

## **DEVELOPING THE CAPACITY OF TARGETED ENTERPRISES IN CONTRACTOR DEVELOPMENT PROGRAMMES.**

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### **INTRODUCTION**

The development of contractors from disadvantaged communities in South Africa commenced in the mid-1980s. A number of contractor development frameworks with varying development philosophies evolved from these initiatives, viz :

- Expose building contractors to a formally structured entrepreneurial development programme coupled with continuous on-site practical guidance.
- Provide support systems to contractors who had previous contractual experience; allow them to make mistakes and then to react to these mistakes by showing them where they went wrong.
- Select trainees, train them for several weeks, allow them to tender on simple contracts and allow them to progress to more demanding contracts once they had established their credibility.
- Provide technical and managerial counselling and training to labour only trade contractors and encourage growth from a micro-enterprise to a large contractor.
- Provide pro-active continuous management support and "on-the-job" training while contractors develop commercial, managerial and administrative skills, credibility in commercial circles, experience in pricing complete contracts while accepting increasingly greater risk and contractual responsibility

More recent South African programmes/initiatives range from those which have as their objective the incorporation of "emerging" contractors<sup>1</sup> into the mainstream of the construction industry to those which lean towards job creation and poverty alleviation. Furthermore, the method of involving these emerging contractors ranges from competitive tendering (with varying degrees of assistance) to sheltered or protective methods involving "set aside" projects and negotiated contract prices.

Contractor development programs should be linked to the prioritised needs of a nation's construction industry. Ofori in a study for the UNCHS (1995) notes the lessons learnt from past contractor development programs in developing countries. These lessons include the following:

- Large companies can be used to develop small ones, making for stronger intra-industry linkages.
- Management contracting, or the development team approach can be used to transfer skills to emerging contractors.
- Contractor associations can play a key role in small contractor development.
- Skills training, focussing on technical and managerial skills has significantly improved the ability of small contractors to function effectively.
- Specific measures should be adopted to wean contractors off supporting schemes.

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<sup>1</sup> The Construction Industry Development Board Act (Act 38 Of 2000) defines an "emerging enterprise" as *an enterprise which is owned, managed and controlled by previously disadvantaged persons and which is overcoming business impediments arising from the legacy of apartheid and the "emerging sector" as that sector of the construction industry which comprises emerging enterprises;*

This paper, based on recent developments in South Africa, proposes an integrated approach to the development of country prioritised contractors (typically indigenous /local contractors, with or without size restrictions) to overcome the basic constraints to their growth and development viz. access to markets, skills, finance and and supportive institutional arrangements.

## **PROVIDING ACCESS TO MARKETS**

The Procurement Reform Task Team, established by the Ministries of Finance and Public Works in South Africa, has since the inception of the procurement reform process in 1995, been actively involved in the conceptualisation and development of a system of procurement, commonly referred to as Targeted Procurement, to implement an Affirmative Procurement Policy. (Refer to [www.targetedprocurement.com](http://www.targetedprocurement.com)) (Watermeyer *et al*, 1998)

Targeted Procurement provides employment and business opportunities for marginalised / disadvantaged individuals and communities. It enables social objectives to be linked to procurement in a fair, transparent, equitable, competitive and cost effective manner. It also permits these social objectives to be quantified, measured, verified and audited. This system of procurement, which was developed to enable the 10 Point Plan to be implemented, satisfies the framework provided in the Preferential Procurement Policy Framework Act (Act no 5 of 2000). Targeted Procurement as such allows preferential procurement policies to be implemented. (Watermeyer, 2000)

The Targeted Procurement System classifies contracts on the basis of the scale and nature of resources which are required as being international, major or minor and on the basis of who the contracting entities are, i.e. as being prime, structured joint venture contracts or development contracts. (See Table 1).

The manner in which contracts classified on the basis of “who the contracting entities are”, can best be understood by considering engineering and construction works contracts which are a combination of goods and services. Such contracts are a synthesis of the four basic functional activities, viz labour; materials; construction and materials management; and plant and equipment. The classification of contracts as being prime, structured joint venture or development depends upon the manner in which these functional activities are structured in the tendering entity as outlined in Table 1.

