Preferential Procurement Policies using Targeted Construction Procurement Procedures*.) Put in another way, the use of these methods may not compromise value for money or exclude firms who have the ability and capacity to perform the procurement from competing for the award of the contracts or being awarded the contract.

It must, however, be stressed that the Promotion of Equality and the Prevention of Unfair Discrimination Act of 2000 (Act 4 of 2000) expressly prohibits the state from discriminating unfairly against any person on the grounds of race through the denial of access to contractual opportunities for rendering services or by failing to take steps to reasonably accommodate the needs of such persons. A schedule attached to the Act provides an illustrative list of unfair practices in certain sectors. This list cites “*unfairly limiting access to contractual opportunities for supplying goods and services*” as an unfair practice.

Preferencing strictly in accordance with the provisions of the Preferential Procurement Policy Framework Act, i.e. in terms of the points scoring system, is not considered to be unfair discrimination as no person is denied an opportunity to tender and a means is provided for promoting equality. The implementation of preferential procurement policies relating to the advancement of historically disadvantaged persons using one of the following mechanisms may constitute unfair discrimination:

- set asides i.e. allowing only enterprises that have prescribed characteristics to compete for the contracts or portions thereof, which have been reserved for their exclusive execution;
- contractual conditions i.e. making policy objectives a contractual condition e.g. a fixed percentage of work must be subcontracted out to enterprises that have prescribed characteristics or a joint venture must be entered into;
- qualification criteria i.e. the exclusion of firms that cannot meet a specified requirement, or norm, relating to the policy objective from participation in contracts other than those provided for in the law e.g. the Broad-Based Black Economic Empowerment Act; and
- offering back i.e. offering tenderers that satisfy criteria relating to policy objectives an opportunity to undertake the whole or part of the contract if that tenderer is prepared to match the price and quality of the best tender received.

3 The provisions of the Broad Based Black Economic Empowerment Act

The Act enables the Minister of Trade and Industry to issue codes of good practice on black economic empowerment that may include:

- the further interpretation and definition of broad-based black economic empowerment and the interpretation and definition of different categories of black empowerment entities;
- qualification criteria for preferential purposes for procurement; and
- indicators to measure broad-based black economic empowerment and the weighting attached to such indicators;

Every organ of state and public entity is required to take into account and, as far as is reasonably possible, apply any relevant code of good practice issued in terms of this Act in:

- determining qualification criteria for the issuing of licenses or concessions;
- developing and implementing a preferential procurement policy;
- determining qualification criteria for the sale of state-owned enterprises; and
- developing criteria for entering into partnerships with the private sector.

The Preferential Procurement Policy Framework Act requires organs of state to determine their preferential procurement policies within a framework. The Broad-Based Black Economic Empowerment Act expands the framework provided in the Preferential Procurement Policy Framework Act to take into account and to apply codes of good practice. It furthermore provides for the use of qualification criteria⁴ for the issuing of licenses, the sale of state owned assets and the entering into of public private partnerships.

4 Implementing the Preferential Procurement Policy Framework Act

4.1 Introduction

Preferencing forms an integral part of the procurement system. Accounting officers and accounting authorities are required to ensure that the procurement system of their respective institutions satisfy the provisions of the Constitution of South Africa (Act 108 of 1996). Preferencing which is compliant with the Constitution must be within the provisions of the Preferential Procurement Policy Framework Act (PPPFA) (Act 5 of 2000) i.e. each organ of state must determine its own preferential procurement policy and implement it in accordance with the framework provided in the Act.

It should, however, be noted that the PPPFA defines a preferential procurement policy as a *procurement policy contemplated in section 217(2) of the Constitution*. Section 217(2) of the Constitution of the Republic of South Africa (Act 108 of 1996) as such establishes South Africa's preferential procurement policy, namely that organs of state may implement a procurement policy providing for:

- a. *categories of preference in the allocation of contracts; and*

⁴ The Preferential Procurement Policy Framework Act provides only for the use of award criteria (i.e. the granting of a weighting to policy objectives along with the usual commercial criteria, such as price and quality, at the award stage) in the implementation of a preferential procurement policy. The Broad-Based Black Economic Empowerment Act makes provision for the use of the following additional mechanisms to implement a preferential procurement policy in concession contracts and the sale of state assets:

- preferences at the short listing stage i.e. the limiting of the number of suppliers / service providers who are invited to tender on the basis of qualifications and give a weighting to policy objectives along with the usual commercial criteria, such as quality, at the shortlisting stage.
- qualification criteria i.e. the exclusion of firms that cannot meet a specified requirement, or norm, relating to the policy objective from participation in contracts.

b. the protection or advancement of persons, or categories of persons, disadvantaged by unfair discrimination.⁵

Section 2(1)(d) of the PPPFA proposes a range of specific goals associated with the preferential procurement policy established in the constitution without setting any quantitative targets associated with these goals.

Organs of state need to select the specific goals which they wish to pursue, establish quantitative targets associated with such goals and establish implementation procedures which are consistent with the framework provided in the Act. Accordingly, the determination by an organ of state of its preferential procurement policy is to select specific goals, set quantitative targets for the selected goals, and to establish procedures to implement the preferential procurement policy provided for in the Constitution in accordance with the framework provided in the Act. (See Annexure 1 which provides two examples of a preferential procurement policy of an institution.)

It may be necessary in some circumstances to set goals in different sectors. Annex C of SANS 10403 contains a broad listing of Procurement Activity Sectors based on the classifications used by the European Union.

SANS 10396: Implementing Preferential Procurement Policies using Targeted Construction Procurement Procedures provides practical guidance and contains materials which can be of assistance in implementing the provisions of the PPPFA.⁶ SANS 10396 is, however, generic in nature and can as such be used in a number of different procurement regimes. It is accordingly necessary to contextualise the procurement regime within which SANS 10396 is implemented.

Annexure 2 provides two examples of the design of a preferential procurement policy that are consistent with the requirements of the Preferential Procurement Policy Framework Act, using the guidance provided in SANS 10396.

4.2 Specific goals

4.2.1 Goals envisaged in the Act

The Act suggests that specific goals should focus on the engagement of targeted enterprises and targeted labour (natural and juristic persons), historically disadvantaged by unfair discrimination on the basis of race, gender or disability, and on the attainment of programmes of the White Paper on Reconstruction and Development.

The White Paper on Reconstruction and Development in chapter three (The Economic Policy Framework) states that "*the Government's central goal for reconstruction and development is to meet the social and economic needs of the people and to create a strong, dynamic and balanced economy.*" An analysis of this document indicates that:

⁵ A person can refer to a natural person i.e. an individual, or to a juristic person i.e an entity such as a corporation or a partnership, capable of having legal rights and duties.

