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CMG101

Contractor Management Guidelines

Consisting of

1 Establishing a Construction Business

2 Operating a Construction Business

3 Executing a Construction Project

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NURCHA CONSTRUCTION FINANCE

The Construction Industry Development Board

SECTION 1

ESTABLISHING A CONSTRUCTION BUSINESS

	TOPIC	CONTENTS
1	**The fundamentals of a construction business**	• Introduction to the business world • Income • Expenditure • Profits and losses • Resources • Mark-up • Attributes of a successful contractor
2	**The construction business environment**	• Contracting strategies • The professional team (architect, engineers, quantity surveyor and project manager) • Joint ventures • Subcontracting
3	**Forms of business**	• Business types • Sole proprietorships • Partnerships • Close Corporations (CC) • Companies
4	**Taxes**	• Government's primary revenue streams • Value Added Tax • Income tax • Employee tax

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CONTINUED

	TOPIC	CONTENTS
5	**Compliance with statutory requirements**	• Operating a construction business • Unemployment Insurance • Skills development levies • Compensation for occupational injuries and diseases • Taxes • Safety on site • Basic conditions of employment • Labour relations • Registration as a home builder • Registration with the Construction Industry Development Board
6	**Growing a construction business**	• The benefits of growing a construction business • Grow a business or expand it? • Growth: Not always a good thing! • When to start growing a business • Where to find opportunities for growth • Targeting and planning for growth • Driving the business plan • Options for growth

Section 1.1: The fundamentals of a construction business

Introduction to the business world

The business world comprises many enterprises that are selling goods which people need **(products)** and/or doing something for other people **(services)**. Construction businesses sell their services and products to a client through a contract that is either agreed verbally or is committed to in writing.

To be financially sustainable, any business must invoice or bill clients more than the total of all the monies that are expended in the course of running the business. The amount invoiced, and subsequently paid, is known as **income**. The amount of money spent on expenses is known as **expenditure**.

To operate as a successful business in the construction industry, income per contract should always be greater than expenditure per contract.

Whatever a business does, it does so for a profit to grow the business and add value to its shareholders.

Income

The reason why businesses fail is that they do not generate enough income to cover their expenditure. It is therefore extremely important that income and cash received are concepts that are clearly understood.

The price quoted for a project should always exceed expenses. This is, however, not enough. Businesses can fail if monies received do not come in time to pay expenses, for example, when a supplier of goods or services demands payment. Construction businesses can also fail if they have insufficient cash to pay for the plant, equipment, materials and labour (resources) required to construct or maintain works.

A construction business needs to generate sufficient cash to pay for the equipment, plant, materials and labour used to construct the works on time.

The amount of money that is available at any one time to pay for resources, service providers or suppliers is known as the contractor's **cash reserve**. Cash reserves can be built up from borrowings (e.g. from a bank) or earnings (e.g. from projects). It is always better to try to generate cash reserves from your earnings rather than your borrowings. Borrowing money costs money. Businesses have to pay interest on borrowings.

Businesses must only borrow money if they are sure that they will be able to repay the money. People in turn, should only go into business if they are sure that they can manage a business' cash flow.

Total income in a particular year is referred to as **turnover**.

Expenditure

Expenditure includes every single item that a business needs to pay money for, e.g.:

Without a sure income and sufficient cash reserves, a business will not be able to operate and will go out of business.

- **Once-off costs:** these are the once-off costs of the business as a whole. Examples of the once-off costs are the cost of creating the company, office equipment such as computers, software and office furniture that are bought for the business.
- **Recurrent costs:** these are the day-to-day operating costs that are paid every month. Examples of recurrent costs are rent, hire of photocopiers, regular office staff costs, water and lights and insurances.
- **Project costs**: these are the costs specific to each particular contract or project. They include the site

establishment, site overhead and supervision costs, materials, plant, equipment and labour specific to the projects on which a contractor is working.

- **Interest:** borrowing money costs money. Interest on monies borrowed is therefore an expense.
- **Taxes:** these comprise company tax, employees' tax and VAT. Employees' tax is covered in the wage bill. VAT should neither be regarded as an income nor an expense. The government taxes profits. The South African Receiver of Revenue charges a percentage tax on a business' total income, minus their total expenditure, including any interest that was paid in the running of a business.

