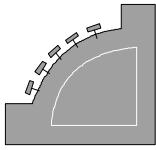


Developing the Small Business Sector in South Africa

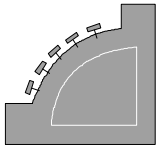
**A Review of Regulatory
and Other Obstacles by the
South African Chamber of Business**

February 1999



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Introduction

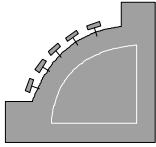
The growth and development of the small, medium and micro-enterprise sector is acknowledged by most interest groups and policy-makers as being of critical importance to South Africa's ability to address the serious problems of unemployment, income inequality, economic concentration, lack of international competitiveness, and low economic growth which currently confront it. In recognition of this, there have been numerous initiatives by a number of different organisations, agencies and government departments over the past five years and more that have sought to "unlock" the potential of the South African small business sector, and to assist with the development process.

In view of the rapid slowdown in the economy during 1998 - which was largely the result of external influences - it is difficult to assess the overall impact of these initiatives. However, it does appear from anecdotal and other evidence that many of the projects have so far failed to achieve their objectives. The reasons for failure are varied, but seem to include:-

- a lack of recognition of the scale and intensity of support required by small and emerging businesses - which results in resources being devoted to projects that are insufficient to ensure success;
- an excessively centralised and bureaucratic approach towards the management of projects and the development process - which has often succeeded in making the initiatives less accessible to smaller businesses, and which may have resulted in resources being channeled away from relatively successful development institutions, and from targeted, local and regional projects;
- the adoption of projects which are not sufficiently targeted, and which seek to achieve too wide an array of objectives - some of which may be in conflict with one another; and
- a lack of recognition of the limitations of direct interventions in the face of a macro-economic and regulatory environment which may be hostile or indifferent towards the growth and development of the small business sector.

In the White Paper on the National Strategy for the Development and Promotion of Small Business, it was acknowledged that inappropriate legislative and regulatory conditions were acting as a constraint on the growth and development of small businesses. In response to this, the Ntsika Enterprise Promotion Agency has commenced a process of reviewing the regulatory environment for small business with the objectives of changing the overall culture of regulation, and of establishing greater co-ordination and consistency in regulations. This document constitutes the input of the South African Chamber of Business [SACOB] towards this process.

Through its affiliated local and regional chambers and national associations, SACOB represents approximately 40 000 businesses from all sectors and from across South Africa. At least eighty percent of these businesses would qualify as small or medium enterprises in terms of the definitions published in the National Small Business Act of 1996. SACOB's constituent chambers and national associations not only represent the interests of such businesses, but are also directly involved in the provision of advisory and other services to them. As a result, the Chamber Movement is well placed to assist in the identification of those regulations and pieces of legislation which are viewed as constraints to the growth and development of the small business sector by the owners and managers of small businesses themselves.



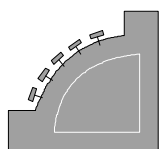
A Suggested Process

As responsible business organisations, SACOB and its affiliates are concerned not only with the narrower interests of individual members, but also with what is in the interest of the country as a whole. The Chamber Movement is therefore forced to acknowledge the need for many of the regulations which currently regulate the activities of the business sector. This precludes SACOB from advocating a purely *laissez faire* approach on the part of legislators and regulators towards the business sector in general, and to the small business sector in particular. Nevertheless, it is SACOB's view that the regulatory environment should principally be of a facilitatory nature - that seeks to enhance the market system so that it can produce better development results. With this in mind, SACOB believes that the review of the regulatory environment should firstly identify which regulations constitute the most significant constraint to small business growth and development, and then embark on a process in respect of such regulations which results in one of the following outcomes:-

- i) A recognition that the rationale for the regulation/legislation is of such a nature that it is not possible to change the status quo. This could apply in cases where health, safety and environmental protections are given effect through such regulations. In such instances the appropriate course of action is to ensure general compliance through adequate policing and enforcement. The negative effects of such regulations could be ameliorated by some form of subsidy or incentive.
- ii) A recognition that there is scope for relief, but that administrative and/or other constraints make it impossible to grant automatic exemption to all small businesses. Application for exemption from some, or all, of the provisions/regulations is required.
- iii) An acknowledgment that there is need for partial relief from the impact of the legislation by exempting all qualifying small businesses from having to comply with certain of its provisions/regulations.
- iv) A recognition of the need for the complete exemption of all small businesses [as defined] from having to comply with the legislation. In such cases the necessity for the legislation must be questioned and its repeal may be recommended.
- v) An acknowledgment that, irrespective of any decisions relating to the legislative and regulatory framework, specific, direct assistance in the form of incentives and/or subsidies is required in relation to the constraints currently faced by small businesses.