⁶ SANS 10396:

- a) sets out the issues and principles which should be considered when formulating preferential procurement policies and developing associated implementation mechanisms;
- b) sets out the principles associated with the engagement of targeted enterprises and targeted labour;
- c) establishes a range of techniques and mechanisms which may be used to provide a framework within which access to markets for targeted enterprises and / or targeted labour can be provided and goals relating to the engagement of such enterprises and / or labour can be set, monitored and evaluated at both project and programme level;
- d) establishes targeting frameworks and strategies which can be used with a number of different procurement regimes;
- e) describes techniques for the monitoring and evaluation of the outcomes of a preferential procurement policy;
- f) provides guidance as to how targeted procurement procedures can be activated in procurement documents; and
- g) provides guidance on the design and implementation of programmes associated with the implementation of a preferential procurement policy.

- employment creation is a central priority⁷;
- greater participation in the economy and less concentrated, more racially and gender inclusive ownership patterns are essential;
- poverty alleviation and the redressing of uneven regional development is crucial; and
- small, medium and micro enterprises need to play a substantially larger part in economic activity.

Accordingly, the law makers envisaged that specific goals would primarily relate to the participation of targeted enterprises and targeted labour in support of these programme objectives.

4.2.2 Practical considerations in the formulation of goals

Specific goals can in theory relate to:

- the structure of the contracting entity (i.e. to the satisfying of nominated requirements to be eligible for the award of a preference);
- the internal workings of the contracting entity (i.e. to satisfying nominated requirements to be eligible for a preference or to undertake to implement certain work-place actions during the performance of a particular contract);
- outsourcing (i.e. to the providing of business and / or employment opportunities to target groups through activities directly related to a particular contract); or
- nominated deliverables (i.e. to the undertaking to provide specific deliverables which may be related or unrelated to a particular contract).

The Act makes it clear, however, that specific goals must be clearly specified in procurement documents and be measurable, quantifiable and monitored for compliance. Thus the Act in effect requires institutions to:

- 1) formulate goals that are to apply to a contract prior to calling for tender offers and to clearly articulate them, including the method of measurement, in procurement documents;
- 2) evaluate preferences in tender submissions only in respect of the parameters stated in procurement documents;
- 3) develop procurement documents that capture sufficient information to enable claims for preferences to be evaluated at tender stage and to document undertakings in the subsequent contract so that they can be monitored for compliance;
- 4) set goals that:
 - a) are capable of being measured, verified and audited; and
 - b) can be either attained within the contract period, unless specific arrangements are put in place to monitor and enforce compliance after the contract has been completed, or measured prior to the award of a contract and maintained for the duration of the contract; and
- 5) provide sanctions to enable compliance to be encouraged or enforced.⁸

It is accordingly recommended that as a general rule:

⁷ It is recognised that procurement can facilitate the generation of jobs in South Africa by:

- ensuring that the foreign content in contracts involving goods, services and works is minimized;
- encouraging the substitution of labour for capital;
- supporting the use of "labour friendly" technologies which utilise a higher degree of labour input than is the case for conventional technologies, or are well suited to implementation by small scale enterprises; and
- encouraging and developing small scale enterprises to implement employment intensive practices and "labour-friendly" technologies.

⁸ The current regulations issued in terms of the PPPFA require institutions, in the event that preferences are fraudulently obtained or contractors fail to attain goals in the performance of the contract, to recover losses or damages that occur as a result of a person's conduct, cancel the contract, impose a financial penalty more severe than the theoretical financial preference or debar a contractor for a period not exceeding 10 years.

- 1) goals relating to undertakings to implement certain work place reform and nominated deliverables should be either achieved:
 - a) during the contract period; or
 - b) prior to the closing of tenders;
- 2) enterprise declaration affidavits (see Annex C of SANS 10396) or statements certified by an auditor should be used to determine the eligibility of tenderers for preferences pertaining to the structure or the internal workings of the contracting entity;
- 3) preferences awarded in respect of the structure of the contracting entity should be subject to the tenderer undertaking to maintain the structure within the nominated requirements for the duration of the contract and to limit the quantum of work subcontracted to firms not satisfying the nominated requirements;
- 4) preferences relating to the targeting of enterprises on the basis of geographic locations should be based on the conducting of business from premises located in defined geographic locations as evidenced from indicators such as payment of rentals or bonds for premises and payment for service charges, levies, rates and taxes to a municipality or regional authority.
- 5) preferences relating to the targeting of labour on the basis of geographic locations should be based on residency as recognised by members of the community residing within that area;
- 6) the participation of:
 - a) targeted enterprises should be measured on the basis of payments made to these enterprises (see clause 4.10 of SANS 10396);
 - b) targeted labour should be measured on the basis of wages and allowance paid to such labour (see clause 4.10 of SANS 10396);
 - c) joint ventures involving targeted partners should be measured on the basis of a balance between the value of work for which the targeted partner is responsible and the resources provided by such a partner (see clauses 4.4 and 4.10 of SANS 10396);
- 7) preferences relating to the participation of targeted enterprises and targeted labour should be based on the attainment of contract participation goals (percentage of the value of the contract which represents the inputs of targeted enterprises and labour in the performance of the contract) as measured in terms of the parts of SANS 1914 (see 3.1.4 below); and
- 8) goals relating to development issues that are unrelated to a specific contract such as to the granting of bursaries, staff training, the provision of housing, education and transport to members of staff and their dependents, donations to community organizations etc, should be based on amounts paid and certified by auditors, expressed as a percentage of audited turnover

Specific goals should not relate to compliance with laws, e.g. compliance with the Employment Equity Act. Tenderers must not be rewarded for complying with the law, they should rather be sanctioned for not doing so.

When formulating specific goals, consideration must be given to measures to prevent fronting and abuse, the application of sanctions as an instrument to promote compliance and the implementation of supply side measures (See clauses 4.12 to 4.14 of SANS 10396)

4.2.3 Awarding of points in respect of specific goals

The Act requires that points be awarded in respect of specific goals. As a general rule, the number of specific goals for which tender evaluation points are awarded should be kept to a minimum to:

- a) ensure efficiency in administration and monitoring for compliance;
- b) promote greater clarity of requirements in procurement documents; and
- c) maintain focus on the primary policy objectives.

The granting of too wide a range of preferences can lead to the situation whereby most tenderers become eligible for the awarding of a preference. This undermines the thrust and intent of preferences.