The safest way of expanding a business is out of retained profit. Profit should not be used to fund spending sprees. It should rather be invested in the business to ensure a more prosperous future.

Profits and losses

Profit is the amount of money that remains after all expenses have been paid. Profit does not include salaries, wages, cost of hire of bakkies, rentals or any other cost that is included in expenditure. Note that the salary of a business owner is an expense and not a profit.

Phrases that are commonly encountered with respect to profit are:

- Profit Before Interest and Tax (PBIT).
- Profit Before Tax (PBT).
- Profit After Tax (PAT).

Loss is the shortfall between income and expenditure that needs to be funded by the business.

Resources

Resources refer to the various elements that a construction business uses to execute a contract. These resources comprise:

- **Labour** which is used to construct or maintain works.
- **Equipment** which is required to construct or maintain works, e.g. machinery, power tools, scaffolding, vehicles, etc.
- **Plant** which is installed into the works.
- **Materials** which are incorporated into the works.
- **Money** required to pay for the labour, equipment, plant and materials.

A business needs to not only manage resources, but also to market resources.

In a construction business, the cost of these resources can be split into various sections, being:

- Business operating costs/recurrent costs.
- Once-off business costs.
- Project overhead costs (preliminary and general items).
- Project work content/measured work.

A contractor should match resources to each of the elements, and then ensure that income includes sufficient money to pay for all the resources identified and to make a profit.

Mark-up

Mark-up refers to the amount that a contractor will add on the cost of the measured works and preliminary and general items. A contractor needs to provide sufficient mark-up to cover the costs of business overheads (business operating costs and once-off business costs), profits, and an **allowance for risks**.

There is always a risk on every project. The extent of the risk will depend on a variety of factors such as the stability of the workforce, dependability of supplies and closeness to your suppliers, ability of the client to pay, etc.

Risk is the chance of something happening that could have a bad impact on the profit associated with a project.

Attributes of a successful contractor

The attributes of a successful contractor are that they:

- Motivate their workforce to produce the correct quality of work in as short a time as possible (i.e. they have high levels of productivity).
- Satisfy their customers' expectations.
- Pay their suppliers on time to increase their credit rating and to obtain any discounts that are offered.
- Have the confidence of their bank manager.
- Pay their taxes on time.
- Comply with statutory requirements.
- Identify opportunities and take maximum advantage of them.
- Have the respect of their clients, their customers and their peers (colleagues and competitors).
- Make a good profit every year.

A successful construction business has:

- A continuous work flow.
- Clients that are fully satisfied with the quality and timelines of its work.

A successful contractor has, or can obtain, various management skills including those relating to:

- Setting of appropriate targets (goals and objectives) for achievement and against which the business can measure itself.
- Marketing the business effectively.
- Pricing products and services correctly.
- The ability to buy and/or hire plant, equipment and materials at competitive prices.
- Managing profits and losses and the business' cash flow.
- The ability to keep records of all business transactions.
- Managing the workforce.
- Planning ahead.
- Managing time effectively.

The success of a construction business depends upon its understanding of how internal and external factors affect the business and how to deal with them.

The construction industry is not a place for the faint hearted.
It is a ruthless world where it is the "survival of the fittest".

In addition, a successful contractor must be able to:

- Interact effectively with clients and their professional teams.
- Have the ability to know what his rights are and, as importantly, when to "fight for his rights", when to negotiate and when not to fight.

As with any businessperson, a contractor must be able to make decisions. These must be based on all the available information and then, once they are made, a successful contractor must stand by those decisions and do whatever is necessary to achieve the required outcomes relating to those decisions.

A successful contractor must be prepared to work long hours as the projects may demand from time-to-time. However, a contractor must be able to manage his overtime to suit personal commitments outside of the business.

Above all, the contractor must observe the three "absolutes" of project/construction management, namely that a project must be completed on time to the required quality and within budget.

The contractor must therefore be able to do the right things, right the first time, at the right time, to the right quality, at the right cost.