The classification of contracts enables standard targeting strategies to be developed and procurement as an instrument of social policy to be implemented in a systematic and uniform manner. The classification of contracts is a useful means by which elements of the Targeted Procurement system can be linked together in a single descriptor. For example:

- a contract classified as a Prime (Major) contract will require the contracting entity to engage targeted enterprises and / or targeted labour through resource specifications in the performance of the contract; the successful bidder being selected in terms of the development objective / price mechanism on the basis of tendered price and tendered resource goal;
- the contracting entity in a contract classified as a Structured Joint Venture will be a joint venture formed in compliance with the requirements of a resource specifications; the successful bidder being selected in terms of the development objective / price mechanism on the basis of tendered price and tendered resource goal;
- a Prime (Minor) contract is a contract in which enterprises enjoying a particular status are targeted in terms of the direct preference form of the development objective / price mechanism; and
- Targeted Procurement will not be utilised in contracts classified as a being Prime (International) contracts.

The Affirmative Procurement Policy in South Africa, a preferential procurement policy aimed at eradicating the skewed business ownership patterns in South Africa arising from the system of apartheid, is being applied to address the skewed business ownership patterns in all construction sub-sectors (building, civil, electrical and mechanical) is redressed. The Targeted Procurement system has been successfully used in the construction industry to provide access to work opportunities and to create a demand for the goods and services of black owned businesses in South Africa. (Gounden, 2000)

**Table 1 Contract Classification (Watermeyer, 2000)**

CONTRACT		DEFINITION	FUNCTIONAL RESPONSIBILITIES (Labour; materials; construction and materials management; and plant and equipment)
TYPE	CLASS		
Prime	International	Contracts in which the bulk of goods and services are likely to be provided by foreign contracting entities and the domestic content is likely to be relatively insignificant.	The contracting entity is responsible for all four functional activities.
	Major	Contracts, which are of significant, scope and size to warrant the attainment of socio-economic objectives by means of resource specifications.	
	Minor	Contracts which generally have low financial values and in which direct preferences are utilised to achieve socio-economic objectives.	
Structured Joint Ventures		A contract awarded to a joint venture which is structured to meet specific objectives of the client body.	The four functional activities are shared between the parties which constitute the contracting entity in response to the client body's requirements to do so.
Development (engineering and construction works only)		A contract in terms of which the client body appoints third parties to provide certain resources which a contractor lacks.	The contracting entity is responsible for some of the functional activities and the client body provides third party management support for the remainder through the appointment of a construction and/or materials manager.

Targeted Procurement can be set up so as to support a preferential procurement policy relating to the development of a prioritised sector of industry within a country (see Table 2) by targeting:

- Targeted Enterprises by means of direct preferences on low value contracts or through resource specifications as prime contractors, joint venture partners, subcontractors, suppliers, manufacturers and service providers.
- Targeted Partners through resource specifications.

### **A STRUCTURED PROGRAMME FOR THE DEVELOPMENT OF CONTRACTORS**

#### **Introduction**

Construction industry development of prioritised sectors is invariably linked to the development of new entrant small businesses and existing small and medium enterprises ie growth from the bottom up. There are however basic constraints to growth in the small business sector which include access to markets; credit; skills; and supportive institutional arrangements.

Procurement interventions can provide access to markets and as such addresses constraints relating to demand. Certain supply side measure are, however, required for the full enablement of small businesses. (Gounden, 2000). Such interventions should be continued until such time as there are no discernible differences in performance between those who are targeted and those who are not ie as long as they are justifiable.

The desirable outcomes of any national contractor development programme aimed at developing prioritised sectors of a country's construction industry should be that:

**TABLE 2 : FRAMEWORK FOR THE TARGETING OF TARGETED ENTERPRISES IN SUPPORT OF AN INDUSTRY DEVELOPMENT POLICY (after Watermeyer 1998)**