One of the problems encountered when trying to assist the small business sector is that - depending on how narrowly it is defined - the number of enterprises involved may be anything from 400 000 to over one million. SACOB is well aware of the resource constraints within government at all levels and is therefore reluctant to propose measures that will demand significantly greater resources from the fiscus. The Chamber also believes that any process of exempting small businesses from certain regulations, or of providing incentives or subsidies to them, should not provide too great a disincentive for such businesses to develop and grow, or encourage "unnatural" splitting of enterprises in order that they remain eligible for such assistance.

Nonetheless, SACOB believes that, in view of the generally accepted importance of the rapid growth and development of the small business sector in South Africa, there are areas where such businesses can be, and should be, assisted.



Labour Regulations

Perhaps the main reason advanced for the need to develop the small business sector in South Africa is the perceived superior ability of such businesses to create employment. This tends to be confirmed by a comparison of the Department of Trade and Industry's Tax Holiday and Small and Medium Manufacturing Development programmes - which indicates that the average capital cost per job created under the latter programme is roughly one fifth of that required for the larger scale projects utilising the Tax Holiday scheme. In view of the fact that the unemployment rate in South Africa is officially estimated at around 28 percent of the economically active population, this makes small business development an obvious priority for policy-makers. However, it is clear from official employment figures that the small business sector has thus far not been able to absorb all of the jobs shed by large scale enterprises - much less assist in reducing the overall level of unemployment in this country.

One of the reasons for this is that many small business owners and managers perceive the prevailing and soon-to-be-introduced regulations governing employment practice and labour relations as excessively onerous - to the point that such businesses are actively seeking ways to reduce the number of people they employ. Many successful small business owners and managers are also reluctant to allow their labour forces to grow beyond those levels which currently allow them exemption from certain provisions of the various pieces of labour legislation - with the result that a somewhat artificial constraint on the growth and development of such businesses has emerged. On the basis of interaction with members of the Chamber Movement, the three most commonly cited problems with the prevailing labour legislation are that:-

- i) it imposes significant additional direct costs on businesses;
- ii) there is a high "hassel factor" associated with compliance; and
- iii) the legislation "robs" owners and managers of some of the control and flexibility which they perceive as being both desirable and necessary to the effective running of their businesses.

SACOB accepts that there must be a balance between the rights of employers and the one hand and that of trade unions and workers on the other. The concerns of employees in finding solutions to the problems relating to labour legislation must therefore obviously be considered, but the balancing of rights must be informed by the economic realities prevailing in South Africa. An extremely high rate of unemployment, low economic growth, and the implementation of a self-imposed structural adjustment programme must have the practical consequence of reducing the level of protection expected by, and afforded to, trade unions and workers. This reality must be reflected in labour legislation.



The Direct Cost Impact

SACOB believes that one of the fundamental problems with the prevailing labour legislation is that it is based on the premise that low wage competition should - as far as possible - be eliminated from the South African labour market, and that businesses should, instead, compete on the basis of other costs and "intangibles" such as quality, reliability and

service. Whilst this approach might have had fewer negative consequences in a country isolated from the rest of the world, the fact is that producers and suppliers in many other developing and developed economies are not constrained to the same degree in their ability to compete.

The integration of national economies has resulted in a worldwide trend towards “down-sizing” and “right-sizing” that has been accompanied by outsourcing and sub-contracting to smaller businesses - usually with the objective of reducing costs and increasing flexibility. However, since South Africa began to liberalise its trade regime, exports have become more capital intensive, and import-intensities have increased across most product ranges, but particularly in the highly labour-intensive sectors. As a result, South Africa is effectively exporting jobs to low wage countries, whilst at the same time pursuing an industrial policy and trade strategy that favours production of skills-intensive, intermediate and finished goods.

The obvious objective is to bring about a rapid increase of skills development within the labour force through training and education. However, to the extent that productivity improvements are not achieved via this process, or there is a mismatch between the demand for, and the supply of, skilled labour, there is a danger that the competitiveness of such higher value-added sectors will be undermined. At the same time, the elimination of low wage competition within South Africa, coupled with further trade liberalisation, will threaten the longer-term viability of jobs within the labour-intensive sectors.