Tender evaluation points can be granted using one of three methods:

- 1) award a fixed number of points for attaining a specific goal;
- 2) award a variable number of points in proportion to the degree to which a tenderer responds to a particular goal (i.e in proportion to the quantum offered); and
- 3) on a comparative basis in terms of which the best offer received scores the maximum number of allotted points; the worst offer scores no points; and the remaining offers are scored between these limits.

Examples of these methods are presented in Table 4.

Methods 1 and 2 are objective and require no subjective judgements to be exercised in the quantification of the preference. The evaluation in these methods merely needs to determine whether or not the tenderer is eligible for a preference. Method 3, on the other hand, requires a somewhat subjective judgement to arrive at the quantum of the preference unless tenderers are required to submit contract participation goals. It is accordingly recommended that where this method is used and contract participation goals are not offered, preferences be evaluated by a panel comprising not less than three persons.

4.2.4 Participation of targeted enterprises and labour in contracts

4.2.4.1 Introduction

Specific goals associated with the targeting of enterprises on a particular contract relate to either the status of an enterprise (referred to as direct participation in SANS 10396) or the quantum of the engagement of targeted enterprises, targeted labour or a combination thereof in the execution of a contract (referred to as direct participation in SANS 10396).

Accordingly, tenderers can be accorded preferential treatment if they enjoy targeted enterprise status, or structure their resources to execute a contract in a manner that engages targeted enterprises and labour or both. Tenderers can either be required to tender a contract participation goal for the engagement of targeted enterprises, targeted labour or a combination thereof or undertake to achieve a contract participation goal prescribed by an employer.

Tenderers, where labour is targeted, can also be required to choose appropriate technologies and methods of construction, manufacture or a combination thereof and to tender contract participation goals associated with such choices. (See clause 4.8 and annex G of SANS 10396).

4.2.4.2 Defining targeted enterprises and targeted labour

Enterprises can be targeted upon the basis of:

- a) locality (domicile);
- b) status as a small, medium, or micro enterprise;
- c) ownership, operational responsibilities and control or a combination thereof by marginalized population groups
- d) a combination of a), b) and c)

Labour can be targeted on the basis of:

- a) gender, race, ethnicity;
- b) residency;
- c) age;
- d) disability;
- e) period of unemployment; and
- f) level of skill (wage levels).

Table 4: Examples of the different forms of preferences that may be encountered in different procurements

Method for granting tender evaluation points	Requirement for the granting of a preference	Tenderer or nominated parameter	Number of tender evaluation points
Method 1 (fixed number of evaluation points)	Have an enterprise profile which satisfies any of the following definitions: <ul style="list-style-type: none"> • Black Business Enterprise • Transforming Enterprise • Woman Business Enterprise • Engendered Enterprise 	Enterprise Declaration Affidavit that demonstrates compliance with the relevant definitions.	20 6 12 8
	Attain one of the following contract participation goals in accordance with the provisions of SANS 1914-1: Participation of targeted enterprises in the performance of the contract: ≥ 10% ≥ 20% ≥ 30% ≥ 40%	As offered by tenderer in a schedule	1 2 5 10
	Undertake to set aside a percentage of payroll for the employment of disabled persons employed in the operation of the facility	2,5% 5,0%	2 4
Method 2 (variable number of points in accordance with a formula)	Attain a contract participation goals in accordance with the provisions of SANS 1914-1: Participation of targeted enterprises in the performance of the contract.	As offered by tenderer in a schedule	$10 \times (D_1 - D_s) / (D_2 - D_s) \#$ Where D_1 is the tendered Contract Participation Goal D_2 is the maximum Contract Participation Goal, namely 60% D_s is the specified minimum contract participation goal, namely 10%#
Method 3 (variable number of points on a comparative basis)	Undertake to set aside a percentage of payroll for the training of employees who are Black Persons, Women and Disabled Persons	As submitted by tenderer in separate schedule	4 points being awarded for the most favourable proposal; 0 points being awarded to the least favourable proposal, and others in between in proportion to their ranking.
	Attain a contract participation goals in accordance with the provisions of SANS 1914-1: Participation of targeted enterprises in the performance of the contract.	As offered by tenderer in a schedule	$10 \times (D_1 - D_s) / (D_H - D_s) \#$ Where D_1 is the tendered Contract Participation Goal D_H is the maximum Contract Participation Goal tendered by a tenderer D_s is the specified minimum contract participation goal, namely 10%#

Tenderers cannot be eliminated from further consideration should they fail tender to tender a contract participation goal or if they tender a contract participation goal lower than D_s . They can merely be denied preference points

Clauses 5.2.2 and 5.2.3 of SANS 10396 provide comprehensive guidance on the definition of targeted enterprises and targeted labour, respectively.

Definitions for targeted enterprises and targeted labour must be contractually enforceable and mirror the intent of the preferential procurement policy of the institution. Poor definitions are often indicative of ill-defined policies. Examples of well formulated definitions are contained in annex B of SANS 10396.

4.2.4.3 Resource specifications

Resource specifications are required to specify and describe contract participation goals at tender stage. They are also required to monitor and verify that the contractor achieves the contract participation goal in the performance of the contract and sanction him should the goal not be achieved. (See clause 5.2.5 of SANS 10396).

Standards South Africa have recently published recently published six targeted construction procurement resource standards (SANS 1914 parts 1 to 6).⁹ These resource specifications are performance standards and have four hierarchical levels, viz: goals/ objectives (level 1), functional requirements (level 2), performance requirements (level 3) and solutions (level 4). The objectives (level 1) are simply to provide business and employment opportunities to specified target groups (targeted enterprises and targeted labour). The functional statement (level 2) is to engage the target groups indirectly or directly in the performance of the contract. The performance requirement (level 3) is to engage target groups to the extent that a contract participation goal (a percentage of the value of the contract which represents the inputs of targeted enterprises and/or targeted labour in the performance of the contract) established for the contract is satisfied. The resource specifications also establish the means by which the contract participation goal may be satisfied (level 4). (See also annex D of SANS 10396)

Table 5 presents the target groups targeted (level 1) and the means by which contract participation goals (level 3) may be satisfied in each of the six resource standards forming part of the SANS 1914 series of resource specifications.

4.2.4.4 Unbundling strategies

Small scale enterprises can participate in procurement in one of two ways. They can either contract directly with a contracting authority, or act as a subcontractor, supplier or service provider to a prime contractor in the delivery chain. The breaking down of contracts into smaller components is not always justifiable, particularly for engineering and construction works. The reasons for this include division of responsibilities, interdependence of activities, programming, duplication of establishment charges and under-utilization of resources. The breaking down of a contract into smaller prime contracts in order to accommodate the aspirations of smaller firms can, also, have a negative impact on cost and time and place a considerable administrative burden on contracting authorities.