CONTRACT		TARGET GROUP	MEANS OF SECURING TARGET	REMARKS
TYPE	CLASS			
DEVELOPMENT	-	Emerging / fledgling / embryonic enterprises or aspirant entrepreneurs who do not have the capabilities or resources to contract as Prime Contractors.	Contracts are unattractive to non-targeted enterprises because of the third party support provided by the employer.  Non Targeted Enterprises are not competitive because of the contacting arrangements  Contract is awarded to enterprise	Third party management support in the form of construction and materials management services, as appropriate, needs to be provided by the Employer.  The Third Party management support is responsible for any their own negligence and or failure to perform in the provision of services.
PRIME (Works contracts only)	MICRO (Quotations or, Tenders, if value above a prescribed threshold).	Targeted Enterprises (small and micro) performing as prime contractors	Accelerated rotation through quotation rosters. 10 adjudication points are awarded to Targeted Enterprises in terms of a development objective / price mechanism when adjudicating both tenders and quotations.	The accelerated rotation through the quotation roster enables Targeted Enterprises to have more opportunities for the preparation of quotations and hence a greater chance of success. Sureties are waived in respect of prime (micro) contracts. 10 adjudication points translate into an effective price preference of 11,1%.
PRIME (Goods, services and works contracts)	MINOR (Low risk works contract or contracts which are below A financial threshold).	Targeted Enterprises (small and medium) performing as prime contractors	10 adjudication points are awarded to Targeted Enterprises in terms of a development objective / price mechanism when adjudicating tenders.	Sureties are 2,5% on works contracts where estimated tender value is less than a prescribed value Sureties are 5,0% on works contracts where estimated tender value is greater than or equal to a prescribed value. 10 adjudication points translate into an effective price preference of 11,1%.
PRIME (Goods, services and works contracts).	MAJOR (Relatively high risk works contracts or contracts having a contract value in excess of a financial threshold).	Targeted Enterprises performing in various capacities : -prime contractor -joint venture partner -subcontractors -suppliers -manufacturers -service providers	Prime contractors are awarded upto 10 adjudication points in terms of a development objective / price mechanism should they engage Targeted Enterprises in the performance of their contract. The engagement of Targeted Enterprises is defined, measured, quantified and audited in terms of the resource specification.	A Targeted Enterprise can act as a prime contractor only if the contract value is not disproportionate to its annual turnover limits if such limits are provided for. A Targeted Enterprise contracting to act as a prime contractor can be awarded a price preference of upto 11,1% depending upon the amount of work subcontracted to others. 10,0 adjudication points translate into an effective price preference of 11,1%. Sureties in an amount of 10% are required (works contracts only).
STRUCTURED JOINT VENTURE (Goods, services and works contracts)	- (Relatively high risk works contracts or contracts having a contract value in excess of a financial threshold).	Targeted Partners acting as joint venture partners and Targeted Enterprises acting as suppliers, manufacturers and service providers.	Prime contractors are awarded upto 10 adjudication points in terms of a development objective / price mechanism should they engage Targeted Partners in the performance of their contract. The engagement of Targeted Partners and Targeted Enterprises is defined, measured, quantified and audited in terms of the resource specification.	10,0 adjudication points translate into an effective price preference of 11,1%. A Targeted Partner can be given control over the contract should the minimum Joint Venture Participation Goal percentage be set at 60%. A non-Targeted Partner can provide the necessary finances or any resources which the Targeted Partner may lack. It is admissible for two Targeted Partners to form a joint venture for the purposes of the contract as it is not a requirement that one of the joint venture partners be a non-Targeted Partner. Joint Ventures formed in this manner will be awarded an effective price preference of 11,1% Sureties in an amount of 10% are required (works contracts only).

- Targeted Enterprises are able to perform contracts or portions thereof which are of significant, scope and size.
- There is an increase in the value and number of contracts executed by Targeted Enterprises.
- There is an increase in the number of Targeted Enterprises able to tender on relatively large construction contracts.
- Targeted Enterprises increase in number at both prime and subcontract level.

### **Proposed principles underpinning contractor development programmes**

Development programmes for prioritised contractors should be underpinned by the following principles (Watermeyer and Jacquet, 2001):

- Support should be provided to targeted enterprises which make best use of supply side interventions.
- Enabling programmes must not perpetuate the division of the construction industry between a relatively well-resourced sectors and unregistered, poorly resourced sectors.
- Criteria for the provision and discontinuation of support must be clearly stated and made known to interested parties.
- The performance of targeted enterprises should be systematically monitored and evaluated using a database/register which creates, *inter alia*, a track record.
- Clients should pay targeted enterprises promptly.
- Uniform and standard procurement documents, practices and procedures; standard targeting strategies and uniform preferential procurement policies, which are developed at a national level with minimal locality/organisational specific amendments, should be used.
- Exemption based strategies to enable targeted enterprises to grow and develop, should not be resorted to.
- An outcomes based approach should form the basis for any managerial or skills development interventions.
- Training should promote career progression.

Interventions should be designed and structured to:

- address supply side constraints so that prioritised contractors can access the opportunities presented by a preferential procurement policy;
- enable prioritised contractors to overcome the impediments which they face so that they do indeed overcome them;
- provide support to qualifying contractors performing at both prime and subcontract level;
- facilitate access to information, advice, mentoring, business and risk finance services and credit;
- support entrepreneurial, commercial and contract related management skills development;
- enable emerging contractors to mature through the execution of public sector construction contracts (engineering and building) to the extent that there are no identifying disparities between such contractors and non-emerging contractors operating in the same markets;
- encourage and reinforce private sector initiatives and avoid reliance on the public sector which cannot substitute or replace existing finance, training, buying and marketing infrastructure;
- balance the objectives of the promotion of the prioritised sectors with development in non-prioritised sectors and other objectives such as community employment and training; and
- enable prioritised contractors to successfully compete for and secure profitable contracts in both the public and private sectors and to execute such contracts both efficiently and competently.

