

# A country at the crossroad towards better regulatory governance in South Africa

South Africa is sitting at an economic crossroad. The National Development Plan proposes many measures to accelerate economic growth and deal with the country's rising social problems. The majority of these are based on the assumption of a reasonably healthy economy.

There is a problem however. Since the introduction – and acceptance of the NDP as South Africa's new economic blueprint - the country's growth rate is hovering at 1.4%. That's far below the minimum 5.4% that the NDP calls for over the next fifteen years. Unemployment has risen to its highest levels, 25.6% under the strict definition and, according to Statistics SA, 16 million people are expected to draw social benefits over the next year at a cost of 60% of government spending.

South Africa needs an economic ecosystem that is designed to support market-driven inclusive growth, provide quality jobs, rapid skills development, innovation, increased productive output and better means to compete in a global economy.

## More business, more employment

Two things are needed to achieve the growth rates planned for in the NDP and rein in unemployment. Firstly, the growth and expansion of existing businesses and, secondly, the emergence of viable new ones. In particular, it is to the small to medium enterprise (SME) sector – acknowledged worldwide as the chief generators of jobs – that the country must look towards.

Government policy certainly seems to support these aims. But the reality is at odds with the language of the NDP. The World Bank's Doing Business report evaluates government laws and regulations which cover the ease of doing business within a country and ranks them according to an internationally recognised scale. Their 2015 report makes a valid point. It argues that government has the power to either support, or bring down, a country's economy. In just the past year alone, South Africa has dropped six places in the Ease of Doing Business rankings, from 37th in 2014 to 43rd in 2015.

Year on year, SBP's SME Growth Index has repeatedly reported business owners saying that it has become harder to do business in South Africa, with 71% saying that the environment had become more hostile in 2013 than in previous years. Leading causes inhibiting the growth and expansion of their businesses include lack of skills, burdensome regulations, local economic conditions, lack of finance and the cost of labour.

Examples cited are many. In just this year, SARS introduced up to 15 changes for their VAT submissions. Small business owners can spend up to 11 days on each case taken to the CCMA. Completing all the necessary administrative steps to open a business can take between 60 to 90 days, far in excess of countries such as Mauritius

## A country at the crossroad – towards better regulatory governance in South Africa

where it takes only 3 days to register a new business. Respondents to SBP's SME Growth Index report that it can take up to eight months to receive a CoR39, the documentation that reports changes to a company's directors and fundamental for the business to operate its banking accounts.

The average small business owner doesn't have the resources to hire experts that ensure they are meeting an increasingly long list of compliance requirements, and many are not even aware of regulations that would have direct impact on their ability to do business. The government looks to the SME to support the country's growth and employment targets but offers little efficacy when it comes to providing guidance and support in return.

The United Kingdom for example, cites 6 simple steps on its official website that a business has to follow in employing a person for the first time. South Africa's official website in comparison, lists more than three pages of the steps necessary to hire an employee – a veritable labyrinth – and these relate only to compliance with the country's labour laws.

Government is clearly aware of the problem. Earlier this year, the Small Business Ministry was established. It was posited as part of government's commitment to cutting back on red tape and to help boost support for small businesses. Yet almost seven months from its establishment, there have been no major policy overhauls or clear-cut announcements on how the new ministry intends to bring South Africa on track when it comes to supporting the small business sector. Instead, positive statements that have been made seem directly at odds with regulatory proposals from other ministries, illustrating a lack of coherence in government policy.

### **Contradictions and inconsistencies**

Business regulation, and small business regulation in particular, suffers from a case of ambiguous motivation. While the vision of the NDP is market-friendly, government policy and its implementation is all too often contradictory to its aims, resulting in an increasingly hostile environment that hampers business growth, especially SMEs.

Speaking at the American Chamber of Commerce in November 2014, Finance Minister Nene stated that the next two years were likely to be tough for the South African economy and that the country would need to rely on the "dynamism and agility" of the business sector in order to grow. Nene was clear on the point that business would play a vital role in innovation and job creation.