The international trend is to procure on the largest possible scale in the knowledge that small specialist firms will manufacture/fabricate/construct/provide various components and so be engaged in the delivery process. Resource specifications can be used to secure the participation of small scale enterprises by requiring prime contractors to "unpack" their contracts into smaller contracts and to procure the services of small businesses to perform such contracts and to administer them, and in so doing, remove this burden from the employer. This approach also offers an effective means in establishing new business linkages, particularly between large and small businesses.

⁹ A resource specification:

- a) describes the general requirements for engaging targeted enterprises and / or targeted labour on a contract for the provision of supplies, services or works, as relevant;
- b) specifies the contract participation goal (the value of a percentage of the value of the contract which represents the inputs of targeted enterprises and/or targeted labour in the performance of the contract);
- c) sets out the methods by which the contract participation goal will be measured, quantified and verified in the performance of the contract;
- d) describes the means by which:
 - i) progress towards the attainment of the contract participation goal is to be monitored;
 - ii) compliance with requirements will be verified and monitored; and
 - iii) the contract participation goal will be adjusted to accommodate variations to the scope of the contract.

Table 5: Goals and means of satisfying goals associated with resource specifications in the SANS 1914 series

Resource specification		Target Groups provided for#	Means of satisfying contract participation goals (CPG) requirements
#	Title		
1914-1	Participation of targeted enterprises	TEs (and TPs who are TEs)	By one or more of the following: -performing the work as a TE Prime Contractor -subcontracting portions of the contract to TEs -obtaining supplies from Suppliers who are TE -purchasing materials from Manufacturers who are TEs -obtaining bonds and insurance policies from TEs -engaging service providers who are TEs -engaging non-TEs who in turn engage TEs -entering into a Joint Venture with one or more TPs -engaging non-TEs who in turn enter into Joint Ventures with TEs
1914-2	Participation of targeted partners in joint ventures	TPs	By forming a joint venture at the Prime Contract level with one or more TPs
1914-3	Participation of targeted enterprises and targeted partners in joint ventures	TPs and TEs who are not necessarily TPs	By : -forming a joint venture at Prime Contract level with one or more TPs -engaging TPs as subcontractors/service provider/Manufacturers and Supplies (At least two thirds of the CPG must be made up by forming Joint Ventures with TPs)
1914-4	Participation of targeted enterprises and targeted labour (local resources)	TEs (including Targeted Manufacturers and Suppliers) and TL	By either : Method 1 : By virtue of TE status, provided that 50% of wages and allowances are paid to TL, and engaging TEs in the performance of the contract ; or by Method 2 : By engaging TEs and TL in the performance of the contract.
1914-5	Participation of targeted labour	TL	By engaging Targeted Labour in the performance of the Contract
1914-6	Participation of targeted enterprises in concession contracts	TEs (and TPs who are TEs)	By one or more of the following: a) by engaging one or more TEs; b) by engaging non-TEs who in turn enter into Joint Venture agreements with one or more TPs; c) by engaging non-TEs who in turn engage one or more TEs

TE = targeted enterprise, TL= targeted labour and TP = targeted partner.

4.3 Establishing and implementing an institution's preferential procurement policy

Well formulated preferential procurement policies should outline clear policy themes, establish priorities where there is more than one policy theme and project policy outcomes. Such policies will enable short and medium term targets or goals (deliverables) to be established when the policy is operationalized. (See Examples contained in Annexure 1)

Goals at project or contract level need to be (see Practice Guide # B2, *Methods and procedures for implementing preferential procurement policies*):

- a) clearly defined to make them contractually enforceable;
- b) measurable and quantifiable to allow them to be monitored and evaluated; and
- c) verifiable and auditable for reasons of transparency and ensuring that policy intent is achieved.

Goals at a programme level need to be aggregated and evaluated to facilitate the monitoring of progress towards the attainment of specific policy objectives.

Clause 4 of SANS 10396 establishes the principles and considerations which need to be taken into account in the development of a preferential procurement policy. The targeted procurement procedures set out in clause 5.2 of SANS 10396 provide a framework within which:

- a) goals can be set, monitored and evaluated, both at a project and programme level;
- b) access to markets can be provided for target groups;
- c) incentives can be provided for contractors to embrace the objectives of an institution's preferential procurement policy in the performance of the contract; and
- d) the participation of targeted enterprises and targeted labour can be secured.

Annexure 2 illustrates the design of a preferential procurement policy.

It is recommended that an institution's preferential procurement policy establish a broad framework for preferencing and not contain detailed implementation procedures. It should, as indicated in the examples contained in Annexure 1, allow those responsible for implementation to decide on the exact definitions of the target groups, the appropriate targeting strategies and the allocation of points for preferences to achieve the best outcomes in particular procurements.

Figure 1 illustrates the recommended approach to establishing and implementing preferential procurement policies. (Practice Guide # B2, *Methods and procedures for implementing preferential procurement policies*, provides guidance to those responsible for implementing preferential procurement policies in particular procurements. Practice Guide # B3, *Preferential Procurement in the Construction Industry*, provides guidance on how to implement policies in support of broad based black economic empowerment).

4.4 Monitoring and evaluation

The monitoring of the attainment of socio-economic deliverables at a project level cannot commence until:

- a) all aspects of the deliverables have been clearly defined and accepted by all the parties to a contract;
- b) the criteria for measuring and quantifying the attainment of deliverables is understood; and
- c) the method by which the deliverables can be audited and verified is laid down.

The targeted procurement procedures contained in SANS 10396 provide a framework within which all of the above can be achieved before the award of a contract is made. This enables monitoring for compliance in respect of social and economic objectives to commence as soon as the contract is effected, both at a project and programme level. (See clause 5.4 and annex H of SANS 10396)

Any evaluation of the degree of success achieved in providing social and economic deliverables is dependent on effective monitoring. Evaluation is an ongoing process and should not be deferred. This is necessary to ensure that any inadequate provision of deliverables is detected at an early enough stage to remedy the situation. Targeted procurement procedures contained in SANS 10396 facilitate this. (See clause 5.5 of SANS 10396)

It is recommended that as a minimum data is gathered in respect of the following for evaluation purposes:

- a) the financial offer of the lowest acceptable tender used for the scoring of evaluation points for price;
- b) the financial offer of the successful tenderer and details pertaining to the specific goals for which a preference is granted.