### **Range of interventions**

The range of interventions in a structured contractor development programme should comprise the following:

## **Type 1 interventions (facilitated by the client)**

The growth of a business is related to a large extent to the experience gained over time in the successful operation of such a business. One of the primary means of accelerating the rate of growth is to accelerate the rate of gain of experience. Type 1 interventions which form an integral part of the procurement arrangements and which are facilitated and paid for by the client, as set out below, provide mechanism for prioritised contractors to accelerate their development by learning from the experiences of other contractors in a structured environment. (Watermeyer and Jacquet, 2001):

- **Third party management support**

In this arrangement, a client employs service providers to provide specific construction and materials management services and to advise, assist and train "on-the-job" fledgling contractors in the execution of the contract and oversee that the works progress satisfactorily according to requirements; thereby reducing the client's risk exposure (Watermeyer, 1992; Watermeyer and Band, 1994; Watermeyer *et al* 1995; Watermeyer, 2000). There is no contract between the prioritised contractor and the third party management support; contracts exist between the third party and the client and between the prioritised contractor and the client.

- **Mentorship**

Mentorship should not be confused with the provision of third party management support. Mentorship is essentially required to bridge the gap between the growth from a fledgling contractor into a fully fledged contractor and from a contractor executing contracts having a particular value and risk profile to a contractor executing contracts having a higher value and / or risk profile. Mentorship is required to accelerate the development of prioritised contractors and in so doing overcome the impediments which they face. Mentorship as such can be seen as the "helping hand" which assists the prioritised contractor to cross the divide between smaller contracts to larger ones. (Watermeyer and Jacquet, 2001)

Mentorship is essential to accelerate the process of development. It affords prioritised contractors, who are awarded contracts in terms of the programme, the benefit of the experience of those individuals who have extensive experience in the construction industry. This exposure is designed to address many of the common shortcomings encountered in such contractors and the lack of track record, eg poor pricing structures, the winning of non-profitable tenders, late starts to contracts, late submissions of payment claims and the late commissioning and hand over of contracts.

A mentor is a trusted and respected advisor. Construction mentors, based on their knowledge gained through practical experience in the construction industry, are able, through their prior learnt skills, to (Watermeyer and Jacquet, 2001):

- guide and advise prioritised contractors in the areas in which they need to improve their competencies;
- develop the technical, managerial, administrative, commercial and business skills of key staff members; and
- set up business systems within emerging companies.

A mentorship programme must neither relieve contractors of any of their contractual responsibilities nor prejudice the competitive position of both prioritised and non-prioritised contractors in the award of contracts. It may reduce the client's risk exposure to non-performance and as such may provide some comfort to financiers and creditors, whilst affording prioritised contractors an opportunity to overcome business impediments. (Watermeyer and Jacquet, 2001)

The client should make provision for the services of an accredited mentor in the contract by including a measurable item for mentorship in the bill / schedule of quantities. This item should comprise a maximum number of hours, the whole or part of which may be omitted by the client, and a fixed hourly rate for mentorship services. (The hours for a particular contract should be based on a formula that takes into account a number of factors, including the estimated value of the contract; the rate for mentors being fixed by the client ). The contractor should appoint the mentor and be reimbursed for the services of the mentor in accordance with the provisions of the contract. As such, there is no contract between the

mentor and the client.

Contractors should be required to obtain the services of accredited mentors. Mentors should assist contractors with the preparation of their tenders at risk and should then be required to certify that, in their opinion, the tenderer is able to complete the contract for the tendered sum. The client should reimburse a mentor for such services, should the tenderer be successful, up to a predetermined amount. The contractor upon award of the contract must submit to the client a mentorship plan that sets out the mentorship requirement for the contract. Mentorship should be provided by the client department only if the plan is approved. The contractor should be required to provide prescribed documentation (evaluation charts, time sheets and the like) with his payment claims for mentorship for certification by the client's agents.

### **Type 2 interventions (facilitated by institutions)**

Type 2 interventions are independent of the procurement arrangements, and generically comprise the following:

- **business and risk management services**

These services should be provided by "for profit" enterprises as is the case for accounting and legal services.

- **supportive institutional arrangements**

These arrangements need to be put in place by government departments, agencies and the like, donor funded non-governmental organisations and related non-profit organisations. Wide ranging interventions may be required, depending upon the regime within which prioritised enterprises operate and may include tender / business advice centres, training in commercial, technical, administration and managerial areas, financial facilitation, "soft" loans, bridging finance facilities, capacity building, etc.