Nene's speech however failed to recognise the growing stagnancy of small firms in particular as job creators. These firms are expected to cater for a large percentage of employment, but findings from the Stats SA Labour Force Survey show that small firms (those employing less than 50 employees) have shed over 1m jobs in the five years to 2013. Smaller firms are becoming less important as job creators in South Africa, in direct contradiction to findings from studies worldwide where small to medium size firms are found to be the drivers of net new job creation.

Studies conducted by SBP and Professor Neil Rankin of Stellenbosch University provide one explanation for this. Smaller firms, particularly in the manufacturing sector, are failing because they are not able to adjust their wages down in response to competition. This is because of their being bound by inflexible bargaining council wage agreements. The Labour Relations Act binds all parties, irrespective of whether they were party to wage agreements, to wage rates that are extended across whole sectors. This forces smaller firms to pay above median wage rates, irrespective of whether they can afford to do so and in many cases force smaller firms to close down. Yet despite this increasing evidence – and a number of cases currently being heard in our high courts - on the negative impact of collective bargaining on small firms, government has stated its intention to introduce a national minimum wage in tandem with the current collective bargaining machinery.

In a similar vein, the Department of Trade and Industry's Deputy Minister, Masina recently spoke about the need to stimulate employment in South Africa, to keep jobs in the country and use the skills here to support the continent's

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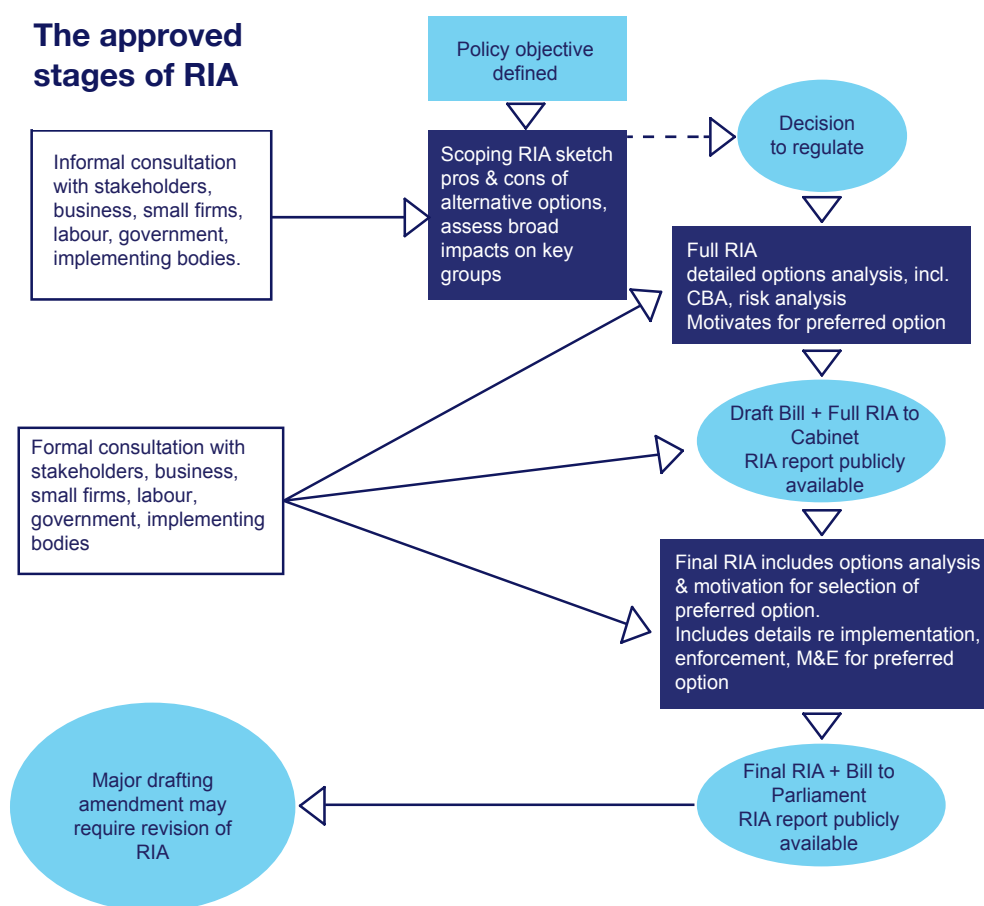
industrial base. Yet he had little to say on how his own department's new BBB-EE Codes and amendments to the Act might have the very opposite effect by reducing the country's local supply and value chains.

