

# Bureaucratic Red Tape

## 1. Objectives

The objective of this brief report is to provide members of the Portfolio Committee on Small Business Development with a summary of activities or practices that could potentially be regarded or defined as 'red tape' and/or 'bureaucratic red tape', distinction or similarity between the two, and measures to mitigate possible undesirable consequences for small enterprises.

## 2. Definition

For the purpose of this brief, it is imperative to note that emphasis is on red tape in as far as it relate or affect small enterprises, negatively or otherwise (not all red tape is bad/redundant). It does not for instance explore sector specific red tape e.g. labour laws, food/agriculture, lack of access to finance or markets as these are dealt with separately under sectoral analysis. It is also essential to specify that the scope of the report is limited to the 'small enterprise' as defined in the Revised Schedule of the National Definition of Small Enterprise in South Africa as, "an entity that turnover no more than R220 million and employ no more than 250 people", implying as a consequent that red tape is contextual. Environmental requirements, construction permits, immigration and wastewater permits etc. are most likely to affect big business more than small enterprises.

Red tape may mean diverse actions to different individuals or audience i.e. applying for a passport or a driver's licence is well known for red tape involved, people complain about the red tape when they are registering a car or buying a house, working with a detached business or government branch or official. Others define red tape generically 'as a colloquial term for bureaucratic practice of hair splitting or foot dragging, blamed by its practitioners on the system that forces them to follow prescribed procedures to the letter', a disposition that infers human behaviour e.g. incompetent, apathetic, corrupt etc.

However, the most widely used description of the red tape is 'rules and regulations, administrative and management procedures and systems, which are not, or are no longer, effective in achieving their intended objectives, and which therefore produce sub-optimal and undesired social outcomes', or, 'an idiom that refers to excessive regulation or rigid conformity to formal rules that is considered

redundant or bureaucratic and hinders or prevents action or decision-making'. Red tape manifests itself in and between all kinds of organisations, such as the different spheres of government, in the private sector and in civil society. This brief concerns itself with bureaucratic red that imposes "compliance, administrative, efficiency and con-compliance burden for small firms". The correct description and categorisation of the phenomenon being examined by this brief is crucial as it empowers members of the Portfolio Committee to respond definitively and unambiguously to the concerns of the small enterprise sector.

### **3. Previous Red Tape Initiatives Re-Visited**

#### **3.1 Regulatory Impact Assessment**

Regulatory Impact Assessment ("RIA") was a tool used to analyse objectives of a regulatory proposal, the risks to be addressed by the regulation and the options for delivering the objectives. It was a formal method for assessing the costs and benefits, economic and non-economic, of regulatory/policy proposals. It could be used to assess:-

- 3.1.1 All potential impacts, social, environmental, financial and economic;
- 3.1.2 All regulations: formal legislation (laws, ordinances, decrees, decisions, and master-plans) and quasi regulations (e.g. guidance or codes of practice, public awareness campaigns, etc.);
- 3.1.3 Distribution of impacts to consumers, business, employees, rural, urban, or other groups;
- 3.1.4 It is essential to note that RIA was not a substitute for decision-making but was best used as a guiding tool to improve the quality of political and administrative decisions. It served the values ascribed to the policy making process of openness, public involvement and accountability. Where legislation has already been committed to by government, the outcome of a judicial decision or an international agreement, the RIA process could still be followed.

### **3.2 Socio Economic Impact Assessment System**

Cabinet approved the Socio Economic Impact Assessment System (“SEIAS”) in February 2015 to replace the Regulatory Impact Assessment. An area of consternation for the Portfolio Committee in the past was the exclusion of the Minister responsible for Small Business Development in the Ministerial Committee. Housed at the Department of Planning, Monitoring and Evaluation (“DPME”), the primary objective of SEIAS is to assist departments to better formulate policies, legislations and regulations and ensure:-

- 3.2.1 Alignment with national priorities in promoting inclusive growth, addressing inequality, spatial imbalances, and environmental degradation;
- 3.2.2 Risks associated with the implementation of such laws are thereof mitigated, thus unintended consequences are minimised;
- 3.2.3 Costs of implementing such prescripts are reduced while benefits by the deprived service recipients are optimised; and;
- 3.2.4 Regulatory burden is reduced, thus a better and efficient administrative mechanisms of implementing the national priorities.