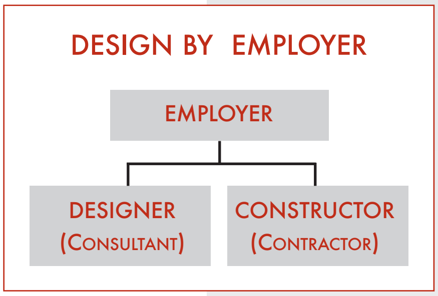
Section 1.2: The construction business environment

Contracting strategies

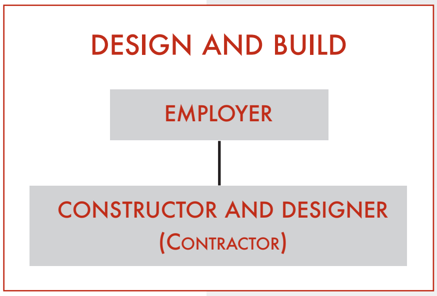
Construction works may be defined as everything that is constructed or results from construction operations. These need to be designed and constructed. Construction works also need to be maintained so that they continue to serve the purpose for which they were constructed.

Clients often do not possess the expertise or resources to design and construct construction works. They contract or employ businesses to do so in which case they are often referred to as "employers".

In the "**design by employer**" contracting strategy, the employer appoints consultants (design professionals) to design the works and a contractor to construct the works designed by the appointed consultants. The consultant is also required to confirm that the contractor constructs the works according to the requirements of the consultant's design.



In the "**design and build**" contracting strategy, the client appoints a contractor to both design and build the works. The contractor usually appoints a consultant to design the works for him.



The "**design by employer**" contracting strategy is the most popular approach in South Africa to providing construction works.

The client may also appoint a professional or a consultant to provide the contractor with the drawings and any instructions regarding how the works are to be constructed. This professional will also be required to certify the amount of money due to the contactor.

The professional team

On projects there will often be what is generally referred to as "the professional team". This team can comprise one or many professional people called "consultants". They are appointed by the client to perform various activities.

The size of the professional team depends on the size of the project. A house construction project may only have an architect whereas a shopping centre construction project could have an architect, quantity surveyor, project manager, civil, structural, mechanical and electrical engineers.

Those responsible for the design of construction works are skilled people who have qualifications from a university or other institution of higher learning and who are professionally registered with the Engineering Council of South Africa or the South African Council for the Architectural Profession.

Architect

The architect is involved in building projects. The architect needs to know various aspects about the building that is being developed. He will know where the building lines are, i.e. the lines away from the boundary over which the building must not be built. He also knows the area of the buildings that is allowed by the municipality to be built on a particular site and the amount of parking that must be provided. He will also know how high a structure can be built on a particular site. His training would enable him to design a building in such a manner that certain parts of the building would receive the maximum amount of sunlight. For example, the architect would normally try to position the living areas of a house to face in a northerly direction and the cooking areas to the south so that the living areas receive the maximum amount of sun during the day. An office window facing west, i.e. into the setting sun would be unbearable in most parts of South Africa in the afternoons without air-conditioning to the building.

The architect is extremely important to the client when it comes to the design of his building. The architect can make a building usable and functional in the most economic and efficient way. If the architect does not have the required training or if an owner builds a building himself without making use of the services of an architect there could be problems with the completed structures. These problems could include not being able to get the approval of the municipality to use the building, or that the buildings would not be functional for the intended use.

The architect also may produce the certificate on which the contractor gets paid, or he may authorise the payment of a certificate that has been produced by a quantity surveyor who has been appointed as part of the same professional team.

Engineers

There are several types of engineers that a contractor may encounter. These include (most commonly):

- Civil engineers.
- Structural engineers.
- Electrical engineers.
- Mechanical engineers.

Engineers are the people who make sure that the various structures or pipe lines or air-conditioning units, etc., meet the design requirements on the various projects. For example, in a building designed by an architect there could be structural components incorporated in the structure, i.e. concrete slabs. The structural engineer will have to calculate the required thickness of the concrete slab and the required amount of reinforcement to be placed in the concrete slab. Should the contractor not build the slab to the required thickness and not placing the required diameter steel in the correct position, the slab could fall.

A road is designed by a civil engineer who will determine the number and loads of the vehicles that will use a particular road over a required period. He will then design the foundation layers of the road to ensure the road will last over the required period. A civil engineer will also be involved in projects involving the construction of municipal services (water mains, sewer pipelines and stormwater systems), and his job on these projects will include calculation of the diameter of water pipes and sewerage pipes and also in ensuring that all the municipal regulations are complied with. Generally, wherever there are roads or services beneath the ground, a civil engineer will be involved, and whenever there are structures above the ground more than one story in height, it is normal that a structural engineer will be required on a project.