The new Codes of Practice for Broad Based Economic Empowerment that will come into effect next year make it harder to employ skilled people, and far more restrictive. Changes to the Act and the Codes will shift policy on a fundamental level, introducing punitive penalties as well as influencing a firm's ability to tender domestically. Many small firms are now facing severe limitations as to how, and when, and with whom they can do business. Those with an annual turnover of between R10 million to R50million will be automatically downgraded if they are unable to comply with the Codes, particularly on ownership. These Codes will have a far reaching impact on the economy; they are not structured to take into account the country's desperate skills deficit. Nor do they recognise the importance of competing in a stagnating economy, the impact of rising input costs and high import competition, and the country's rising unemployment.

### Getting it right

In respect of South Africa's regulatory and policy environment, the evidence speaks of severe governmental deficiencies and inconsistencies. On the one hand, the NDP's vision beckons yet on the other, laws and regulations are passed that will have negative effects on the country's growth and socio-economic goals.

If we are to get back on track, we need to adhere to the principles of better regulation – regulations should be targeted, consistent, proportionate, evidence-based and transparent - and regulatory governance where government only regulates when necessary. This means in the first instance putting each policy and legislative proposal through a rigorous and comprehensive Regulatory Impact Assessment (RIA) process. The provisions of legislation must be carefully considered in light not only of their intentions, but their likely actual outcomes, both intended and unintended.



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SBP has been at the fore-front in pioneering an RIA methodology for the country's policy and law making processes, designing a tailored RIA system in 2005, which was approved by Cabinet in 2007. Since then, SBP has conducted RIAs for national and provincial governments and business.

What we have learnt over the years is that a RIA-orientated regulatory 'culture' needs to be developed in terms of which government, business and civil society expect – and insist upon – open and evidence-based consultation from the early stages of regulatory decision-making, well before specific regulatory proposals are chosen, and from there onwards at points along the line. South Africa is at present a long way from this.

RIA needs to be championed across government in order to bed it in as a normal feature of regulatory policy making. In national departments, the approved RIA template must be used in an honest, comprehensive and context-sensitive way. RIA should not be reduced to a narrowly focused, unimaginative 'box-ticking' exercise, which has been the case in many departments thus far. RIA can play a major role right across the legislative process from the initial stages of policy development to the drafting of Bills; in Nedlac; and in the passage of legislation through Parliament. It serves as a major resource for Parliament oversight's function and on legislator's ability to scrutinise Bills on the basis of fuller, more evidence-based information.

Most importantly, RIA should be transparent. RIAs conducted by government should be open to public scrutiny to determine their quality, the extent to which government has addressed policy objectives and applied its thinking to the consequences, intended and unintended, of regulatory proposals once enacted.

The improved application for better, more transparent RIA is a sine qua non if the country is to attempt to achieve the socio-economic goals of the NDP. For the continued survival - and expansion - of small businesses in South Africa, it is an absolute, unequivocal necessity.



SBP is a not for profit company specialising in improving the environment for doing business. We have worked in Africa and internationally since 1998 providing innovative solutions for policy formulation, better regulation and development in emerging markets. We have a special interest in small business as vehicles for growth and job creation.

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**SBP acknowledges the financial contribution of the Friedrich Naumann Foundation for Liberty.**

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