As regards the development of the small business sector, one has to ask in which other areas they will be able to compete with larger businesses and with foreign competition if they are precluded from competing on the basis of wage costs. The latest Input-Output tables for South Africa indicate that the contribution of various inputs to total production costs is as follows:

Intermediate Inputs	-	65%
Labour Remuneration	-	19%
Gross Operating Surplus	-	13%
Net Indirect Taxes	-	3%

Generally, it is not possible for small businesses to obtain many [if any] of their intermediate inputs at lower prices than their larger competitors, although they may be able to offset some of the cost disadvantage through better control over fixed costs. At the same time, the greater dependence of smaller businesses on loan capital within an environment of high real interest rates means that a competitive edge in terms of the cost of capital can only be accommodated by a reduction in their profits - with resulting disincentive effects. There is also little real possibility of smaller enterprises reducing their net indirect taxes.

This means that, if they are precluded from competing on the basis of wage costs, the primary area in which a competitive edge may be sought by small businesses will be in the fields of “intangibles” such as quality, reliability and service. However, these intangibles are likely to be more important in high value-added, more capital-intensive sectors than in lower value-added labour-intensive ones - with concomitant negative implications for the labour-absorption capacity of the small business sector.

SACOB therefore believes that, given our level of development, there is a fundamental inconsistency between the objective of eliminating low-wage competition - which is the intended or unintended result of many of the provisions of prevailing labour laws - and the goal of achieving a dynamic, rapidly-growing, labour-absorbing small business sector. The Chamber recognises that this particular “mix” could change over time - but only through a process that can, at best, be facilitated by government regulations. Attempts to “speed-up” the process by excessive regulation are almost certain to prove counterproductive.



The Costs of Compliance

Small businesses are generally characterised by a very small number of people in management positions. In many cases the owner/manager is required to take responsibility for most of the management functions, and to ensure compliance with legislative provisions and regulations. To the extent that such provisions and regulations impose an “onerous” administrative burden on managers, they clearly diminish the ability of such persons to focus on factors which are more important to the longer-term growth and development of the business concerned.

In SACOB’s experience, many small business owners and managers perceive the compliance “costs” associated with the prevailing labour legislation as being too high, and as acting as a disincentive to employment. So much so, that many appear intent on actively seeking ways to reduce their exposure to labour through the adoption of labour-saving technologies. As a result, the process of capital-deepening is continuing. Worse still, where labour cannot be competitively replaced by capital, entrepreneurs are simply forced to abandon that particular economic activity - leaving the sector open to greater import penetration.



Control and Flexibility

Many of the more successful owners and managers of small businesses were previously employed by, and acquired skills in, larger corporations. One of the principal motives behind their decision to start, or to manage, their own businesses is a perception that they will have more direct control over the enterprise, and greater flexibility to adjust quickly to the opportunities and threats of the market. To the extent that legislation is perceived to reduce the owner’s control over his/her business, and the flexibility to adapt to new circumstances, it can act as a disincentive to both the starting of new businesses, and to the growth and expansion of existing ones.

In SACOB’s experience, many small business owners perceive that prevailing labour laws undermine their control over their enterprise to an unacceptable extent. They are also concerned at the fact that, by seeking to regulate labour relations within small firms, labour laws are contributing towards an alienation of workers and management, and are - in the process - eliminating an important potential area of competitiveness.



Proposals Relating to the Labour Relations Act

There appears to be three broad problem areas for small business in the Labour Relations Act [LRA], namely:-

- i) bargaining councils;
- ii) dismissal of staff; and
- iii) Commission for Conciliation, Mediation and Arbitration [CCMA] proceedings.

Bargaining Councils

Small businesses often regard bargaining councils as “unrepresentative” institutions imposing “big business” conditions of service upon them. The practice of extending agreements to non-parties is also often regarded as being contrary to the principle of voluntarism. The effective representation of small businesses on such councils, although theoretically provided for in the LRA, is in fact a practical problem as small business owners and managers often simply do not have the time or the expertise to participate effectively in such bodies. The effective use of the new independent exemption bodies in all instances is also questionable.

SACOB would therefore like to propose the following possible solutions to the problems associated with bargaining councils by small businesses for consideration:-

- i) The “representivity” test to extend agreements to non-parties is widened beyond only the number of employees who are members of trade unions and who are employed by party employers to also take account of the number of employers within the designated sector covered by the bargaining council.
- ii) Factors other than the stability of the industry are also taken into account when consideration is given to the extension of agreements to non-parties. Such factors could include the impact on job-creation and unemployment, and small business development.
- iii) The criteria for granting exemptions is specifically and clearly spelt out in either the legislation or the agreement. The procedure for exemptions should also be transparent, accessible and efficient. At present the only criteria for exemption is that it must be “fair and promote the primary object of the Act” - but this may not necessarily be in the interests of the small business sector.
- iv) Alternatively, a separate, lower schedule of service conditions could be agreed for small business, whilst at the same time retaining an exemptions facility to address other, unforeseen problems. Specific exemption criteria and a proper procedure would also be required.
- v) Whilst “blanket exemptions” are not acceptable to some parties, consideration could be given to the granting of such exemptions to start-up businesses for a certain defined period - resulting in a rising floor of compliance.
- vi) Party employers should also be allowed to apply for exemption from bargaining council agreements.
- vii) As far as the weak representation of small business in employer organisations is concerned - many of the reasons for which are the same as for their lack of representation on bargaining councils - SACOB is opposed to the introduction of compulsory membership.