Before starting a project contractors should understand who is on the professional team and what their roles and responsibilities are in accordance with their contract.

It is in the contractor's interest to get on with each of the members of the professional team. This is not always easy, but wherever a contractor can, he should strive to do this.

The mechanical engineer's function is to ensure that all the mechanical equipment that is built into a particular building will function satisfactorily, for example, the air-conditioning. The mechanical engineer will know how much air-conditioning will be required to keep rooms and areas in a building at a particular temperature within various seasons at various times of the day. He will thus design the air-conditioning plant and the air-conditioning units to suit the most efficient and effective way that the building's temperature can be regulated.

An electrical engineer will be required to design the lighting layouts in a building and to make sure that all the mechanical equipment, apparatus, stoves, etc., have sufficient power for them to operate satisfactorily.

The client pays the municipality or Eskom based on the amount of power that is supplied to a building. If the electrical engineer overestimates the power requirements, then the owner of the building will pay too much. If he underestimates the requirements, then various pieces of equipment will not function properly.

The other types of engineers that a contractor may come across are lift engineers or refrigeration engineers that have specific and detailed knowledge of various elements of the building in which they specialise. The similarity between all of the engineers is that they are all qualified to design the various aspects of a construction works project by way of their qualifications and experience. They take the responsibility for the design and, if the contractor builds to their design and the design fails, then the engineer is liable to rectify the work at his own cost, or he can be sued for damages that occur due to poor design. This can include injury to persons and loss of life. If the contractor does not build in accordance with the engineer's design, then the responsibility is transferred to the contractor, who then becomes liable for any faults and becomes responsible for any damages that can arise in the buildings and civil works due to the non-compliance to the design and/or specifications by the engineer.

Quantity surveyor

The quantity surveyor is also a qualified professional who is employed on building projects to "measure" the works. He will calculate the cost of a building by splitting the building up into various elements and trades which will include brickwork, plastering, carpeting, etc., and will measure the work that is required in each of the trades. He will then produce a bill of quantities and the contract documents on which the contractors bid. The quantity surveyor will be involved in the adjudication of the tenders and ensuring that all contractors comply with the terms and conditions of the contract. The quantity surveyor is employed on the project to measure the works on behalf of the client as the contractor progresses with the work and produce the payment certificate which the client uses to pay the contractor.

The quantity surveyor is employed on building projects and is generally not involved on civil engineering projects where the quantities are measured by the civil engineer. On some building projects the architect himself performs the quantity surveying functions with regard to the producing of the payment certificate. In fact, the architect may issue certificates on building projects even though the architect may have a quantity surveyor working with him.

Project manager

The project manager is chosen by the client for that person's or organisation's ability to successfully manage the completion of a project on time, within budget and to the required quality. It is possible that the project manager will not liaise directly with the contractor, but will liaise with the professional team who are appointed to ensure that the works progress satisfactorily. The roles and responsibilities of a project manager could be very broad and could include the management of a whole project from its conceptual design stage through its tendering stage, its construction stage and its handover and commissioning phases. It could, however, be restricted to purely the installation of shop fitting for a particular company who are going to be letting some space in the building that is being constructed.

The contractor may also appoint a person whom he refers to as "project or contracts manager" but he will not be a part of the professional team.

The contractor must ensure that he knows what the responsibilities of the project manager are on a project, if there is one appointed.

Joint ventures

Joint ventures are unincorporated bodies, regarded in law as partnerships in which the partners are jointly and severally liable for the acts, neglects and omissions of the partnership.

Contractors may form joint ventures for a number of reasons, including:

- The project is too large or complex for one company to undertake with its available resources.
- The project requires specialist skills or abilities which the company is unable to provide on its own.
- In developing countries, including South Africa, the skills and expertise of emerging firms can be developed through their association in joint ventures with well-established, experienced companies.

