



Open Contracting and Inclusion

Preferential Procurement

South Africa

This case-study is part of a larger study that explores the possible benefits of open contracting for marginalized communities. Research was done by Francois van Schalkwyk & Miko Cañares. The complete study and results are found [here](#).

The passing of legislation to make public procurement more inclusive, particularly in terms of the inclusion of marginalized groups such as women, small businesses and the youth, is becoming increasingly common. The African Union roadmap on harnessing the so-called ‘demographic dividend’ offers general recommendations on employment and entrepreneurship, including increasing youth’s access to government procurement and finance facilities (AU n.d.). And there are several examples globally of initiatives that seek to include small- to medium-sized enterprises (SMEs) in public procurement opportunities (see DCED [2017] for a comprehensive overview of policies that promote SME participation in public procurement). There are, however, relatively few examples of initiatives that target specific marginalized groups (DCED 2017). South Africa is one such country.

Context

South Africa has been plagued by corruption in public procurement and expenditure since the dawn of democracy in the country in 1994 (PWC 2014, 2016). In October 2016, shortly before he retired as the National Treasury’s chief procurement officer, Kenneth Brown warned that up to 40% of the state’s total procurement budget, then worth ZAR600bn, was tainted by ‘inflated prices and fraud’. In November 2018, Auditor-General Kimi Makwetu reported that irregular expenditure¹ by national and provincial departments, as well as some state-owned entities amounted to approximately ZAR51-billion. Some of the reasons behind this exorbitant figure include non-compliance with procurement laws and unfair procurement practices. Corruption at all levels of government has hampered the delivery of public services (particularly in health, education and transport), and crippled public utilities which, in turn, have dented investor confidence and hampered the development of the country.² This has left previously disadvantaged and other marginalized communities on the fringes.

At the same time, South Africa has made several global commitments to combat systemic corruption. These include its statement on anti-corruption commitments at the London Anti-Corruption Summit in May 2016; its membership of the Open Government Partnership, a global member organization that promotes open and transparent government; and its membership of

¹ Any expenditure which does not comply with the Public Finance Management Act (PFMA).

² <https://city-press.news24.com/Voices/politicians-loot-without-consequence-no-wonder-the-people-take-law-into-their-own-hands-20190926>

the G20 Group of countries which established the Anti-Corruption Working Group in 2010,³ and developed in 2014 the G20 Anti-Corruption Open Data Principles⁴ as a step towards leveraging open data as a crucial tool to enable a culture of transparency, accountability and access to information to prevent corruption. A report published by Transparency International⁵ in 2017 found that South Africa is commitment rich and implementation poor; that too few key anti-corruption datasets are available as open data; and that the use of open data to make government more transparent in efforts to combat corruption is not even across government departments (Van Schalkwyk 2017).

South Africa has in place a legislative framework that aligns with the principles of open contracting (see Naidoo et al. 2018). As in the case of its global commitments, the law is poorly implemented (Naidoo et al. 2018). In January 2017, the South African government passed legislation requiring that all public contracts that exceed a prescribed amount must include provisions for the outsourcing of at least 30% of the contract to designated previously disadvantaged groups, that is small businesses owned by black people, black youths, black women, black people with disabilities, black people living in rural or underdeveloped areas or townships, a cooperative owned by black people or black military veterans.⁶ The promulgation of this legislation is an attempt by government to use its purchasing power to achieve economic transformation or, in terms of the interest of this study, greater inclusion in the contracting process and in the awarding of public contracts.

This legislation came into effect in a context where globally the construction, energy and mining sectors experience the highest levels of bribery (PWC 2014). In 2013, the country's Competition Commission levied fines of approximately R1.4bn (USD93m) on construction companies that had colluded to inflate costs for the construction of football stadiums. The introduction of the legislation has had unexpected effects on the construction industry. Small contracting firms insist that despite the provisions for preferential procurement, they remain excluded from larger construction contracts. Frustrated by their lack of inclusion, they have mobilized existing business

³ <https://star.worldbank.org/star/about-us/g20-anti-corruption-working-group>

⁴ <http://www.g20.utoronto.ca/2015/G20-Anti-Corruption-Open-Data-Principles.pdf>

⁵ https://www.transparency.org/whatwedo/publication/open_data_and_the_fight_against_corruption_in_south_africa

⁶ Preferential Procurement Regulations, 2017.

forums and disrupted work on construction sites to draw attention to their demands for the implementation of the outsourcing provisions in public procurement legislation.