Dismissal

A second problem area for small business lies in the field of dismissal. Small employers often do not have the time or expertise to deal with unduly complicated legal and procedural employment practices. It is recommended that a simplified dismissal procedure with clear guidelines is adopted for use in small business. CCMA rules should also make special allowance for procedural deficiencies in arbitration awards.

CCMA Proceedings

The third problem area in respect of the LRA that has been brought to SACOB's attention by small businesses relates to CCMA proceedings. Small employers are intimidated by these proceedings and often do not have the expertise to effectively represent themselves. SACOB therefore proposes that:-

- i) A stricter screening process is followed by the CCMA to prevent abuse of the system. A deposit should be paid by applicants to limit the scope for frivolous or vexatious cases being presented.
- ii) The question of representation at conciliation proceedings is revisited.

Although all business are affected by the new strike law dispensation, small businesses are particularly hard hit by strikes that turn violent, or get out of hand. Small business is also very vulnerable to sympathy strikes where they have absolutely no ability to affect the outcome of the primary dispute. Experiences over the past few months have now made a review of South Africa's strike law essential.



Proposals Relating to the Basic Conditions of Employment Act

The present investigation which is being conducted into the impact of the Basic Conditions of Employment Act [BCEA] with a view to a Ministerial determination aimed at assisting small businesses should, in SACOB's view, have been completed before the Act was promulgated. Whilst the task team conducting the investigation has proposed that the ministerial determination should apply only to businesses with ten or fewer employees, and that only four conditions of employment should be varied for such businesses, SACOB submits that the priority to raise the rate of economic growth and reduce the rate of unemployment demands that both the definition of qualifying businesses and the scope of the determination should be extended. With this in mind, the Chamber proposes that :-

- i) bargaining council agreements should not supersede [but may extend, or grant additional measures to assist] the Ministerial Determination for small businesses as this would undermine any efforts to accommodate the sector;
- ii) the special accommodation should apply to businesses employing up to fifty employees - ie to businesses defined in the National Small Business Act as "small";
- iii) the determination should extend the overtime hours from a maximum of 10 hours to 15 hours per week, and the daily limit on overtime hours should be adjusted accordingly - or scrapped - in order to provide small businesses with greater flexibility;
- iv) the overtime rate for small business should be reduced from time-and-a-half to time-and-a-third, in order to enhance the competitiveness of the sector;
- v) small businesses be allowed to offset family responsibility leave against annual leave;
- vi) the averaging of working hours is permitted by individual [as opposed to collective] agreement, and small businesses are allowed to determine for

- themselves how the hours are to be averaged over a four month period - thereby enhancing their flexibility and competitiveness;
- vii) Section 28(2) - which exempts businesses employing fewer than 5 people from certain record-keeping and reporting requirements - should be brought into line with the variations under consideration;
 - viii) the double time premium for Sunday work is scrapped and a uniform time-and-a-half premium is adopted for all work on Sundays;
 - ix) provision is made for an exemption of small business from the requirement to pay severance pay if good cause for doing so can be demonstrated;
 - x) small businesses are allowed to shorten the notice period to two weeks by individual agreement; and that the ability of small businesses to dismiss employees on 24 hours notice during an employee's probationary period [which may be limited to three or six months in order to provide protection to employees] is reintroduced; and
 - xi) the night shift allowance only apply to work done after 23h00, and that the code of good practice on the regulation of working time provides small businesses with a more lenient dispensation in respect of the availability of transport and the provision of medical examinations.

Whilst points iii) to vi) above have been proposed by the Task Team, SACOB believes that the extension of the Ministerial Determination to cover the other points listed above would go a long way towards reducing the direct costs, and compliance costs, which the BCEA currently imposes upon small businesses.