Joint ventures may operate in two distinctly different ways, but in practice most operate as a mix of the two broad alternatives which are:

- The members of the joint venture pool their resources and the contract is executed by the joint venture using the pooled resources.
- The work and obligations making up the contract are broken down into discrete elements or sections, usually on the basis of locality, the nature of the work or the capabilities and resources required. Each element is assigned to a specific member of the joint venture who assumes full responsibility for its execution under the direction of the joint venture.

A joint venture agreement should:

- Clearly and comprehensively set out the contributions to be made by each member towards the activities of the joint venture in securing and executing the contract and should allocate monetary values to such contributions.
- Record the percentage participation by each member in all aspects of the fortunes of the joint venture, including risks, rewards, losses and liabilities.
- Provide for meaningful input by all members to the policy-making and management activities of the joint venture.
- Provide for the establishment of a management body for the joint venture.
- Should provide measures to limit, as far as possible, losses to the joint venture by the default of a member.
- Promote consensus between the members whilst ensuring that the activities of the joint venture will not be unduly hindered by failure to achieve it.
- Provide for rapid, cheap and easy interim dispute resolution and for effective final dispute resolution, if required.
- Be sufficiently flexible to allow for joint ventures which differ in nature, objectives, inputs by members, management systems, etc.

The successful operation of a joint venture requires a high degree of trust and cooperation between the members.

The following standard joint venture agreements are available:

- cidb Joint Venture Agreement.
- The South African Federation of Civil Engineering Contractors (SAFCEC) Joint Venture Agreement and Heads of Agreement.

SUBCONTRACTING

The practice of subcontracting portions of a construction works contract to others is a well-established practice in South Africa and elsewhere in the world. The reasons for subcontracting vary between the different types of construction works contracts. In some contracts, there may be a need to acquire specialist capabilities to perform certain aspects of the work. In others, there may be a need to subcontract portions of the work to increase the contracting capacity of the contractor or to satisfy client requirements or expectations relating to the engagement of small and micro enterprises or local enterprises in a contract.

There are three types of subcontractors:

- **A domestic subcontractor** is a subcontractor appointed by the main contractor at his discretion in which case the contractor is free to negotiate the prices and terms for subcontracting.
- **A nominated subcontractor** is a subcontractor nominated by the employer which the contractor is obliged to appoint as a subcontractor.
- **A selected subcontractor** is a subcontractor selected by the contractor in consultation with the employer in terms of the requirements of the contract.

The main contractor has no control over the appointment of a nominated subcontractor and as such cannot be held responsible for any delays in appointing such a subcontractor. A contractor may on justifiable grounds refuse to contract a nominated subcontractor.

The contractor remains responsible for providing the portion of the works that was subcontracted to a domestic subcontactor or a selected subcontractor as if the work had not been subcontracted.

A contractor is free to negotiate prices and the terms of the contract with a domestic subcontractor.

The employer usually selects nominated subcontractors following a competitive tender process.

A selected subcontractor is usually appointed following a competitive tender process.

Section 1.3: Forms of business

Business types

Contractors typically trade under one of the following business types:

- Sole proprietor.
- Partnership.
- Close Corporation (CC).
- Proprietary Limited (Pty) Ltd.

Sole proprietorships

An individual may set up a business and work on contracts without registering a company. A sole proprietorship, in law, is regarded as an extension of an individual and offers no protection against business risk. If the company owes money, it is the same as owner of the company owing money. If there are claims against the business, the claims are against the owner in his personal capacity.

As far as income tax is concerned, the taxes that the company is liable for is the same as that of the owner. Any profits in the business are taxed as personal income.

A sole proprietor, like every other contractor, is required to register as an employer with various bodies such as the Unemployment Insurance Fund and Compensation Fund (see section 1.5).

A sole proprietor is the easiest business type that a contractor may operate under. It is, however, a very risky option as the owner is liable in his personal capacity for any debts of the business. It is for these reasons that other types and styles of business are recommended. A number of employers do not encourage contractors to trade as sole proprietors and prefers to deal with CIPRO-registered entities.

Partnerships

Another risky business alternative in the construction industry is a partnership (or unincorporated joint venture) (see section 1.2).

A partnership is formed when two or more people (but not more than 20) agree to come together and operate a business as partners.

Each person might bring something to the business such as their own particular skills, people, equipment, or money. As with a sole proprietorship, everything is at risk in the event of a collapse of the partnership as the law regards a partnership as a group of individuals who are co-owners of the assets and liabilities of the partnership.

