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TO: The Standing Committee on Appropriations
Chairperson Mmusi Aloysias Maimane, MP

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SUBJECT: **Submission on 2025 Division of Revenue Bill**

Introduction – Key Proposals

IRR Legal's proposals in this submission, just as in the last round, aim at amending the 2025 Division of Revenue Bill (the Bill) to achieve two direct objects:

- Make BEE premiums in public procurement transparent.
- Reduce BEE premiums in public procurement to R0, ie. maximize value for money.

A BEE "preference premium", to repeat a phrase used by Acting Chief Procurement Officer Willie Mathebula, is currently "capped" at 25% for contracts under R50 million and 11.1% for contracts over R50 million in terms of the Public Procurement Policy Framework Act (PPPFA).

IRR Legal proposes that BEE premiums be made transparent and reduced to R0 in order to bring fiscal outlays in all spheres in government in line with constitutional requirements, to maximize value for money, to heed the spirit of the advice of the Commission of Inquiry into Allegations of State Capture, Corruption, and Fraud in the Public Sector including Organs of State Report, better known as the Zondo Report, which in turn will unlock South Africa's capacity to grow economically in real terms, which has not happened overall since 2007, thereby reducing unemployment.

IRR Legal's ultimate practical goal is to facilitate the reduction of unemployment.

In order to achieve this purpose the Bill must be amended so that the conditions on which allocations are made to the national, provincial and local spheres of government, as well as all other allocations made in the Bill, explicitly guarantee the explication of BEE premiums in public procurement, and, separately, the reduction of such premiums to R0.

IRR Legal urges the Appropriations Committee to be mindful of the following fact: transparency is not the same as maximizing value for money.

IRR Legal is aware that some members of the Committee are committed to supporting fiscal decisions that deviate from value for money by continuing to require state sponsored BEE premiums in public procurement. Those members of the Committee, however, should *a fortiori* want transparency over how much is being spent on BEE premiums.

Likewise, some members of the Committee would prefer a maximum value for money approach. Those members should also want transparency over how much is being spent on BEE premiums, even if this comes to those members as bad news.

In short, all members of the Committee are urged to unify around the common value of transparency. This can be explicitly guaranteed by simple amendments to the Division of Revenue Bill.

Estimate of Cost

The estimated cost breakdown is as follows:

BEE Premium Recorded Spend	R5.7 Billion per annum
BEE Premium Unrecorded Spend	R11.3 Billion per annum
BEE Premium Total Licit Spend	R17 Billion per annum
Total Corruption Cost	R240.6 Billion per annum
Zondo Dividend	R132.3 Billion per annum
BEE Premium Total Cost	R149.9 Billion per annum

Source: IRR Blueprint for Growth, Slash Waste & Cut Taxes, 2024.

The breakdown for each estimate is available at the source, where further breakdowns are referenced. Here, for brevity, each line item is explained.

BEE Premium recorded spend refers to the amount recorded (but not published) every year. Whenever a contract is awarded on the basis of BEE “points”, in terms of “special goals” in Section 2 of the Public Procurement Policy Framework Act (PPPFA), or in terms of “set-asides” and “prequalification” under Chapter 4 of the Public Procurement Act (PPA), a BEE premium is spent.

The BEE Premium recorded spend is equal to exactly the difference in cost between the winning bid (at the point of awarding the contract) and the cost of the contract that would have won if BEE “points” were not part of the tender process.

For an example, consider the City of Cape Town’s “Procurement Transparency Report”, where GEL batteries could have been bought from the manufacturer, which submitted a bid, but the same product was bought at a higher price from another company, because it scored higher in terms of BEE¹.

The recorded spend of BEE premiums is very easy to calculate with only two data points per contract according to this formula for the winning bid:

$$\text{BEE Premium (ZAR)} = \text{Contract value} * (80 - \text{Price Points}) * 1.25$$

That formula assumes a contract on the 80/20 system. If it is on the 90/10 system:

$$\text{BEE Premium (ZAR)} = \text{Contract value} * (90 - \text{Price Points}) * 1.11$$

BEE premium unrecorded spend refers to the licit cost that is not calculable by simply looking at the record of bids and applying the formula above. This might occur because a company realizes that even though it can offer the same goods or services at the best price, it is likely to lose on BEE points, so it does not enter a bid. In that case the true best price option is not reflected in the points allocation. Alternatively, a company might be outright excluded on the basis of race, as was provided for by the Finance Minister’s regulations under the PPPFA issued in 2017 (later struck down at court). The latter form of paying unrecorded BEE premiums is set to be returned by the PPA.