Proposals Relating to the Employment Equity Act

In SACOB's view, the provisions of the Employment Equity Bill will impose onerous direct and compliance costs on businesses that simply do not have the capacity to fulfil them. The Chamber therefore urges that the definition of "designated employer" is amended to only include businesses with 250 or more employees. SACOB believes that only enterprises of such a size workforce will realistically be able to meet the legislative requirements of the Employment Equity Act, and to make a genuine contribution to affirmative action.

SACOB also believes that the turnover criterion which was added during the negotiations on the legislation is not appropriate to the definition of a "designated employer". Turnover is not directly related to either administrative capacity or profitability, and the threshold will act as a disincentive to small entrepreneurs who are the principal job creators.

The section on the wage gap should be removed from the legislation as wage differentials are due to skills shortages which cannot be addressed through statutory intervention.

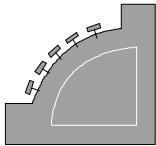


Proposals Relating to the Skills Development Bill

The proposed training levy will - when taken together with other cost implications of prevailing labour legislation - impose a heavy cost burden on small businesses, and could serve as a further disincentive to employment creation. SACOB therefore believes that:-



- i) consideration should be given to sectoral exemptions from the levy - especially for start-up small businesses;
- ii) procedures to access training grants should be simple and sympathetic to the needs of small business;
- iii) attempts should be made [within the limitations which exist] to ensure that small businesses are effectively represented on SETA's to ensure that their needs are met; and
- iv) a special "learnership wage rate" should be set to encourage small businesses to take on learners.



Finance

Many entrepreneurs and owners of emerging and “start-up” small businesses perceive the lack of access to finance as the major obstacle to the growth and development of their business. Often this belief is misplaced inasmuch as it obscures the shortcomings of the entrepreneur, the business concept, and the management structures of the enterprise concerned. However, historical imbalances created by the system of apartheid - such as the lack of appropriate collateral to secure loan finance from the banking system - have added another dimension to this problem. The high costs of loan finance are also cited as a problem by many established small businesses - who are often forced to pay risk premiums to financial intermediaries. The principal problems associated with finance are therefore ones of *access* and *cost*.

From SACOB’s perspective the high costs of loan finance are symptomatic of an underlying shortage of savings within the economy. Relatively high interest rates are required to ration the available loanable funds in a manner that encourages them to be invested in those ventures which promise the greatest return at the lowest risk. To the extent that legislative interventions pursue objectives other than financial stability by seeking to channel financial resources away from such ventures, there is an increased danger that interest rates will not reflect the relative scarcity of loanable funds, and that South Africa will become more vulnerable to the kind of financial instability that has characterised many other emerging markets in recent times. SACOB therefore believes that measures that aim to reduce the costs of loan finance to smaller businesses by non-market means should not be a favoured policy instrument, and should - where used - be narrowly targeted.

SACOB is of the view that the bigger problem which small businesses have in relation to finance is one of access - most notably to smaller loans where the maximum interest that may be earned by the financial institution is insufficient to cover its administrative costs and provision for bad debts. So, whilst South Africa has a relatively well developed financial services sector, commercial banks have generally shunned the small loans sector of the market because they view it as unprofitable. It is only relatively recently that some new financial intermediaries have emerged to address this segment of the market, but they are often constrained in the number of loans that they are able to grant because they are unable to accept deposits without first registering as a bank under the Banks Act. New technology is also making it possible for traditional commercial banks to reduce their administrative costs and thereby increase the number of smaller loans which they extend to businesses.



The Banks Act

SACOB is reluctant to propose that non-bank financial intermediaries wishing to accept public deposits are exempted from the provisions of the Banks Act, because of the increased potential for collapse, and the fact that depositors would have no guarantee of the repayment of their capital. It may be argued that, as long as such organisations clearly inform depositors up front that their capital is not guaranteed, they should be allowed to accept deposits without registering as a bank. However, there is a danger that vulnerable depositors would be attracted by the higher interest rates which such institutions would probably offer, and would overlook the risks. Recent collapses of pyramid-type schemes suggest that there is

still an expectation that Government will effectively guarantee the capital of investors in the event of failure.



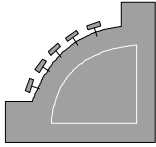
The Usury Act

The Usury Act - which places an upper limit on the amount of interest that may be charged on loans less than R6000, and a slightly lower limit on loans greater than R6000 but less than R500 000 - has the effect of precluding a lending institution from recovering its costs on loans below a certain level. Faced with an inability to recoup its costs by charging higher interest rates, most lending institutions simply refuse to make loans to what they judge to be higher risk applicants, and many discourage loan applications from smaller borrowers. So whilst the objective of the Act is to protect borrowers from “exploitation”, the net effect is that access to smaller loans is severely constrained.