### **3.3 Red Tape Impact Assessment Bill**

The Portfolio Committee received referral papers from Announcements, Tabling and Committee Report (“ATC”) of Tuesday, 18 October 2016 which was the Red Tape Impact Assessment Bill. The Bill had been introduced in the National Assembly, proposed as a section 75 and was published in the Government Gazette Number 39907 of 7 April 2016. The Bill seeks to provide for the assessment of regulatory measures developed by executive, legislatures and self-regulatory bodies in order to determine and reduce red tape for businesses. It further seeks to provide for the establishment of Red Tape Impact Assessment (RIA) Units. (For ease of reference the bill is attached herewith this brief).

### **3.4 Guidelines for Reducing Municipal Red Tape Re-Visited**

During July 2013, the Department of Trade and Industry (“**the dti**”) published the “Guidelines for Reducing Municipal Red Tape”, a collaborative effort with Cooperative Governance and Traditional Affairs (“CoGTA”) and South African Local Government Association (“SALGA”). The guidelines were

largely an attempt aimed at improving service delivery for small businesses. The guidelines had been informed by the results of the 2011/2012 National Red Tape Reduction Pilot involving 12 municipalities and funded by **the dti** and CoGTA and with support from SALGA. Focus areas of the guideline were definitions, causes of red tape, impacts, tools to reduce red tape, improvement in municipal performance and service delivery, as well as guidelines and tips for addressing specific municipal red tape issues impacting on small businesses (For ease of reference the guideline is attached herewith this brief).

### **3.5 Legislative and Regulatory Protocols Impeding SMMEs and Co-operatives within the National Sphere of Government**

During the financial year 2016/17 the Department of Small Business Development (“DSBD”) undertook to conclude a study, which was being done in partnership with the Department of Planning, Monitoring and Evaluation (“DPME”), on legislative and regulatory protocols impeding SMMEs and co-operatives within the national sphere of government. The study has not been made public hence, little is known about its outcomes or impacts thereof.

### **3.6 Red Tape Reduction Programme**

In a Portfolio Committee meeting of 31 October 2018, the Committee learnt that DSBD was in the process of drafting a national Red Tape Reduction (“RTR”) strategy. According to the Department, the “RTR strategy was a comprehensive programme that had been developed successfully and was being piloted with the Gauteng Province in the Lesedi and Merafong municipalities”. The strategy has not been tabled to the Portfolio Committee. Recently, however, in a written reply to a parliamentary question by DA MP Hendrik Kruger, former Small Minister Lindiwe Zulu said “DSBD was driving the development of a draft national strategy to reduce red tape for small businesses”, which she anticipated would be ready by the end of 2019 for consultation. She added that the strategy would provide a clear programme of action for the period 2020-2024.

## **4. World Bank Ease of Doing Business Index**

The World Bank’s Ease of Doing Business report evaluates government laws and regulations that covers the ease of doing business within a country and ranks them according to an internationally recognised scale. According to the 2019 report, the global average time to prepare, file and pay taxes

has fallen from 324 hours in 2005 to 237 hours in 2017, while Sub-Saharan Africa has been the region with the highest number of reforms each year since 2012. South Africa continues to slide, from position 37 in 2014 to 43 in 2015, to position 82 in 2019. Mauritius, Rwanda and Kenya continue to outshine three foremost continental economies of Nigeria (146), South Africa and Egypt (120).

However, it is important to particularly point out that some of the variables used e.g. construction permits, getting electricity, protecting minority investors, registering property, trading across border etc. goes beyond the realm of the DSBD mandate, but require a concerted effort by government across all spheres to work together. On the other hand, other variables such as starting a business, enforcing contracts, paying taxes, getting credit and resolving insolvency etc., directly affect DSBD constituency. Previous reports have made mention of the Companies and Intellectual Property Commission (“CIPC”) and South African Revenue Services (“SARS”) as being the regular offenders. For instance in 2015, SARS was alleged to have introduced up to 15 changes for their Value Added Tax (“VAT”) submissions, while director amendments (COR39) at CIPC can take up to 60 days, not much has improved since then (report available).