A set of indices to evaluate the range of socio-economic objectives associated with a preferential procurement policy should be developed for a particular programme along the lines of that presented in clause 5.5.2 of SANS 10396.

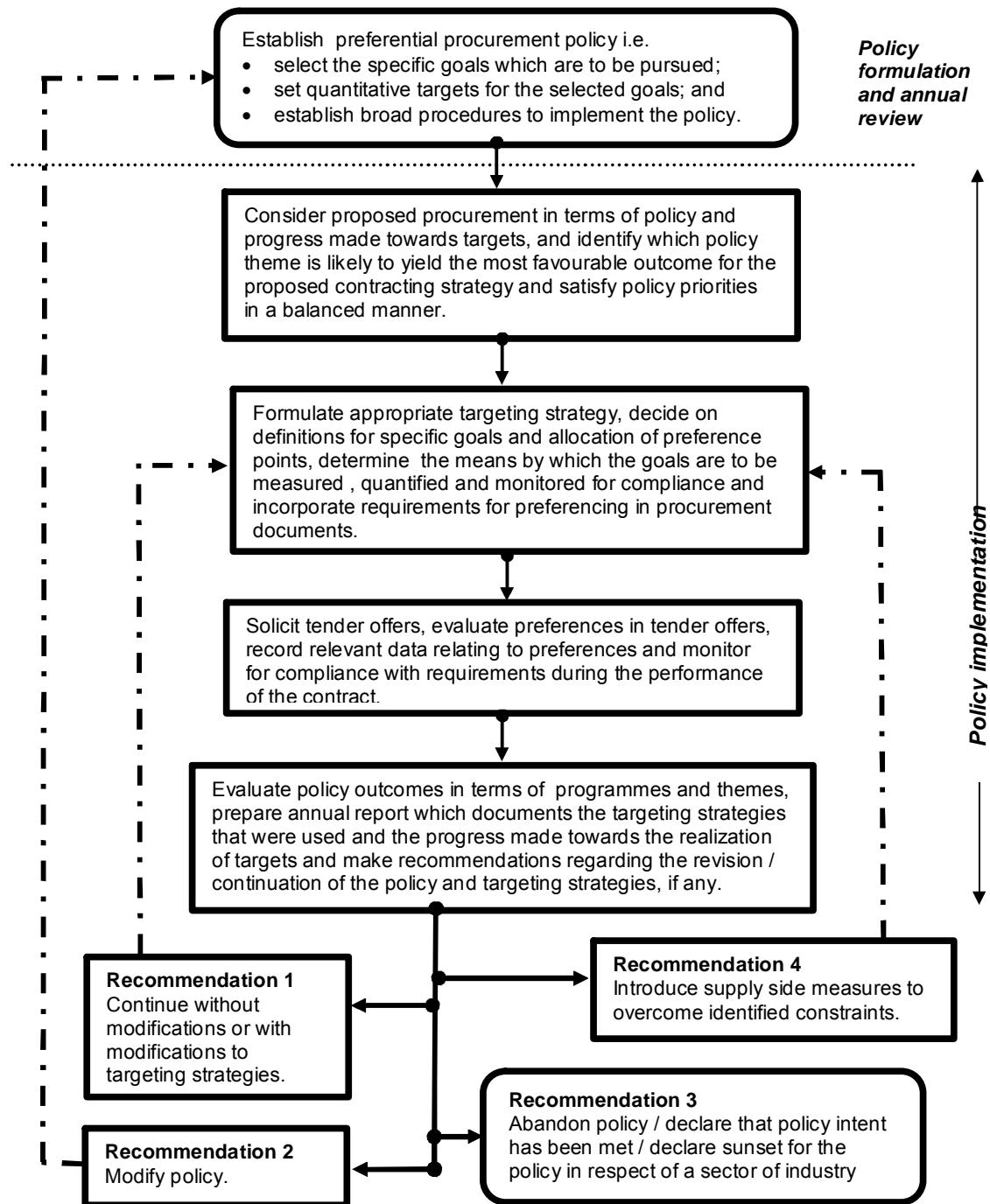


Figure 1: Recommended approach to formulating and implementing preferential procurement policies

4.5 Incorporating requirements for preferences in procurement documents

Clause 6 of SANS 10396 provides guidance as to how requirements for preferences can be incorporated in procurement documents. It is possible to prepare comprehensive preferencing schedules, which establish all the requirements and undertaking required to claim a preference, respectively. Where such schedules are issued with tenders and incorporated in the Scope of Works in the contract, all the issues, which need to be captured in the contract, can be incorporated in such schedules.

4.6 Evaluation of preferences in tender offers

An approach to the evaluation of tenders that is consistent with the Act is to:

- 1) Reject all tenders received that are not responsive to requirements (ie make a determination as to whether or not the tender complies in all respects with the specifications and conditions of tender as set out in the tender document.)
- 2) Reject as unacceptable all tenderers who have not satisfied their tax obligations or, if stated in the tender documents, are not in compliance with the requirements of the Employment Equity Act or any other piece of legislation.
- 3) Reject all unrealistically priced tender offers (i.e. those offers which are judged not to be possible to execute within the financial offer) as being unacceptable as their use as the benchmark for the calculation of price will distort the scoring and may result in negative values being recorded if the current formula in the regulations is adopted. (The evaluator should ascertain whether or not there is a valid reason for the tender price being unrealistic, and if not, eliminate the tender from further consideration. Such tenders would have in any event been rejected when objective criteria are considered.)
- 4) Score the remaining responsive tenders received and confirm that the commercial risk in awarding the tender to the tenderer scoring the highest tender evaluation points is acceptable. If not, record the reasons for overlooking this tenderer and consider the tenderer with the next highest number of points etc.

It should be noted that a tender may not be declared to be non-responsive / unacceptable, and as such be rejected, should a tenderer not comply with requirements relating to a preferential procurement policy e.g. for failing to provide a minimum amount of equity in the tendering entity or to commit to a minimum contract participation goal that may be established by the employer. Such requirements are not provided for in the Act.

5 Electronic rotating data bases (rosters)

Preferences can also be provided within nominated procurement procedures described in the CIDB's Standard Rules for Public Procurements.¹⁰ This can be achieved by:

- a) registering interested firms on an electronic data base;
- b) ranking them in the data base in terms of date of entry to the system and targeted enterprise status;
- c) selecting a limited number of firms (typically not less than five) to submit tenders for each new contract based on their rankings on the data base and subject to them satisfying specific criteria such as locality, services offered, specialist capabilities and capacity to deliver;
- d) applying preferences in the evaluation of such tenders; and
- e) repositioning tenderers (both successful and unsuccessful) on the data base at new positions dependent on their targeted enterprise status and record of previous tenders and contracts.