The inclusive contracting initiative

Principles of open contracting are provided for in the South African constitution which, in a specific section on procurement, states that all public contracts for the provision of goods and services must be fair, equitable and transparent (Constitution of South Africa 1996, section 217[1]). South Africa also has in place over 80 legal instruments related to public sector procurement and a legislative framework that aligns with the principles of open contracting (Naidoo et al. 2018).

The Preferential Procurement Policy Framework Act No. 5 of 2000 came into effect on 1 April 2017. Tolo Nkosi, the CEO of Umso Construction,⁷ describes the Framework as a necessary 'platform for participation' between communities, small businesses and their larger counterparts.

There are three subcontracting rules in the Preferential Procurement Regulations that organs of state must adhere to when issuing tenders to the general public:

1. Regulation 4 states inter alia: if an organ of state decides to apply pre-qualification criteria to advance certain designated groups that organ of state must advertise the tender with a specific tendering condition that only certain bidders may respond.
2. Regulation 9 states inter alia: if it is feasible to sub-contract for a contract above R30 million, an organ of state must apply sub-contracting to advance designated groups. The designated groups mentioned in Regulations 4 and 9 are small and micro enterprises owned by:
 - a. at least 51% by black people;⁸
 - b. at least 51% by black people who are youth;
 - c. at least 51% by black people who are women;
 - d. at least 51% by black people with disabilities;

⁷ <https://www.youtube.com/watch?v=SJyU0MI5WWw>

⁸ A 'black person' is defined in the Broad-Based Black Economic Empowerment Act No. 53 of 2003 as 'is a generic term which means Africans, Colored's and Indians'.

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- e. black people living in rural or underdeveloped areas or townships;
 - f. a cooperative which is at least 51% owned by black people;
 - g. at least 51% by black people who are military veterans;
3. Regulation 9 also states that if an organ of state applies subcontracting, it must advertise the tender with a specific tendering condition that the successful tenderer must subcontract a minimum of 30% of the value of the contract to designated groups.

A fourth subcontracting rule is related to the subcontracting of the tender after the award. Regulation 12 states inter alia: a person awarded a contract may not subcontract more than 25% of the value of the contract to any other enterprise that does not have an equal or higher B-BBEE status level of contributor than the person concerned, unless the contract is subcontracted to an EME that has the capability and ability to execute the subcontract.

Organs of state are expected to apply these regulations rigorously.

In February 2013, in his annual budget speech, minister of finance Pravin Gordhan revealed that the government had appointed a new chief procurement officer as part of its fight against corruption and to bring public procurement in line with the provisions of the Constitution (National Treasury, 2015).

The Office of the Chief Procurement Officer (OCPO) is a division of the National Treasury, and its main aim is to restructure and simplify governmental procurement processes. The strategic objectives of the OCPO rest on five pillars: (1) value for money; (2) open and effective competition; (3) ethics and fair dealing; (4) accountability and reporting; and (5) equity.^{9,10} It is evident that openness is a central tenet that cuts across most of the pillars.

One of the six functions of the OCPO is ICT, e-procurement and data management (National Treasury 2015). However, technology is not seen as playing a central role in creating a more

⁹ "The word 'equity' in the context of these Guidelines means the application and observance of government policies which are designed to advance persons or categories of persons disadvantaged by unfair discrimination. This fifth pillar is vital to public sector procurement in South Africa. It ensures that government is committed to economic growth by implementing measures to support industry generally, and especially to advance the development of Small, Medium and Micro Enterprises and Historically Disadvantaged Individuals."