## **5. The Entrepreneurial Life Cycle - Role of the State Sector**

It is vital for the Portfolio Committee members to go over and understand the life cycle of an entrepreneurial venture with a fine-tooth comb to find that missing paperwork because, in most instances, this is here where bureaucratic red tape hit them the most. Many die before they could even start. Entrepreneurial activity by 25-34 year-olds, among whom unemployment is highest, has fallen by more than 40%, and the time it takes to complete the procedures necessary to start a business in SA has more than doubled since 2015. There is a lot of risk and efforts involved in pulling up a new enterprise to a successful one. The life cycle of an entrepreneurial venture comprises numeral phases from ideation phase, various registration procedures to implementation. This is not an academic report but its purpose is to interrogate the role of the state sector players towards inculcating or depressing the culture of entrepreneurship. The process is long, winded and costly.

### **5.1 Companies and Intellectual Property Commission**

The Companies and Intellectual Property Commission (“CIPC”) presupposes that an aspirant entrepreneur has gone past ideation stage and s/he is ready to get the ball rolling. The shift away

from manual to electronic lodgement(s) is a step in the right direction for CIPC and ought to be applauded. However, for rural and township aspiring entrepreneurs seemingly, most households and individuals that we are mandated to develop, do not have access to internet, particularly where there are no internet cafes, thus the burden begins right when one must register with the CIPC as an Agent. The following procedures are therefore standard:-

- 5.1.1. Registration with CIPC as an Agent is the standard requirement, once agent code is created, it is then used or quoted as a reference when depositing funds at ABSA (R175). This is for the name reservation and Memorandum of Incorporation (“MoI”) for a private company and no transaction can take place until money reflects on the applicant’s account;
- 5.1.2 The two processes, name reservation and MoI, cannot be done simultaneously, implying additional transport and/or internet café costs for those residing in far-flung areas or without access to internet;
- 5.1.3 The applicant send four names in order of preference, starting with the most preferred, that s/he would like his or company called (R50). Once the name is approved, a process that has seen a great improvement as the approval process takes a matter of hours, an applicant can then create electronic MoI by logging into the system;
- 5.1.4 The MoI is created by filling in all the applicant personal information on the CIPC database which is linked to the Department of Home Affairs (“DoH”) database, certified ID copy or copies of all the Directors certified within three months, each Director to supply his or her physical and postal address, cell phone and telephone numbers and email addresses;
- 5.1.5 For Financial Intelligence Centre Act (“FICA”) purposes it is imperative that all personal and company information submitted is verifiable and proof of address both for the applicant and company are easily accessible or obtainable;
- 5.1.6 Once all that procedure is concluded successfully, the name reservation (CoR9.4), MoI (14.1), Notice of Incorporation (CoR14.1A), and all other supporting documentation are scanned, and lodge electronically to CIPC for final processing;
- 5.1.7 This is again an area that has seen significant improvements, one (1) day, compared five (5) years ago where it would take on average 14 days to register a private company;
- 5.1.8 Amendments, restorations and conversions are some of services currently being scaled up by CIPC to improve service delivery but still take on average 60 days to finalise;

- 5.1.9 Annual returns submission, whether the entity has traded or not, are compulsory. If not lodged, may lead to deregistration of the entity. Companies have 30 business days from the date that the entity become due to file annual returns before it is in non-compliance with the Companies Act. Most entrepreneurs have expressed displeasure at the compulsory submission of the annual returns at CIPC and SARS as creating a redundant and costly bureaucratic layer;
- 5.1.10 The utilisation of unscrupulous business advisors who charge up to R1500 to register a private company or R2500 for a co-operative is widespread on the internet and outside CIPC offices, the his is perhaps another area that should be given attention.