¹⁰ The CIDB Standard Rules for Public Procurements describes the procedure as follows:

Institution admits tenderers that satisfy prescribed criteria to an electronic data base and awards contracts or invites tenderers to submit tenders based on search criteria and their position on the data base and repositions such tenderers upon appointment or upon the submission of a tender offer.

The abovementioned procedure not only accelerates the rate at which targeted enterprises are invited to tender, but also provides a preference to targeted enterprises in the evaluation of tenders. This approach allows a preference to be applied in the shortlisting of tenderers and in the evaluation of tenders.

Clause 5.2.8 of SANS 10396 provides an example as to how enterprises are initially positioned and repositioned on the roster after being invited to tender.

Annexure 1: Examples of preferential procurement policies

Example 1: Policy of a Municipality

Policy objectives

The preferential procurement policy objectives of the municipality are to utilise procurements and disposals where appropriate to promote:

- a) the redressing of skewed business ownership patterns along racial and gender lines;
- b) employment to relatively unskilled workers residing within the area under the jurisdiction of the municipality;
- c) the market share of small businesses;
- d) businesses located within the jurisdiction of the municipality; and
- e) South African manufactured goods.

Priority is to be given to objectives a) and b)

Targets

The policy outcomes which are to be strived for are as tabulated in Table 1.1.

Table 1.1: Anticipated policy outcomes (targets)

Policy objective	Target	Method of measurement
The redressing of skewed business ownership patterns along racial and gender lines	By year 2010, the market share of black businesses is to be 50% of all municipal procurements. By year 2010, the market share of women businesses is to be 17,5% of all municipal procurements	Where direct preferences are used: 0,9 times the contract value of the contracts awarded to the targeted enterprise.
The market share of small businesses	By year 2010, the market share of small businesses is to be 30% of all municipal procurements	Where direct participation is used: 0,9 times the value of the work performed by the targeted enterprises
Businesses located within the jurisdiction of the municipality	By year 2010, the market share of local businesses is to be 60% of all municipal procurements	
Employment to relatively unskilled workers residing within the area under the jurisdiction of the municipality	At least 30 % of the total construction cost of contracts, excluding design and supervision fees and VAT, should represent the payment of wages and allowances to local labour.	Rand value of wages and allowances paid to local labour.

Specific goals for next three years

The targets for the next three years will be as follows:

Black Business Enterprises (BBeEs)	20%
Women Business Enterprises (WBEs)	5%
SMMEs	15%

These targets will apply in respect of all Procurement Activity Sectors for the first year of operation. The targets will be adjusted after the first year of operation, based on the profile of businesses contracted to the municipality and the targets achieved in respect of each targeted enterprise in a number of economic sectors.

Target groups

The target groups associated with the municipality's preferential procurement will be defined along the lines of that set out in Table 1.2.

Table 1.2: Target groups that will derive benefit from the Preferential Procurement Policy.

Target group	Definition
Black Business Enterprise (BBE)	Enterprise which is in the control of one or more black persons and is at least fifty one percent owned by one or more black persons who are principals.
Local Business Enterprise (LBE)	Enterprise which has its sole office or head office located within the area under the jurisdiction of the municipality.
Local Labour	South African citizens who permanently reside within the municipal boundaries and earn wages and allowances that are no more than one and a half times the minimum wage established for construction related work.
Small Business Enterprise (SBE)	Enterprise which satisfies the definition for a micro or small business in terms of the Small Business Act (Act 102 Of 1996)
Woman Business Enterprise (WBE)	Enterprise which is in the control of one or more women and is at least fifty one percent owned by one or more women who are principals.

Targeting strategies

One of the following two basic targeting strategies as detailed in Table 1.3 will be used in all procurements and disposals, except where the estimated value of the procurement or disposal, inclusive of VAT is less than R 30 000 where no preferencing will be applied:

- a) direct preferences in terms of which tenderers are granted a preference should their enterprise satisfy the requirements of one or more targeted enterprise definitions provided in the procurement documents or the supplies are manufactured in South Africa; or
- b) direct participation in terms of which a tenderer offers to attain a contract participation goal relating to the engagement of targeted enterprises or targeted labour as stated in the procurement documents in the performance of the contract.

Table 1.3: Targeting strategies associated with disposals and various categories of procurement

Category	Targeting strategy
Disposals	Direct preferences in respect of BBEs, WBEs, SBEs and LBEs
Procurement – supplies, hiring and letting	Direct preferences in respect of BBEs, WBEs, LBEs and South African manufacture
Procurement-services other than professional	Option 1: Direct preferences in respect of BBEs, WBEs, SBEs and LBEs Option 2: Direct participation
Procurement- professional services	Option 1: Direct preferences in respect of BBEs, WBEs and LBEs Option 2: Direct participation targeting BBEs
Procurement – engineering and construction works	Option 1: Direct preferences in respect of BBEs, WBEs, SBEs and LBEs Option 2: Direct participation targeting BBEs Option 3: Direct participation targeting LBEs and local labour Option 4: Direct participation targeting local labour

Mechanisms for measuring, monitoring and auditing the projected and actual outcomes

The preferential procurement policy will be implemented in accordance with the provisions of SANS 10396: Standard for Implementing Preferential Procurement Policies using Targeted Procurement Procedures in so far as they are applicable to ensure that socio-economic deliverables are appropriately

defined in the procurement documents and are measured, quantified, verified and audited in the execution of contracts.

Use of the following South African National Standards will be made to permit tenderers to offer contract participation goals and enable tenders to be evaluated in accordance with the provisions of the Preferential Procurement Policy Framework Act:

- a) SANS 1914-1: Participation of targeted enterprises
- b) SANS 1914-4: Participation of targeted enterprises and targeted labour (local resources)
- c) SANS 1914-5: Participation of targeted labour

Where a contractor fails to adhere to the conditions associated with the granting of preferences, financial penalties will be applied which must be approximately equal to one and a half times greater than any theoretical cost advantage that they may have received as a result of being granted the preference.

Annual reports to Council

The Municipal Manager will present an annual report to the Council on the outcomes of the preferential procurement policy. The report as a minimum must indicate the value of the contracts associated with each of the targeting strategies, the estimated value of work performed by each of the targeted groups and progress made towards the attainment of targets.