BEE premium total licit spend refers to the sum of recorded and unrecorded BEE licit premiums.

¹ Pg. 19, City of Cape Town Procurement Transparency Report 2022.

Total Corruption Cost refers to the estimated loss of resources due to corruption in the procurement system that is funded by taxpayers and channelled through the Bill².

Zondo Dividend refers to the reduction in waste due to corruption that is expected to be achieved if the Zondo Report advice is heeded to derive maximum value for money³ in public procurement without ambiguity⁴. Notice that this is a fraction of total avoidable corruption costs.

BEE Premium Total Cost refers to the sum of the **Zondo Dividend** and the **BEE premium total licit spend**.

IRR Legal would be eager to provide more details on how the estimates were calculated, and how modest they are compared to publications referenced by the IMF, World Bank, Harvard Growth Lab, etc. Should the Committee request further details IRR Legal will eagerly supply them.

Key Constitutional Provisions

IRR Legal's submission is based on the Constitution of the Republic of South Africa. Key provisions are highlighted for your convenience.

214 Equitable shares and allocations of revenue

The 2025 Division of Revenue Bill is tabled in terms of section 214 of the Constitution.

214(2)(a) states that the Bill "must take into account – the national interest".

The Zondo Report dealt with the "inevitable tension" between BEE premiums in public procurement and "maximum value-for-money" in the section on "Problems in the legislative design" in Volume 1.

It stated that first that legislation ought to prioritise one over the other unambiguously, either value for money, or BEE premiums. The Zondo Report states (with added emphasis):

"There are of course many cases, one hopes the vast majority, in which the award of the tender satisfies both objectives of the Constitution but undoubtedly there are other cases some of which may well be high-value tenders in which one or other of these two objectives must be preferred, and it is in such cases that the legislation fails to give guidance. In the view of the Commission the failure to identify the primary intention of the Constitution is unhelpful and it has negative repercussions when this delicate and complex choice has to be made, by default, by the procuring official."

Secondly, the Zondo Report stated that the national interest lies in prioritizing value for money.

"Ultimately in the view of the Commission the primary national interest is best served when the government derives the maximum value-for-money in the procurement process and procurement officials should be so advised."

Again, the national interest *must* be taken into account in the 2025 Division of Revenue Bill; and the primary national interest is to maximize value for money. That means reducing BEE premiums to R0.

214(1)(c) of the Constitution provides the relevant mechanism to maximize value for money.

214(1)(c) states that the Bill "must provide" for "...any conditions on which those allocations may be made."

² SCMR 2015, SCMR Update 2016, IMF Public Procurement in South Africa 2023.

³ Para 532., *State Capture Commission Report, Volume 1*.

⁴ *Ibid.* para 531.

The Bill must be amended so that the conditions on which all allocations that bare a nexus to procurement in terms of the PPPFA are qualified: a) in order to make any payment of BEE premiums explicit, reportable, and reported back to National Treasury; and b) to reduce BEE premiums to R0.

Furthermore, Section 17 of the Bill ought to be amended to make explicit that appropriations will be withheld if the conditions a) and b) above are not met within a reasonable time.

216 Treasury control

216(1) states:

“National legislation must...prescribe measures to ensure both transparency and expenditure control in each sphere of government, by introducing – ...

(b) uniform expenditure classifications; and

(c) uniform treasury norms and standards.”

In this context the phrase “both transparency and expenditure control” means that transparency must be both prospective and retrospective. That means BEE premiums that will be paid must be budgeted, and BEE premiums that have been paid must be budgeted.

The Bill must provide for the exchange of information that facilitates this double-barrelled notion of transparency, as required by the Constitution.

The expenditure classification for BEE premiums is already defined as the deviation from value for money due to considerations of “specific goals” under 2(d) of the PPPFA, or in terms of Chapter 4 of the Public Procurement Act (PPA).