¹⁰ http://ocpo.treasury.gov.za/About_Us/Pages/Strategic-Objectives.aspx

open procurement process; rather, the focus is on technology's role in improving the performance of the procurement process: "Technology is employed to simplify, standardize and automate SCM with a view to optimize performance."¹¹

Publication of public contracting data has lagged behind government policy and strategic objectives of the OCPO. According to a 2015 National Treasury report (2015: 22), procurement practices were not always implemented in line with legislation. For example, although procurement notices were published, no bid documentation was available online; minutes of the Bid Evaluation Committees were not available for public access; contracts entered into with winning firms were not available for public scrutiny; some bids were not opened in public and the list of bidders was not published; the bid evaluation process was not open to public scrutiny; and contract progress reports were not publicly available.

A 2015 survey of procurement officials in South Africa found that only 59.7% of respondents agreed that procurement information is available via a central portal (Naidoo et al. 2017). The South African government committed to improve transparency in the public procurement process by: (a) developing and prescribing a public disclosure framework, which governs transparency within the procurement process; (b) prescribing that all information in the bid process be disclosed publicly; (c) improving the accessibility of information; (d) improving the quality of information and encouraging its strategic use; (e) creating an environment conducive to stakeholder participation in the different stages of the procurement process; and (f) building the capacity of the private sector, civil society and relevant stakeholders to take part effectively in enhancing transparent public sector procurement (National Treasury 2015: 23).

Commitments were also made to improve the public procurement system so that it "will enable electronic validation of supplier tax compliance. Suppliers will also be able to register and maintain their details on a central supplier database, thus eliminating unnecessary effort and cost. Tender portals, e-procurement platforms and e-auctions will be among the options available to suppliers competing for government business" (National Treasury 2015: 65).

¹¹ http://ocpo.treasury.gov.za/About_Us/Strategic_Areas/Pages/Information-and-Communication-Technology.aspx

National Treasury acknowledges that “capacity is generally weak with practitioners unable to conceptualize and implement tenders aligned with government’s developmental objectives” (National Treasury 2015: 14).

Since the publication of the 2015 report by National Treasury, a central supplier management system has been implemented as well as an electronic tender information portal. However, ongoing calls by civil society suggest that not enough progress has been made:

While there have been some noteworthy reforms in the country’s procurement landscape, we are deeply concerned by what appears to be some loss in momentum and commitment on this front. The establishment of the Office of the Chief Procurement Officer in 2013 as well the introduction of government’s e-tender portals and central supplier databases in 2015 constitute fundamental strides towards more transparent government systems. However, it is clear that more can – and must – be done (Selabalo et al. 2019).

An assessment of the e-tender portal conducted as part of this study shows that, in general terms, progress has been made in increasing the amount of information available on public tenders and in centralizing all government tenders in one online space. However, it is also clear that integrating tender information across multiple government entities remains a challenge. Presenting information in standardized formats highlights the many gaps public in procurement data.

The experience of the International Budget Partnership South Africa (IBP) (South Africa) is instructive in relation to the limitations of the e-tender portal. IBP supports citizen monitoring of public goods and service delivery (social audits) by grassroots organizations that engage directly with government to improve the quality of civil goods and service provision. IBP has published several papers and reports on public procurement,¹² including “A Guide to Finding Information About Municipal Contracted Services in Your Community”¹³ and “Monitoring Public Procurement In South Africa: A Reference Guide For Civil Society Organizations”.¹⁴

¹² <https://www.internationalbudget.org/budget-work-by-country/ibps-work-in-countries/south-africa/>

¹³ <https://www.internationalbudget.org/publications/south-africa-guide-to-finding-information-about-municipal-contracted-services/>

¹⁴ <https://www.internationalbudget.org/publications/monitoring-public-procurement-south-africa-guide/>

As part of its approach, IBP helps community-based organizations to work with poor, marginalized and often largely illiterate communities, to find and understand procurement documents to monitor whether the services provided meet the standards defined in public contracts. The end result is to create feedback loops between government, civil society organizations and the public.