In SACOB’s view this constitutes a significant constraint on the growth and development of the small business sector - particularly for those sectors of the community who are unable to resort to borrowing from family and friends, or who do not have the necessary collateral to secure commercial loans. SACOB therefore proposes that either:-

- i) the Usury Act’s limits on interest rates are repealed in their entirety - thereby making it possible for lending institutions to extend small loans on a profitable basis and providing increased motivation for commercial banks and other financial intermediaries to enter the small loan market; or
- ii) the existing exemption of loans to natural persons that are below R6000 and that have a term of 36 months or less is extended to include loans up to R50 000, and that such limits are adjusted regularly for inflation.

In the Chamber’s view either of the above steps will have the effect of encouraging more entrants into the small loans market - thereby increasing both the access of small businesses to loan finance, and improving the service of lenders.



Taxation

There are two acknowledged reasons for taxation. The first is to raise revenue to finance the operations of government at various levels. The second is to bring about a different allocation of resources within an economy. In the first case, the issue of the efficiency of the tax system will dominate, whilst in the second, other aspects - such as the attainment of socially-desirable objectives, including the growth and development of the small business sector - will be the focus of tax policies.

It is important to recognise that the tax system cannot, and should not, be seen in isolation from society and the economy within which it operates. Given present backlogs in social spending, and the transformation process that is currently taking place, the South African tax system is likely to be expenditure-driven for many years to come. Under these circumstances it will be very difficult to reduce the State's share in the economy, and thereby limit the overall tax burden on society. It should also be noted that, if attempts to promote the growth and development of small business are to succeed, then the complexity of the tax system - at least as it relates to such businesses - will have to be addressed..

There are two philosophical approaches towards addressing the problem of high compliance costs for small - and particularly emerging - businesses. The first is to exempt such businesses from the provisions of some, or all, tax legislation. The second is to assist small businesses to comply through a subsidy which covers some, or all, of the administrative costs of compliance, or through the simplification of tax legislation in ways which reduce administrative costs, and encourage compliance.

SACOB does not favour any proposal which seeks to exempt businesses from paying taxes - except within the context of a narrowly-defined tax holiday scheme - because this undermines the integrity of the tax system. At the same time, SACOB is doubtful that there is significant scope for simplification of the tax system in the context of global trends.

Over recent years, SACOB has put forward a number of proposals aimed at reforming the tax system. Although relatively few of these proposals were "targeted" specifically at small businesses, the Chamber believes that their acceptance would be to the benefit of all businesses in South Africa. SACOB has argued that:-

- The Secondary Tax on Companies [STC] makes the tax system more complex, distorts decision-making, and encourages retentions. It should therefore be scrapped - even if this means that the nominal corporate tax rate has to rise.
- The corporate tax rate and the maximum marginal personal tax rate are too high by international standards and should be reduced. The rates of both taxes should be aligned to eliminate any bias against unincorporated businesses.
- Properly designed tax incentives can be more cost-efficient than a blunt instrument such as a general tax rate reduction - provided that they are narrowly targeted and are accompanied by the necessary administrative capacity. The most appropriate areas for incentives are for the upgrading of skills and training; research and development activities; investment in new technologies; small and medium-sized enterprises; and exports. The most appropriate and efficient types of incentives are full expensing, investment tax credits, and accelerated depreciation.



A Cash Basis of Taxation

From the Chamber's experience, the principal problems experienced by small businesses in relation to the tax system are the effects of the various taxes on the cash flow of the business, and the administrative costs of compliance. For this reason, SACOB put forward a proposal to the Katz Commission which would allow qualifying small businesses to elect to account for tax on a cash basis. Effectively, this would mean that small businesses that made use of the scheme would only have had to pay tax on taxable income which they had actually received. As a result, the cash flow problems which many small business experience would be eased - without diminishing their ultimate tax liability. This form of tax accounting would also simplify accounting and administrative procedures.

The Katz Commission effectively accepted the SACOB proposal, but the tax authorities have thus far failed to adopt the scheme. Furthermore, the option of small, incorporated businesses accounting for value added tax on a cash basis was repealed in the 1998/99 Budget. SACOB believes that both of these forms of cash taxation should be available to qualifying small businesses - both incorporated and unincorporated.



Dedicated Taxes and Levies

One consequence of the fiscal discipline imposed by the Finance Department has been that various government departments that are constrained in their ability to deliver have proposed numerous special levies, user charges and dedicated taxes to supplement their fiscal allocations. Many of these proposed taxes would be levied on business activities, or be collected by businesses. If they were to be introduced, such taxes would therefore not only raise the overall tax burden in South Africa, they would also add significantly to the administrative burden of small businesses and make the tax system even more complex.