Programmes funded by others

The policy objectives and implementation procedures of programmes funded by bodies other than the municipality will be pursued provided that it is established by the Municipal Manager that such objectives and procedures are consistent with the Preferential Procurement Policy Framework Act. (Act 5 of 2000).

Annual review of policy

This policy will be reviewed annually in the light of the outcomes achieved in a year and will be adjusted, if necessary to ensure that the targets are met and the needs of the community which the municipality serves are taken into account.

Example 2: Policy of a National Department

Policy objectives

The preferential procurement policy objectives of the Department are to utilise procurements and disposals where appropriate to promote:

- a) the redressing of skewed business ownership patterns along racial and gender lines;
- b) the market share of small businesses; and
- c) South African manufacture.

Priority is to be given to objective a).

Targets

The policy outcomes which are to be strived for are as tabulated in Table 1.4.

Table 1.4: Anticipated policy outcomes (targets)

Policy objective	Target	Method of measurement
The redressing of skewed business ownership patterns along racial and gender lines	By year 2010, the market share of black businesses is to be 50% of all departmental procurements in each sector of industry. By year 2010, the market share of women businesses is to be 17,5% of all departmental procurements	Where direct preferences are used: 0,9 times the contract value of the contracts awarded to the targeted enterprise.
The market share of small businesses	By year 2010, the market share of small businesses is to be 30% of all departmental procurements	Where direct participation is used: 0,9 times the value of the work performed by the targeted enterprises (contract participation goal)

Target groups

The target groups associated with the department's preferential procurement will be defined along the lines of that set out in Table 1.5. It is, however, recognised that in some sectors of industry that it will be necessary to encourage transformation through the awarding of preferences to transforming firms along the lines of that set in Table 1.6. In some instances, where the supply of targeted enterprises is extremely low, specific goals may include those relating to the internal workings of the contracting entity, eg the monies spent on the provision of bursaries or specialized training expressed as a percentage of turnover.

Table 1.5: Target groups that will derive benefit from the Preferential Procurement Policy.

Target group	Definition
Black Business Enterprise (BBE)	Enterprise which is in the control of one or more black persons and is at least fifty one percent owned by one or more black persons who are principals.
Community-based organization (CBO)	Enterprise whose management and daily business is in the control of one or more black persons and which is at least 50% owned by one or more black persons or empowerment shareholders.
Small Business Enterprise (SBE)	Enterprise which satisfies the definition for a micro or small business in terms of the Small Business Act (Act 102 Of 1996)
Woman Business Enterprise (WBE)	Enterprise which is in the control of one or more women and is at least fifty one percent owned by one or more women who are principals.

Table 1.6: Target group that may derive benefit from the Preferential Procurement Policy for a limited period of time

Target group	Definition
Black-empowered enterprise (BE)	Enterprise which has at least one third of its principals who are black persons and which is at least 25% owned by one or more black persons who are principals.

Where the target groups contained in Table C2 are targeted, the method of measurement of progress towards the attainment of the target will change to the following:

$$0,9 \times (W_1 + W_2 + 0,5 \times W_3)$$

Where W is the value of work executed as either prime contractors or at any point in the supply chain and the subscripts 1, 2 and 3 indicate the values in respect of black business enterprises, community-based organizations and black-empowered business enterprises, respectively.

Targeting strategies

One of the following two basic targeting strategies will generally be used in all procurements, except where the estimated value of the procurement or disposal, inclusive of VAT is less than R 30 000 where no preferencing will be applied:

- a) direct preferences in terms of which tenderers are granted a preference should their enterprise satisfy the requirements of one or more targeted enterprise definitions provided in the procurement documents or the supplies are manufactured in South Africa; or
- b) direct participation in terms of which a tenderer offers to attain a contract participation goal relating to the engagement of targeted enterprises or targeted partners as stated in the procurement documents in the performance of the contract.

Only direct preferences will be used in procurements involving disposals

Mechanisms for measuring, monitoring and auditing the projected and actual outcomes

The preferential procurement policy will be implemented in accordance with the provisions of SANS 10396: Standard for Implementing Preferential Procurement Policies using Targeted Procurement Procedures in so far as they are applicable to ensure that socio-economic deliverables are appropriately defined in the procurement documents and are measured, quantified, verified and audited in the execution of contracts.

Use of the following South African National Standards will be made to permit tenderers to offer contract participation goals and enable tenders to be evaluated in accordance with the provisions of the Preferential Procurement Policy Framework Act:

- a) SANS 1914-1: Participation of targeted enterprises
- b) SANS 1914-2: Participation of targeted partners in joint ventures
- c) SANS 1914-3: Participation of targeted enterprises and targeted partners in joint ventures

Where a contractor fails to adhere to the conditions associated with the granting of preferences, financial penalties will be applied which must be approximately equal to one and a half times greater than any theoretical cost advantage that they may have received as a result of being granted the preference.

Data relating to black empowerment will be gathered in respect of all contracts awarded irrespective of the specific goal that applies to the procurement. The latter information should be used to monitor progress towards the attainment of the stated targets.

Annual reports to the Minister

The Accounting Officer Manager will present an annual report to the Minister on the outcomes of the preferential procurement policy. The report as a minimum must indicate the value of the contracts associated with each of the targeting strategies, the estimated value of work performed by each of the targeted groups and progress made towards the attainment of targets.

Programmes funded by others

The policy objectives and implementation procedures of programmes funded by bodies other than the municipality will be pursued provided that it is established by the Accounting Officer that such objectives and procedures are consistent with the Preferential Procurement Policy Framework Act. (Act 5 of 2000).

Annual review of policy

This policy will be reviewed annually in the light of the outcomes achieved in a year and will be adjusted, if necessary to ensure that the targets are met and the needs of the community which the municipality serves are taken into account.

Annexure 2: Examples of the design of a preferential procurement policy

Example 1: Black economic empowerment policy

Focus: The redressing of skewed ownership patterns along racial lines

Key performance indicators: 10 year targets flowing out of the BEECom final report.

#	DESCRIPTION	TARGET
1	Equity participation of historically disadvantaged individuals in each sector of the economy	25%
2	Number of historically disadvantaged non-executive and executive directors of companies listed on the JSE	40%
3	Market share (financial value of contracts) of targeted enterprises in public procurement	50%
4	Number of historically disadvantaged senior and executive management in private sector companies (with more than 50 employees)	40%
6	Market share of targeted enterprises in private sector procurement	30%
8	Shares of companies listed on the JSE owned by target group people (including businesses and collective enterprises)	25%

Direct impact of procurement policy: Procurement policy has a direct effect over KPI # 3 only.