IBP has consulted communities to determine the types of information that are needed for their monitoring activities. These include: bid specifications; a centralized list of current contracts that specify when the contract is due to start and expected to end; whether a tender used an open tender process; and information on extensions. In an ideal scenario, IDB suggests that communities would be able to access information about the timeline of all phases (tender start and end dates, award date, contract start and end dates), and what should be public at each point (the legally mandated publishing requirements). This would enable them to compare what is actually being published against the mandated information requirements, which would enable them to spot missing information and correct information. Tracking the quality of services and goods requires information on what the final good or service is supposed to look like (technical specifications). Key information for signed contracts includes a description of each phase of development, and by those phases that should be completed (milestone dates and milestone descriptions).

While IBP reports successful outcomes from the social audits, these rely on direct engagement between affected communities and their local governments. IBP reports that their partner community-based organizations are unable to rely on government procurement portals to access comprehensive and reliable data on public contracts awarded for the delivery of goods and services to marginalized communities and that no mechanism is in place for the data needs or information gathered from social audits to be fed into government's central procurement system.

From the perspective of prospective bidders, not all bidders are equally placed to access online procurement data, with those targeted by preferential procurement legislation being less likely to find the e-tender portal accessible. According to Tolo Nkosi, the CEO of Umso Construction, many of the business forums discover only new contracting opportunities when their communities are included in pre-contracting consultations initiated by successful bidders. In

other words, the small businesses that represent marginalized communities (black South Africans, youth, women) do not access data or information from online procurement portals and must rely on the actions of successful bidders for an opportunity to participate in large public construction projects.

Given the current design of the e-tender portal, even if access to the portal was to be improved, it is not possible to filter tenders on the e-tender portal by tender amount/value making it impossible to locate those tenders that are required by law to subcontract 30% to designated groups.

Outcomes

Government's policy to regulate the awarding of public contracts to designated groups combined with the interpretation and implementation of the regulations by successful bidders, has led to unanticipated, negative outcomes. Frustrated small, black-owned businesses have resorted to occupying construction sites, and threatened violence and other intimidatory tactics, in cases where they believe contractors are not subcontracting as per the conditions of their tender awards. There are also reports of increased levels of corruption to secure subcontracts.

The Delangokubona Business Forum allegedly occupied construction sites in the KwaZulu-Natal province and threatened violence as it demanded a share in major construction contracts. The Forum's intimidatory tactics stalled several construction projects in the province.¹⁵ In April 2018, the Forum, acting together with the military veterans association and a local taxi group, brought a large road construction project outside Durban to a halt.¹⁶ The group demanded a 30% stake in these construction projects, saying local black business must be given its fair share of local projects. Similar demands are being made by forums in other parts of the country.¹⁷

The demand for a fair share of contracts is also reportedly what lays behind the killing and injuring of mineworkers from the Modikwa Platinum mine near Burgersfort in Limpopo in April 2018. A

¹⁵ <https://www.timeslive.co.za/news/south-africa/2016-06-04-durban-building-site-shut-down-after-workers-assaulted/>; <https://www.timeslive.co.za/news/south-africa/2018-02-09-mafia-style-business-forum-halts-multi-million-road-project/>; <https://citizen.co.za/business/2105688/kzn-business-forum-denies-beng-behind-mafia-attacks-on-construction-projects/>

¹⁶ <https://www.timeslive.co.za/news/south-africa/2018-02-09-mafia-style-business-forum-halts-multi-million-road-project/>

¹⁷ <https://www.moneyweb.co.za/news/south-africa/construction-mafia-moves-from-kzn-to-joburg/>

local official from the National Union of Mineworkers blamed the deaths on local business people trying to 'gain access to contracts'. This assessment was echoed by a traditional leader, Chief Masiya Mohlala, who said that 'conflict among people competing for mining tenders in the area was the root cause of the problem, with desperate unemployed young people being used to instigate violence against competitors' businesses'.¹⁸

The Federation for Radical Economic Transformation (Fret)¹⁹ was established in 2017 to represent the growing number of business forums. Fret represents more than 30 business forums, including the Delangokubona Business Forum, which reportedly has more than 3 000 members. According to Malusi Zondi, the president of Fret, for small and micro enterprises that qualify under the provisions of the preferential procurement regulations, exclusion persists because the decision to subcontract rests with the successful contractor, and there is no mechanism in place to monitor whether or how the contractor has awarded subcontracts.²⁰