## **5.2 South African Revenue Services**

- 5.2.1 It is a legislative requirement that all Directors, or founding members in the case of a co-operative, to have Personal Tax Reference numbers;
- 5.2.2. Once the company or a co-operative is registered, one of the Directors whom the company or co-operative would have appointed as a Public Officer must approach SARS to apply for the Company Tax Reference number. As a matter of process or procedure, CIPC registration certificate does come out with the tax reference number. However, this does not absolve an entity from applying direct with SARS;
- 5.2.3 In a scenario where Director/s or founding members of a co-operative do not possess individual tax numbers, the law requires that they be registered, and a personal tax reference number imply a costly personal bank account;
- 5.2.4 For a co-operative with approximately 12 members, domiciled in Nyani village in Limpopo, the only SARS offices are in Giyani, Lebowakgomo, Polokwane and Sibasa, some 200 kilometres odd distance, the transport costs for all 12 members are way too ridiculous and a direct cost for members;
- 5.2.5 The discontinuation of appointing an individual or accountant through Power of Attorney (“PoA”) to conduct or engage SARS on behalf of the persons or company, is a serious regression and places serious liability for co-operatives. In the past, PoA was an acceptable and satisfactory requirement for one individual, even among the members themselves, to represent other members including applying for individual tax reference and company/co-operative tax number(s);

- 5.2.6 While SARS has improved in some areas, it has considerably regressed in others. For instance, the phasing out of a Tax Clearance Certificate (“TCC”) requirement and application is a step in the direction. The online application (sarsefilling) has now been introduced. Nevertheless, this is being introduced and rolled out without giving tax e-filers adequate training and capacity building, including its own staff. Consequently, most e-filers are either defaulting or resorting to a very expensive use of accountants;
- 5.2.7 On 14 December 2018, SARS issued a public notice that gives it permission to impose penalties on companies for not submitting income tax returns. This is a new addition to the legion of penalties already faced by companies and permits the imposition of a monthly penalty on a company ranging from anything between R250 to R16 000 a month. It is compulsory for all registered companies – small or large – to submit their income tax returns within 12 months of the end of the company’s financial year. Shockingly, dormant companies - as an example, registered companies that have no receipts or assets - are also required to file returns, to prevent a penalty being imposed;
- 5.2.8 Furthermore, SARS has a bank account obligation for both the individual and the company. In other words, individual or company/co-operative tax matters cannot be processed without a valid banking account;
- 5.2.9 Hence, the requirements to register are MoI (CoR14.1), Certificate of Registration (CoR15.1A), proof of bank for both the individual member(s)/founding member(s) and the company, proof of address for the director/founder member as well as proof of address for the company;
- 5.2.10 SARS services are free and its database is linked to DoH databank.

### **5.3 Banking Account**

- 5.3.1 As alluded to herein above, bank account requirement is mandatory in almost all the institutions;
- 5.3.2 The minimum fee to open a business account is R500, monthly charges, assuming no transactions are performed, is R80;
- 5.3.3 Opening of business account cannot be delegated;
- 5.3.4 All the directors/founding members in case of a co-operative must avail themselves simultaneously when opening a bank account, each with his/her proof of address, proof of

address for the entity, valid green or card ID book, Memorandum of Incorporation and certificate of registration;

- 5.3.5 Proof of addresses must correspond to the addresses that shall have been provided during the company registration [*as per stage 5.1 above*];
- 5.3.6 Once bank account is successfully opened, proof of bank letters are required by almost all the institutions, so it is always advisable to request a minimum of five (5) letters confirming proof of bank. Many banks only issue one, and start charging R25 per each letter issued;
- 5.3.7 All commercial and mutual banks systems and platform have a capability to interface with DoH database. The bank verifies your identity by simply placing a finger on a biometric reader which reads the fingerprint against the Home Affairs database.

#### **5.4 Black Economic Empowerment**

- 5.4.1 Black ownership is a major requirement to be considered as a supplier for most large corporates and state departments;
- 5.4.2 Qualifying Small Enterprises (“QSE”) are only excluded from a Black Economic Empowerment (“BEE”) scorecard completion when they have a minimum of 51% black ownership;
- 5.4.3 The same is also applicable to Exempt Micro Enterprise (“EME”) (annual turnover of R10m to qualify for exemption from being measured), automatically achieving a BEE level-4 recognition;
- 5.4.4 From a high of R1500 in 2015 to obtain a BEE certificate, valid only for a period of 12 months, an Exempted Micro Enterprise is now only required to obtain a sworn affidavit on an annual basis confirming annual turnover and level of black ownership or downloadable from CIPC website.