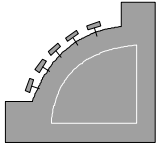
SACOB is therefore opposed, in principle, to the introduction of dedicated taxes and levies and believes that this should only be undertaken if Government creates the necessary "tax space" to ensure that the overall tax burden does not rise. At the same time, the Chamber is not opposed to the introduction of user charges in respect of the products and services supplied by the public sector - provided that this is done in accordance with the market mechanism and that the price of such products and services is in accordance with the quantity consumed.



Regional Service Council Levies

Regional Service Council [RSC] levies were ostensibly introduced to provide funds for the construction of basic infrastructure between adjoining municipalities and within black communities. Although the Regional Service Councils Act was repealed, the sections pertaining to the levies were reinstated by the Provinces in order to provide fiscal continuity. These levies are no longer the only source of revenue for local authorities, which means that the uses to which they are put have become less transparent. As a result the levies now conform even less to the principles of a "good tax". In addition, the levies are administratively

burdensome - particularly for small business - and are probably unconstitutional. SACOB therefore believes that they should be scrapped.



The Judicial Process

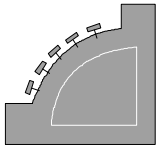
The effective operation of the market economy is dependent on the ability of contracting parties to enforce contracts. It is also necessary for the criminal justice system to bring criminals to justice quickly and efficiently in order to reduce the level of crime and encourage respect for the rule of law. At the same time, the cost of litigation may inhibit the use of the courts to enforce contracts which involve smaller amounts, and long delays in bringing cases to court can significantly increase the costs of the judicial process. As a result, many citizens and small businesses in particular may be discouraged from using the courts - thereby undermining the value of contracts and making it increasingly difficult to do business.

Although SACOB believes that the introduction of small claims court has improved access to the judicial process, small businesses can only make use of the process if they are unincorporated. This creates a disincentive to the registration of companies and close corporations, and may also contribute towards a breakdown in overall morality - because it is often not cost-effective to pursue smaller claims through the courts. Legal fees are high, judgments against debtors are often of little value, and procedures for the attachment, and subsequent execution, of debtors assets are often time-consuming and costly.

With this in mind, SACOB recommends the following:-

- i) Government should allocate the necessary funds to ensure the efficient administration of justice, and expedite the judicial process in both criminal and civil courts.
- ii) Consideration should be given to the introduction of a new class of legal practitioner with a shorter period of training, and the right of appearance in the lower courts.
- iii) Practicing attorneys and advocates should have the right to appear in all courts.
- iv) The Rules Board should develop proposals aimed at reducing the costs of appearing in the High Court, and Government should introduce a comprehensive system of legal aid which is adequately funded.
- v) Incorporated businesses should be allowed to make use of the small claims court, and the claim limits of that court should be raised to R25 000, and be regularly updated in the light of inflation.

SACOB believes that if some, or all, of the above steps were adopted, the access of small businesses to the judicial process would be significantly enhanced, and that the overall operation of the judicial system would be improved.



Other Regulations

In addition to those issues already addressed above, there are a number of other areas of concern to small business, that have been raised with SACOB and its affiliates in recent times. Some of the more significant constraints are raised in this section.



Registration of Trademarks, Patents and Designs

In an era in which technology and branding are constituting an increasingly important aspect of the competitiveness of individual firms, and in which investment in such “intellectual capital” is rising rapidly, it is important that enterprises be afforded adequate protection of their copyrights, trademarks, patents and designs. A failure to ensure the necessary protection of such investments will discourage innovation and could make firms vulnerable to the theft of ideas and to attacks aimed at damaging their reputation in the market. Smaller businesses are often particularly vulnerable in this regard.

For this reason, SACOB regards complaints of long delays in the registration of such intellectual property with concern, and believes that efforts should be made to make the registration process more efficient.



Tender Procedures

Whilst SACOB is supportive of attempts to use the procurement process to develop small and medium enterprises and associated social objectives, such an approach will introduce greater subjectivity into the adjudication process. For this reason, the Chamber believes that the existing preferences should be subject to a sunset clause.

SACOB supports attempts to simplify and standardise tender procedures and is of the view that the focus of the procurement process should be on encouraging and promoting linkages between smaller enterprises and larger ones. Generally, parastatals should be discouraged from tendering for government contracts, but where tenders are awarded to such organisations, there should be transparency in respect of resource allocation to ensure that cross subsidisation does not give them a competitive advantage.