Competition for BEE construction contracts is also contributing to new forms of corruption. One example is the reported rigging of the ruling government party's internal elections. Says ANC member Omry Makgoale: 'There is a process of paying for bulk [ANC] memberships at construction sites, where businessmen will pay large sums of money for people to become ANC members. These people have no clue about ANC policies, their sole task being to vote for specific slates at an [ANC] conference that will secure these businessmen ... the promise of future tenders.'²¹

Without full transparency, accountability and remedial action, a well-meaning regulatory intervention in public procurement has had the unintended consequences of furthering corruption.

¹⁸ <https://irr.org.za/media/the-bee-sting-that-kills-2013-analysis-of-a-policy-gone-horribly-wrong-biznews>

¹⁹ <https://www.facebook.com/FFRETSA/>

²⁰ <https://iono.fm/e/670584>

²¹ <https://city-press.news24.com/Voices/anc-killings-are-caused-by-rigged-conference-elections-20180517>

Case analysis

As set out in the conceptual framework, it is important to understand the distribution of power if one wishes to understand the likely effects or impact of making certain data openly accessible. In this case, power is concentrated in a small network of large construction companies, often referred to in the country as the 'Big Five'.²² While these construction companies form a tight network in South Africa, they are intricately connected to global capital markets. All are listed on the Johannesburg Stock Exchange and count global investors among their shareholders. Any attempts at introducing greater transparency and accountability in this sector -- or ones that seek to distribute the benefits of public contracting more equitably -- must take into account the dominance of large construction companies and their ambitions that are defined in terms of global capital markets rather than local needs and priorities.

The South African case has shown how a critical change in procurement conditions was effected with the introduction of new legislation aimed at bringing previously excluded and marginalized businesses into the public procurement process as primary beneficiaries of public expenditure. In other words, through legislation, the government of South Africa created an opportune niche in public procurement. This has created a space for business forums to enter into procurement negotiations on behalf of their members who are typically small businesses or sole proprietorships located in or near sites where large public works are taking place. These business forums are, in other words, intermediaries between their representative constituents and the large construction companies, and have 'emerged' as a result of regulations requiring the participation of small businesses owned by marginalized communities in large publicly-funded construction projects.

While National Treasury has sought to make the procurement process more transparent and efficient by developing a central supplier database and e-tender portal, there is no evidence that these technologies have disrupted the asymmetrical flows of data that have historically favored the big construction companies. Data published is incomplete and inconsistent, precluding the e-tender portal from connecting marginalized communities to government.

²² <https://constructionreviewonline.com/2018/07/top-construction-companies-in-south-africa/>

Those intermediaries that have emerged to provide new, third-party websites and tools for identifying relevant public tenders appear to target established businesses. No intermediaries have emerged to connect what data is available to those marginalized business owners who are expected to benefit from the introduction of the preferential procurement regulations. These business owners only become aware of large construction projects when they break ground rather than at earlier phases of the construction process when there are likely to be favorable opportunities to negotiate participation and partnership in public tenders. There is, therefore, no organization attempting to translate when data is published into more usable (valuable) data for those communities identified as beneficiaries in the procurement regulation.

At the same time, as the work of the IBP illustrates, the absence of award and project implementation data on the e-tender portal, make it impossible for communities where public services or works are being delivered to conduct monitoring and accountability exercises.

In short, legislation has created the opportunities for increased inclusion of marginalized communities as primary beneficiaries of public expenditure. However, the publication of poor quality data from only a part of the public contracting process, places limits on more effective participation and monitoring of public procurement by marginalized communities. The result is business as usual in the awarding of large public construction projects, and a lack of transparency regarding the outsourcing practices of the large construction companies, leaving those traditionally marginalized from public procurement to resort to more aggressive tactics to challenge existing power structures in order to lay claim to their legally-enshrined right to participate.

Unlike in the Bantay Kita case, no trusted intermediary has emerged in South Africa to engage across the spectrum of stakeholders and suppliers, to create value from the available data and to mediate solutions to the undesired outcomes that have materialized.