#### **5.5 Share Certificates**

- 5.5.1 In terms of the companies act (2008), it is obligatory for each director to hold or have a valid share certificate, clearly indicating shares held by each director at any given point in time;
- 5.5.2 Average fee charged by accountants to produce share certificate is usually R500.

## **5.6 National Central Supplier Database**

- 5.6.1 Central Supplier Database (“CSD”) registration for the purpose of obtaining CSD number is compulsory if one intends bidding for public sector contracts;
- 5.6.2 The registration is free of charge, fairly smooth and done online at [www.csd.gov.za](http://www.csd.gov.za);
- 5.6.3 To register, all the above processes i.e. CIPC, SARS, bank account, BEE and share certificate must have been successfully concluded;
- 5.6.4 The CSD system has an ability to interface with CIPC (it can pick up invalid registration number or outstanding annual returns), SARS (invalid or expired tax clearance certificate), invalid bank account etc.

## **5.7 Construction Industry Development Board (Optional)**

- 5.7.1 If one’s company intends doing construction, plumbing, building, storm water and/or fencing, it is obligatory that it be registered with the Construction Industry Development Board (“CIDB”);
- 5.7.2 CIDB charges R450 for each category i.e. GB and CE, a total of R900 is required;
- 5.7.3 Requirements are: 14.3/Certificate of Registration, Certified ID copy or copies if more than one Director, certified copies of Share Certificates, certified copy of BEE certificate, original Tax Clearance Certificate [not a copy], original Proof of Bank letter and original proof of addresses;
- 5.7.4 So much resources are being ploughed into construction and build industry e.g. maintenance and refurbishment of courts, hospitals, prisons, schools, construction of new student residences etcetera may well be an answer in tackling youth unemployment provided barricades preventing new enterprises from playing an active role are dismantled.

## **5.8 Other Registrations**

Depending on one’s preferred sector or industry, there are numerous other registrations, which are required to be performed e.g. Compensation for Occupational Injuries and Disease, Electrical Conformance Board of South Africa, Private Security Industry Regulatory Authority and Unemployment Insurance Fund to name the few.

## **6. Tendering Process**

In most occasions, new enterprises are enticed into the business setting mainly to take advantage of the state procurement. A tender refers to the process whereby governments invites bids for projects that must be submitted within a prescribed deadline. Tender or bid procedure can be very cumbersome and complex for a new entrepreneur. The entire bidding process, right from the point of accessing tender advert or bulletin to the stage of submitting tender documents is extremely costly, tiresome and one of the major obstacles that make it extremely difficult for a new enterprise to break into the market. Small businesses, especially, find it particularly difficult to overcome barriers to entry. In a market with large and well-established enterprises dominating the market share, it is virtually impossible for newcomers to get a foothold. Not only is it hard to get in, but also difficult to thrive if they manage to enter. While in some cases, as this Portfolio Committee has established, big businesses deliberately and ruthlessly strangle small enterprises out of the market.

Hence, South Africa has one of the highest mortality rates in the world. Barriers to entry protect the companies that currently dominate a sector because new rivals are unlikely to appear. Even if some do appear, they will probably remain small because the barriers keep them down. As a result, for every success story, several businesses do not make it through the first two years of existence. There are few pertinent areas for further examination by DSBD, these include but not limited to:-

### **6.1 Bridging the Divide between the Small and Well-established Businesses**

The inflexible and irrational requirements e.g. CIDB grading of five (5) GB, CE, SQ and above, experience and financial capability are still being used perversely to eliminate small enterprises from participating in what others call, first or formal economy. In other countries, the power of the purse is most often utilised by government to induce big businesses to collaborate with small enterprises. In the case of South Africa, this practice has not been enforced, and small enterprises are still being barred from entering lucrative value chains.