At the same time, the Chamber has received complaints from some small businesses about a lack of transparency in the adjudication of tenders. Businesses that believed they had submitted competitive tenders [after taking account of the points preferences] were unable to obtain adequate explanations about why the tender was awarded to competing firms. SACOB believes that neutral representatives from the private sector should be included in the tender evaluation process. An independent tribunal should also be established to deal with procurement irregularities and the inevitable grievances which they give rise to.



The Postal Services Act

The Postal Services Act is intended to promote a universal and affordable service. In pursuit of that objective the Post Office is granted exclusive rights to handle and deliver articles weighing less than one kilogram and/or falling within certain dimension specifications. The legislation provides for unreserved services including courier services to be subject of registration by the Postal regulator which may grant a licence provided certain conditions are met [collection and delivery schedules, track and trace]. Besides being an impediment to competition the legislation constitutes an entry barrier to an industry capable of being undertaken by small business. Whilst supporting the objectives of a universal and affordable service, SACOB believes that these could be achieved by limiting the reserved service to articles up to 0,5 kilogram and by allowing courier services to operate without hindrance from the Act.



The Liquor Bill

In SACOB's view, if there is assurance that the new Competition Bill is an appropriate legislative mechanism for dealing with all aspects of competition in South Africa, it should surely be applicable to a specific industry such as liquor. This raises a question as to the necessity of the Liquor Bill. From a competition standpoint, the concern must be that if the provisions of the Competition Bill are seen to be unsuitable for the liquor industry, then it may be possible for the liquor industry's provisions - which focus on the regulation of the industry - to be seen as suitable by those administering Competition Policy.

Attempts to provide a legislative basis for the transfer of economic power within the liquor industry should, in SACOB's view, be approached with caution. Economic power ultimately rests on entrepreneurial principles, and there is a danger that such legislation will result in distortions and inefficiencies. The Chamber therefore believes that a "sunset clause" should apply to these provisions. SACOB has also argued that:-

- i) the provisions governing the conditions applicable to the storing and display of liquor do not allow sufficient flexibility; and
- ii) the prohibitions on the provision of functional equipment by a manufacturer or a wholesaler to a retailer are not conducive to assisting aspirant entrants to enter the industry.



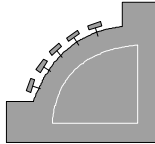
The VAT Act

The South African Revenue Service [SARS] replaced the old General Export Incentive Scheme with a new scheme, and also issued a new Practice Note relating to the validating documentation required by a South African vendor when zero-rating a transaction for export purposes. As a result a massive fraud occurring in this area a new system was introduced whereby exports that are not delivered by the SA vendor personally, or by a SA cartage contractor on the instruction of the SA vendor, may not be zero-rated for purposes of VAT. In these cases the buyer must pay VAT and apply for a VAT refund at the border. Where the SA

vendor is responsible for the transportation of the goods outside the country, additional documents are now required to be presented to SARS as proof that the export actually took place.

Although SACOB was initially supportive of the measures that SARS introduced to combat the problem of fraud [which is estimated to cost the fiscus approximately R100 million per month] the Chamber expressed some reservations concerning the administrative burden that the new measures would impose on businesses. In particular, SACOB was opposed to the requirement that proof of payment for the goods be presented within two months. Many members have opened credit terms or 120 day credit terms with their buyers – making it impossible to fulfil the requirement.

SARS has agreed that companies that cannot obtain this information within two months may make application for an additional two month period. SACOB would like to see the period extended to four months in all cases as the current procedure requires vendors to create extra systems in order to apply for extensions timeously.



Conclusion

The above issues constitute those concerns which have most frequently been raised by smaller business members of the Chamber Movement, and which are clearly viewed by the owners and managers of such businesses as being the most significant legislative constraints on the growth and development of their enterprises. SACOB accepts that there are many areas outside of legislative provisions and regulations in which emerging businesses experience difficulty. The responsibility for providing assistance in these areas does not rest entirely with government, but is shared by a wide range of organisations and institutions - including local and regional chambers of business, and national associations.

However, there are numerous other areas of policy and legislation which impact on the business sector as a whole, and which would - if addressed - improve the overall environment for both large and small businesses. For this reason, this submission should be read in conjunction with the 1998 edition of "The Policy Positions of the South African Chamber of Business" - which addresses a much wider range of issues.

SACOB believes that the new Competition Bill has implications for an array of other pieces of legislation which impact directly on the business sector - many of which will have to be amended. In the Chamber's view, this process affords the relevant authorities with an opportunity to also review such legislation with the objective of ensuring that they are more consistent with the objective of developing the small and medium enterprise sector.