### **Linking procurement and supply side interventions**

Figure 1 shows how the above mentioned interventions can be linked to the procurement regime previously described to accelerate the growth of prioritised enterprises. (Watermeyer and Jacquet, 2001)

## **RECOMMENDATIONS**

The authors based on a decade of experience in contractor development and related procurement arrangements in South Africa recommend that SADC nations adopt the approach to contractor development as set out in this paper to develop indigenous / local contractors within their countries.

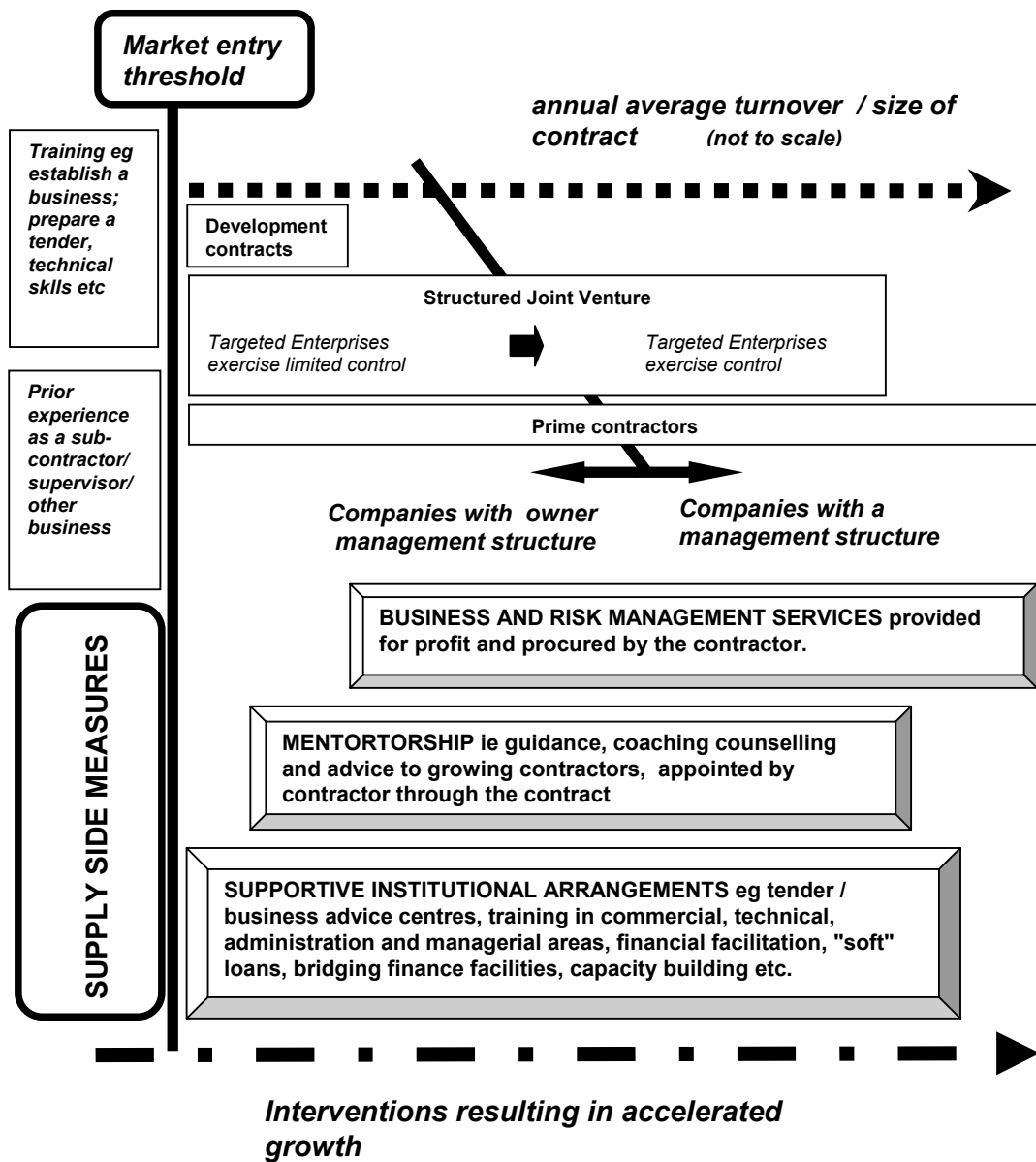


Figure 1: SUPPLY SIDE INTERVENTIONS REQUIRED TO ACCELERATE THE GROWTH OF PRIORITISED ENTERPRISES (Watermeyer and Jacquet, 2001)



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