In particular, the construction and build, wholesale and retail, financial services, light manufacturing as well as agriculture and agro-processing are just few of the crucial sectors, with beneficial upstream and downstream opportunities, within reach for small enterprises. They have the propensity to make an expressive contribution in confronting socioeconomic misfortunes ravaging our country but the government keeps faltering in creating a conducive environment for small

enterprises to seize these opportunities. For instance, in the United States, Small Business Jobs Act “directs the head of each federal agency to ensure that its decisions regarding consolidation of contract requirements are made with a view to providing small business concerns with appropriate opportunities to participate as prime contractors and subcontractors”.

## **6.2 Sale of Tender Documents**

One of the strategic motive behind the creation of the Chief Procurement Officer (“OCPO”) was to modernise and centralise procurement activities into a single point of entry for the state. Furthermore, OCPO created a web portal or depository of all state tender documents <https://etenders.treasury.gov.za/> but the usage of this portal remains fairly subdued. The technology is a powerful lever that could provide transparency and break down barriers to entry. Suppliers in government are like an old boys’ club, the sector is concentrated and difficult for new competitors to penetrate. However, bid documents are still being sold at an exorbitant amount of money when they could very well be downloaded from the web portal. This is one of the major impediments for hopeful entrepreneurs to enter the market that require careful attention.

## **6.3 Cancellation of Bids**

Possibly one of the most painful injustice to young and upcoming entrepreneurs are cancellation of the tender process. Once cancelled, bidders are not entitled to refund. This is one area of supply chain management that is prone to corruption as it is often alleged that bids are cancelled in order to eliminate rivalry. Obviously, lot more resources would have been spent before bid is cancelled e.g. acquiring bid documents, attending briefing sessions, collation of other supporting documentation, delivery (courier, posting and overnight). The amount of money being lost by aspirant entrepreneurs run into millions.

## **6.4 Briefing Sessions**

Similar to 6.3 above, some bids do not require compulsory briefing sessions, site meetings or information sessions. Nonetheless, some state departments and municipalities insist on briefing sessions and use such as one of the evaluation criteria. These are meetings that are held before the quotation or a competitive bid (tender) is due. Most of the time these sessions are compulsory and not attending them can and might most probably lead to a tender response being disqualified. There

is not a doubt that for some bids, these sessions are critical but making them compulsory defeats their purpose.

### **6.5 Late Payment of Service Providers**

The issue of the late payments of service providers both by the private and state sector is one of the foremost challenge plaguing small enterprises. Until recently, the private sector, owing to lack of transparency, statutory reporting and accountability similar to state sector, has been operating below the radar without attracting much controversy. The root of the problem with the private sector is that, most small businesses are selling to companies larger than themselves, who have the advantage of a full-time finance director. These seasoned professionals know how to manage cash-flow, and therefore how to improve their companies' bottom line instantly by quietly moving payments from thirty to ninety days.

In terms of the Public Finance Management Act ("PFMA") and the Municipal Finance Management Act ("MFMA"), Accounting Officers are required to settle all contractual obligations and pay all money owing, including intergovernmental claims, within the prescribed and agreed period. However, due to lack of consequent management late payment of services providers continues unabated. Numerous National Treasury regulations specifying that the prescribed period for the payment of suppliers is 30-days from receipt of a legitimate (undisputed) invoice have been issued, Cabinet briefings and recently, the establishment of a special Unit in the Department of Planning, Monitoring and Evaluation to tackle the problem of non-payment of suppliers within 30 days. During the fifth Parliament, the Portfolio Committee lengthily dealt with this matter, including carefully examining the role of the private sector, and reached a conclusion that the time was opportune to legislate.

### **6.5 Other Exclusionary Practices**

Exclusionary practices are prevalent especially in the money-spinning sectors of the economy. Such tendencies manifest themselves through irrational contracts, pricing strategies and more commonly actions taken by dominant firms to deter new competitors from entering an industry, to mercilessly force competitors to exit the industry, to restrain rivals in their own little corner, and/or to prevent them from expanding.