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# THE AMENDED BEE CODES AND OWNERSHIP STRUCTURES

The amended BEE Codes were published in the Government Gazette of 11 October 2013. They will come into operation within 12 months from the date of publication.

The amended Codes will replace the Codes which were published in February 2007.

Many companies have been restructured so as to comply with the ownership requirements of the 2007 Codes.

This circular looks at the impact on the ownership provisions of the 2013 Codes and how structures established under the 2007 Codes will require amendment.

## THE RAISED THRESHOLDS AND NEW DEEMING PROVISIONS

The thresholds for exempted micro-enterprises and qualifying small enterprises have been raised. Previously, the threshold for an exempted micro-enterprise was an annual turnover of R5 million or less. This has been increased to an annual turnover of R10 million or less.

The threshold for a qualifying small enterprise was previously between R5 million and R35 million turnover. The turnover threshold has now been raised to between R10 million and R50 million.

An exempted micro-enterprise is deemed to have a BBBEE status of a Level 4 contributor. If the exempted micro-enterprise is 100% black owned, it then qualifies for elevation to a Level 1 contributor.

If the exempted micro-enterprise is at least 51% black owned, then it is deemed to be a Level 2 contributor. Despite the deeming provisions, the exempted micro-enterprise is allowed to be measured in terms of the QSE Scorecard.

The exempted micro-enterprise simply has to obtain a sworn statement on an annual basis confirming its total revenue and level of black ownership. This would then entitle it to the relevant deemed score.

The same principles apply to a qualifying small enterprise. A qualifying small enterprise which is 100% black owned is deemed to be a Level 1 contributor. A qualifying small enterprise which is 51% black owned is deemed to be a Level 2 contributor. The qualifying small enterprise is only required to obtain a sworn affidavit, on an annual basis, confirming that its annual total revenue is less than R50 million and its level of black ownership.

## PRIORITY ELEMENTS AND ENHANCED RECOGNITION

The Codes introduce a new concept of priority elements. In respect of ownership, the minimum requirement for ownership is 40% of net value based upon the time based graduation factor. The time based graduation factor provides for the reduction, over time, of the level of debt attributable to the economic interest held by the black participants relative to the value of the economic interest.

If a large enterprise or a qualifying small enterprise does not qualify for the minimum requirement for ownership, then its general score will be discounted by one level down until it does qualify.

Start up enterprises may be measured as exempted micro-enterprises during their first year following their formation regardless of their expected total revenue.

Ownership on the generic scorecard now counts for 25 points whereas under the 2007 Codes, it counted for 20 points.

Enhanced recognition is given to black women and black people with disabilities, black youth and black people living in rural areas.

## THE FLOW THROUGH PRINCIPLE AND THE MODIFIED FLOW THROUGH PRINCIPLE

The flow through principle, as contained in the 2007 Codes, as read with the modified flow through principle, has been retained. The flow through principle is that the rights of ownership of black people in a measured entity, which is a juristic person, flow through the different tiers of ownership until it ends with a natural black person holding rights of ownership. The modified flow through principle is to the effect that in the chain of ownership, if black people have a flow through level of participation of at least 51% in one measured entity, then the black participation is treated, for that entity, as if it is 100%.

## BROAD BASED OWNERSHIP SCHEMES AND EMPLOYEE SHARE OWNERSHIP SCHEMES

Additional requirements have been imposed for broad based ownership schemes. These include :

(a) the constitution of the scheme must define the participants and the proportion of their claim to receive distributions;

(b) a written record of the name of the participants or the use of a defined class of natural person satisfies the requirement for identification;

(c) a written record of fixed percentages of claims or the use of a formula for calculating claims satisfies the need for defining proportion of benefit;

(d) the fiduciaries of a scheme must have no discretion on the above mentioned terms;

(e) the independent trustee must have no employment with or direct or indirect beneficial interest in the scheme;

(f) at least 50% of the trustees must be black people;

(g) the constitution, or other relevant statutory documents of the scheme, must be available, on request, to any participant in an official language in which that person is familiar;

(h) the trustees must present the financial reports of the scheme to the participants yearly at an annual general meeting of the scheme.

An additional rule has been added for employee share ownership programmes. This is that all accumulated economic interest of the scheme is payable to participants at the earlier of the date specified in the scheme constitution or on the termination or winding up of the scheme.

## RULES FOR TRUSTS AND FAMILY TRUSTS

The rules for trusts remain the same.

New rules have been inserted for family trusts. Family trusts are not expressly defined in the Codes.

The qualifying criteria for the recognition of a family trust are that the trust deed defines the beneficiaries and the proportion of their entitlement to receive distributions, there is a written record of the name of the beneficiaries or the use of a defined class of natural persons and there is a formula for calculating entitlement defining the proportionate benefit. In addition, only the trustees must have discretion on these terms and on winding up or termination of the trust, all accumulated economic interest must be transferred to the beneficiaries or to an entity representing the interests of the participants or class of beneficiaries.

## PRIVATE EQUITY FUNDS

Additional requirements have been inserted for private equity funds.

The 2007 Codes stated that more than 50% of the value of the funds invested by any private equity fund must, at all times, be invested in black owned enterprises that were at least 25% black owned before the investment of the private equity fund. This requirement has been watered down to 25% black shareholding using the flow through principles. In addition, the private equity fund can facilitate direct black shareholding at the time of entering into the transaction should the target company not meet the requirement of at least 25% black shareholding at the time that the transaction is concluded.

The amended Codes also state that in recognition of the fact that it is currently a challenge for private equity fund managers to find companies to invest in that already have a significant black shareholding, in practice, it should be allowed to achieve the 51% target over a period of time based on a new formulation set out in the Codes. The rule will apply to all investments made after 11 October 2014. The commencement date is the later of 11 October 2014 and the date of establishment of a new fund.

Within one year from the commencement date, more than 5% of the value of the funds invested by the private equity fund must be invested in enterprises that have at least 25% black shareholding. Within two years, this increases to 10%. In the third year, it increases to 20%, the fourth year 25%, the fifth year, 30%, the seventh and eighth year 40% and in the ninth year, at least 51%.

## CONCLUSION

Companies will have one year to comply with the new Codes published on 11 October 2013.

The rules for micro-enterprises and qualifying small enterprises have been simplified where they are 100% black owned or 51% black owned. Ownership has now been treated as a priority element with a penalty provision if the minimum requirement has not been met. A penalty applies to both a large enterprise and a qualifying small enterprise. The ownership element of the scorecard has also been increased.

Broad based ownership schemes will have to be amended so as to ensure that their constitutions are consistent with the new provisions. The same applies to employee share ownership schemes. In some cases, this will be difficult to achieve.

The deeds of trust of family trusts will probably also have to be amended so as to ensure that they are consistent with the provisions relating to family trusts.

The rules relating to private equity funds have been relaxed but it will be difficult to ensure that there is compliance with the time based provisions requiring that the value of the funds invested in companies which have at least a 25% black shareholding increase from 5% within the first year to 51% by the ninth year.

## FURTHER ADVICE

Should you require advice or assistance on the amended BEE Codes and Ownership Structures so as to comply with the revised Codes, please contact Michael Jackson on 031 – 536 8512, email : **mjackson@coxyeats.co.za**. Keren Watson on 031 - 536 5818, email : **kwatson@coxyeats.co.za** or Simon Watson on 031 - 536 8530, email : **swatson@coxyeats.co.za** or Jason Goodison on 031 - 536 8517, email : **jgoodison@coxyeats.co.za** or Jenna Padoa on 031 - 536 8529, email : **jpadoa@coxyeats.co.za**.