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B-BBEE COMMISSION
a member of the dti group

THE BROAD-BASED BLACK EONOMIC EMPOWERMENT

PRACTICE GUIDE 01 of 2016

THE RECOGNITION OF THIRD PARTY PROCUREMENT SPEND

1. The Broad Based Black Economic Empowerment Commission ("B-BBEE Commission") is an entity established by the Broad-Based Black Economic Empowerment Act 53 of 2003 as amended by Act 46 of 2013 ("the Act"), to oversee the implementation of the Act, which includes provision of explanatory notices, non-binding advisory opinions and clarification services to improve the understanding of the Act.

2. This Practice Guide is issued as a non-binding guide purely to assist with the interpretation to ensure consistency in the application of the Act. Should this Practice Guide not be clearly applicable to your specific set of facts at any given time, you are advised to approach the B-BBEE Commission for a non-binding advisory opinion, which will be more specific to your set of facts.

3. This Practice Guide does not constitute a legal document or a ruling of the B-BBEE Commission on the issue concerned. Further, although this Practice Guide is not binding on the B-BBEE Commission, it does set out the approach that the B-BBEE Commission is likely to take on any matter relating to the recognition of third party procurement spend for consistency.

4. Section 9 (1) of the Act empowers Minister of Trade and Industry to issue Codes of Good Practice ("the Codes") on broad based black economic empowerment ("B-BBEE") to promote the purposes of the Act. The Codes as amended are underpinned by the need to drive inclusive economy, and must at all times be interpreted and applied in a manner that is consistent with the objectives and purposes of the Act, and in compliance with the Constitution.

5. The preferential procurement criteria in Code Series 400, is one of the instruments used to drive economic transformation throughout the economy, by encouraging procurement only from suppliers that are compliant with the B-BBEE scorecard. The instruments also provide for third party procurement spend.

6. In keeping with Code Series 400, and after carefully considering the current practice on the treatment of third party procurement spend, the B-BBEE Commission deems it necessary to provide a clarification on the recognition of third party procurement spend for the economy to derive the desired benefit for B-BBEE.

7. A third party refers to a middle person who facilitates the provision of goods or services between two entities or parties, such as a travel agent facilitating a booking of air travel between the traveller and preferred or affordable airline and receiving a commission in return for that service. Investopedia defines a third party as "an individual or entity that is involved in a transaction but is not one of the principals". (www.investopedia.com: 27 July 2016)

8. The following example serves as a guide on the recognition of third party procurement:

8.1 Entity A is a car rental provider, Entity B a travel agent, and Entity C the measured entity. The measured entity makes car rental bookings for its officials through Entity B. Entity B hires the rental cars with Entity A for the sum total of R15 000. Upon return of the rented cars, the measured entity pays R15 000 to Entity B. Entity B pays R10 000 to Entity C and retains R5 000 as its commission for the service.

8.2 In such a case, this is how the measured entity ought to recognise the third party procurement spend as part of its Total Measurement Procurement Spend (TMPS):

8.2.1 If Entity B's B-BBEE certificate was used, the measured entity cannot claim the full R15 000 as part of its TMPS. The measured entity will only include the R5 000 commission as part of its TMPS as it is the true income Entity B recognised in its financial statements for the service offered to the measured entity.

8.2.2 The sum of R10 000 was paid to Entity A, and that is the amount Entity A will recognise as income in its financial statements. This qualifies as pass-through procurement which is an exclusion from the calculation of TMPS in terms of section 6.3 of Code Series 400.

8.2.3 Therefore, Entity B has the responsibility to provide the measured entity with the breakdown of the spent amount indicating its direct costs from the service offered.

8.2.4 For the measured entity to count R15 000 as part of its TMPS, it should have both Entity A and Entity B's B-BBEE certificates with clear breakdown of how much was directly spent with each supplier.

8.2.5 Alternatively, the measured entity can only claim the full R15 000 against Entity B, if the full amount is recorded as income in Entity B's financial statements.

9 The example above is given to illustrate the importance of and the need to clarify and provide guidance on this issue, as highlighted below:

9.1 If the amount of R15 000 recorded as expenditure in the measured entity's financial statements is not recorded as income in either Entity A or Entity B's financial statements, it will nullify the B-BBEE certificate the measured entity used to recognise the procurement spend.

9.2 If the measured entity recognises the full amount as the expenditure against Entity B, this will affect Entity B's classification as an EME, QSE or Large Entity. Reason being that Entity B may regard itself as an EME or QSE because it only recognises a certain percentage as income from the R15 000 amount. But if the full amount is recognised, the measured entity's financial statements may reflect Entity B as a Large Entity and thereby requiring a generic certificate and not an EME or QSE certificate, as the case may be.

9.3 This could be regarded as a misrepresentation of Entity B's B-BBEE status which is an offence in terms of section 13O (1) (a) of the Act.

9.4 The measured entity can also be seen to be committing a fronting practice by submitting false information regarding its TMPS during verification, and such would constitute an offence in terms of section 13O (1) (b) of the Act.

10 All verification professionals have a responsibility and duty to provide entities with proper advice and guidance, including the implementation of this guide for the determination of the B-BBEE status of entities.

11 In terms of section 13O (2) a verification professional, procurement officer or any official of an organ of state or public entity who becomes aware of the commission of, or attempt to commit, any offence referred to under section 13O (1) and fails to report it, is guilty of an offence.

12 In terms of section 13F (1) (d) read with section 13J of the Act, the B-BBEE Commission has the power to investigate, either on its own initiative or in response to a complaint received, any matter concerning B-BBEE.

13 If an entity is found to have violated the Act, an entity could be fined up to 10% of its annual turnover, and individuals involved could be imprisoned for up to 10 years, and or fined. Specifically, an offence under section 13O (2) could lead to imprisonment of up to 12 months, or a fine, or both the fine and imprisonment.

14 This Practice Guide is issued as a guide purely to assist with the interpretation and application of Code Series 400 with regard to third party procurement spend, and as indicated, it does not constitute a legal document or ruling of the B-BBEE Commission.

15 This Practice Guide may be updated anytime by the B-BBEE Commission if there are any material changes arising from developments in the application of Code Series 400. In such an instance, an amended version will be published to replace this one.

16 For any queries or further clarity on this Practice Guide, kindly feel free to contact us at the following contact details:

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