Indirect effects of procurement policy: Procurement policy can cause businesses to restructure their businesses and supply chains to take advantage of public procurement opportunities. This will facilitate the attainment over time of other targets.

Strategy for change: Change, at a scale which will have an impact, may result from:

- 1) The empowerment processes presently operating in the South African economy whereby changes are occurring in the structure of equity ownership of large firms.
- 2) The establishment and nurturing of significant numbers of small businesses under effective ownership by previously disadvantaged individuals.

The first option is shaped more by high level financial considerations than by operating factors in the construction industry. The results of changes in ownership tend to manifest at company board level and are rarely felt in the company operating structures at the lowest levels. Significant changes in the structure of participation would thus be slow, if government placed passive reliance on changes driven primarily by exogenous financial factors.

The second option, that of supporting growth in participation by small businesses owned, managed and controlled by black people / women allows control over of some of the factors which have a direct bearing on the participation and performance of companies in public sector construction activities. The potential contribution of the public sector procurement system as an incubator of enterprises with these characteristics must be exploited.

Target groups: Enterprises with black control and 50,1% equity by black persons or empowerment shareholders.

Transforming firms with significant black equity and senior managers / companies which score highly in terms of government's broad based black empowerment scorecard in their respective sector.

Characteristics of businesses at different stages of transformation

Category of enterprise	Ownership	Control	Management
Black business enterprise	50,1% black owned (private company)	Vested in black persons	50% of senior managers are black persons (public companies)
Transforming business	25% black owned (private companies)	One third of its principals are black persons	30% of senior managers are black persons (public companies)

Actions:

Give preferences for participation by target groups in the evaluation of tenders.

Gather statistics of successful tenderers to track progress towards objectives iro:

- Equity participation of blacks
- Number of black non-executive and executive directors in companies listed on JSE
- Number of black persons who are senior managers in private companies.

Open up a register of targeted enterprises and accredit such enterprises.

Publish a directory of black and transforming firms to facilitate business linkages in procurements.

Short term targets (3 years)	% market share of department's procurement (by value)
Supplies contracts	5%
Works (civil contracts)	15%
Works (building contracts)	40%
Services contracts	5%

Targeting strategies Direct preferences on small value contracts.

Target group	Percentage of tender evaluation points allocated for goals
Black business enterprises Enterprises scoring highly in terms of the score card (large contracts only)	100%
Black-empowered enterprise / enterprise scoring moderately in terms of the score card (large contracts only)	50%

Direct participation using the SANS 1914-1, 1914-2 or 1914-3 specifications, depending upon the nature of the project.(0 points for zero contract participation goals and 100 points for 100% contract participation goal). Modify credits so that credits for transforming enterprises are reduced by multiplying the credits by 0,5. (See Practice Guide # B3, *Preferential procurement in the Construction Industry*)

Data capture	Capture the following data upon award and termination in respect of : <ul style="list-style-type: none"> • enterprise statistics of successful tenderer; • goals tendered and achieved • price (successful tenderer and price used in determination of the preference)
Monitoring for contract compliance	Monitor for compliance with conditions attached to the granting of preferences Monitor the attainment of contract participation goals in terms of Annex H of SANS 10396.
Evaluation	Calculate market share (value of work performed) of targeted businesses using the following formula: Market share = 0,9 x (W₁ + 0,5 xW₂)
	Where W is the value of work executed as either prime contractors or at any point in the supply chain and the subscripts 1 and 2 indicate the values in respect of black business enterprises and transforming business enterprises respectively.
	Produce report on a quarterly basis which provides details at both a project and programme level.
Review	The policy outcomes and targeting strategies used to achieve policy outcomes in specific projects will be reviewed on an annual basis as well as the supply side interventions that were employed with a view to improving performance in subsequent years. New three year targets will be set at the beginning of each financial year.

Example 2: Job creation in civil engineering infrastructure

Focus:	Job creation by increasing employment per unit of expenditure in civil engineering construction (i.e. the ratio of total construction costs excluding VAT but including any management fees directly related to construction activities to the total volume of employment generated (personhours) in the construction of civil engineering infrastructure.)
Key performance indicators:	Expenditure on semi-skilled and unskilled workers expressed as a percentage of the total cost of construction
Target:	At least 30% of the cost of construction represents the expenditure on semi-skilled and unskilled workers
Direct impact of procurement policy:	Provide incentive through preferences to contractors to select construction work methods and technologies which promote the creation of employment so as to promote the creation of employment
Indirect effects of procurement policy:	Unskilled and semi-skilled workers will receive some training. Money will flow from the project into the local community.
Strategy for implementation:	<p>Policy for the employment of temporary (contract specific workers), acceptable to stakeholders will be put in place in order to minimize risk exposure.</p> <p>A mechanism in terms of which contractors can define the portion of the excavation works which will be excavated by hand methods will be included in procurement documents along the lines of that proposed in annex G of SANS 10396.</p> <p>Tenderers will be permitted to choose which road construction technology they wish to make use of.</p> <p>No tender evaluation points will be granted in respect of contract participation goals less than 10%. Tenderers will be granted preferences in proportion to their tendered contract participation goal with the maximum points being awarded to the tenderer with the highest tendered contract participation goal.</p>
Target groups:	South African citizens who permanently reside within the boundaries of and earn wages and allowances amounting to less than R 9-00 per hour.
Actions:	<p>Give preferences for participation by targeted labour in the evaluation of tenders.</p> <p>Gather statistics on employment generated in different types of civil engineering infrastructure projects</p> <p>Review labour-based technologies to enable tenderers to exercise a wide choice of technologies in contracts.</p>
Targeting strategies	Direct participation using the SANS 1914-5 specifications, depending upon the nature of the project.(0 points for 10% contract participation goals and maximum points granted to the tenderer offering the highest contract participation goal. Weighting factor = 1,0)
Data capture	Capture the following data upon award and termination / completion iro respect of : <ul style="list-style-type: none">• choices / options selected;• goals tendered and achieved• price (successful tenderer and price used in determination of the preference)
Monitoring for contract compliance	Monitor for compliance with conditions attached to the granting of preferences Monitor the attainment of contract participation goals in terms of Annex H of SANS 10396.

Evaluation	Calculate increase in employment per unit of expenditure from the following formula: <u>Sum of (contract participation goals x contract value)</u> Sum of (contract value x 10) Produce report on a quarterly basis which provides details at both a project and programme level.
Review	The policy outcomes, targeting strategy used to achieve policy outcomes, and the selected technologies in specific projects will be reviewed on an annual with a view to improving performance in subsequent years.