However, the Bill is an appropriate instrument in which to reiterate the expenditure classification of BEE premiums, and to condition all allocations upon the transparent reporting of future, current, and past expenditure on this item.

Furthermore, the uniform treasury norms and standards already exist, at least implicitly, in existing legislation, but the Bill is an appropriate instrument in which to explicitly condition ongoing allocations according to the transparency requirements viz BEE premiums.

Proposals:

Chapter 1 Interpretation

1

[Insert bold]: **““BEE Premium” means any amount paid for in public procurement that deviates from value for money due to considerations of specific goals defined in 2(d) of the Public Procurement Policy Framework Act, or Chapter 4 of the Public Procurement Act.”**

Chapter 2 Equitable Share Allocations

[Insert bold]: **“Section 3(3): The allocation of BEE premiums, which are the only expense that deliberately deviates from value for money in government expenditure, must be made explicit in Column C of Schedule 1.”**

Insert Column C into Schedule 1 accordingly. The allocation in each instance should be “R0.00” if both proposals are heeded to make BEE premiums explicit & to maximize value for money.

Alternatively, if only the proposal is heeded to make BEE premiums explicit then the amount should be stated accordingly.

[Insert bold]: **“5(4): The allocation of BEE premiums, which are the only expense that deliberately deviates from value for money in government expenditure, must be made explicit in Column C of Schedule 3.”**

Insert Column C into Schedule 3 accordingly. Again, the allocation in each instance should be “R0.00”, or some other number if the Committee does not intend to maximize value for money.

Part 2 Duties in respect of annual financial statements and annual reports for 2025/26 financial year:

[Insert bold]: **“14(1) The 2025/26 financial statements of a national department responsible for transferring an allocation in Schedule 4, 5 or 7 must, in addition to any requirement of any other legislation—...(g) indicate the total amount allocated to a province or municipality for the purpose of paying BEE premiums.”**

[Insert bold]: **“14(4) The 2025/26 annual report of a provincial department receiving an allocation in Schedule 4, 5 or 7 must, in addition to any requirement of any other legislation—...(f) indicate the extent to which the provincial department complied with this Act by specifically reporting BEE premiums.”**

[Insert bold]: **“14(5) The 2025/26 financial statements and annual report of a municipality receiving an allocation in Schedule 4, 5 or 7 must be prepared in accordance with the Municipal Finance Management Act, and with the requirement of this Act to transparently report BEE premiums.”**

[Insert bold]: **“14(6) To facilitate the monitoring of performance and the audit of the allocations for the 2025/26 financial year, the National Treasury may determine the format in which receiving officers must report on conditional allocations to municipalities in terms of sections 11(2)(c) and 12(2)(c). National Treasury must determine the format in which receiving officers must report on conditional allocations of BEE premiums to municipalities in terms of this Act.”**

Part 3 Matters relating to Schedule 4 to 7 allocations

[Insert bold]: **“15(1) The National Treasury must, within 14 working days after this Act takes effect, publish by notice in the Gazette—... (c) the framework for each conditional allocation in Schedules 4 to 7 including an explicit prescription for BEE premium reporting in the framework.”**

Part 4 Expenditure in terms of purpose and subject to conditions

[Insert bold]: **“16(2)(a) A framework may provide for components within a conditional allocation that are subject to specific conditions. If BEE premium is to be paid within a framework, then the framework must provide for that component explicitly subject to specific conditions that allow transparency and cost management.”**

All relevant schedules should be amended, *mutatis mutandis* to a) require transparency in BEE premiums & b) reduce BEE premiums to R0 to maximize value for money.

Transparency – PPA

The Bill makes no mention of the PPA. It is common cause that the PPA will impose significant costs, both in terms of reporting compliance, and in terms of expanded BEE premiums. As no provision is

made for this in the Bill, the Bill effectively forecloses the possibility of the PPA coming into effect while the Bill is operative.

PPPFA – Consistency

If any organ of state finds its duties of compliance under the Bill to be inconsistent with requirements under the PPPFA, then it can apply for an exemption from payment of BEE premiums under section 3 of the PPPFA.

Therefore, the Committee need not fear any clash between implementing the proposals provided by IRR Legal, in compliance with the Constitution, and section 2 of the PPPFA.