If one of the partners becomes unable to pay his debts in his personal capacity, the liquidator may attach the assets of the partnership. If the value of the assets is not enough to cover the debt, the liquidator may then decide to attach the personal assets of the other partners.

When setting up a business, the initial step should be to consider the most appropriate way the owner wishes to conduct his business.

This is where the individual trades under his personal name, although he may often add " Trading as..." under another name.

Sole proprietorships and partnerships permit an individual to work independently, or with others in partnership. They do not necessarily cost anything to set up, but offer no protection to the owners in the case of claims and the owners are thus subjected to a high degree of risk.

A partnership may be entered into by means of a written or verbal contract. A partnership agreement should cover at least the following items:

- The shareholding of the partners.
- The sharing of the profits (and losses).
- The senior partner and what he is entitled to do on behalf of the business, i.e. what is his authority.
- What the other partners are allowed to do on behalf of the business i.e. what is the authority of each of the partners.
- How often formal partner meetings are to be held and what will be discussed at the meetings.
- The contributions, monetary and otherwise, to be made by each of the partners.
- What circumstances will cause the partnership to dissolve (end).
- Payment of taxes.
- The functions of the partners.
- The remuneration to be paid to the partners.

It is unlikely that a partnership agreement will protect a partner if one of the partners has manipulated the books or has created a debt in the company that it cannot pay. The agreement will allow partners to seek compensation against a defaulting partner. However, any person claiming (claimant) against the partnership will be unlikely to concern themselves with the internal agreements of the partnership.

Advantages of a Close Corporation include:

- A CC is a unique legal entity.
- No annual returns are currently required.
- Audited financial statements are not required.
- Meetings are not compulsory and can be held on an ad hoc basis.
- CCs may become shareholders in other companies.
- All members may take part in management.
- The proprietor or member is not personally liable for the debts of a CC.
- The legal procedures for registration and administration are kept relatively simple.

Close Corporations (CC)

A Close Corporation (CC) is a legal entity in its own right, comprising one or more members (but not more than 10 members). A liability in terms of the law against the Close Corporation is not a liability against an individual member. If a member is sequestrated in his personal capacity, his share of the CC can be sold to pay for his personal debts, but not the shares or personal assets of the other members.

To register a Close Corporation, a Founding Statement under the Close Corporations Act of 1984 must be completed in triplicate and submitted to the Registrar of Companies and Close Corporations. To make it easy, the Registrar merely requires that the form called CK1 be filled in as this form includes all the information that is required (obtainable from http://www.cipro.co.za).

The information required is straightforward, such as information regarding the members of the CC (full names, ID numbers, postal and street addresses, percentage share, contribution of each member) and the address, etc. of the Close Corporation itself. Three points to specifically note on the form are:

Chosen name of the CC: It is good to have alternatives as your chosen name may not be acceptable. A name would not be acceptable if it has already been used, if it is too broad and non-descriptive, for example South Africa CC, or if it is derogatory or vulgar. (Form CK7 must be completed and submitted to apply for the reservation of a name for the CC).

Description of business: The form requires that the description of the business be entered. This should be stated in a broad and flexible manner, for example: "The development, management and implementation of construction projects".

Accounting officer: The name of the accounting officer, together with his address and membership or practice number needs to be filled out on the form. A letter from the accounting officer, accepting the appointment, needs to be submitted with the CK1. An accounting officer may be contracted from information obtained from the Institute of Chartered Secretaries and Administrators (Tel. 011 403 2900).

One revenue stamp (currently R100,00 in value) must be fixed to the first copy of the form, together with the letter from the accounting officer, and all three forms must be sent or hand delivered to the Registrar.

All the above can be done by the members themselves at relatively little cost. There are, however, business attorneys and other experienced individuals who specialise in setting up Close Corporations. They often do not charge excessively.

Founding Agreement: When there are two or more members in the CC, it is advisable to have a Founding Agreement in writing. The Founding Agreement is an agreement that is signed by each of the members and it is recommended that it should contain all the aspects as outlined in the partnership's agreement.

The members of a CC are the registered "owners". Any changes in respect of the members of the CC must be notified to the Close Corporation Registration Office in Pretoria. (PO Box 429, Pretoria, 0001).

Companies

There are two types of business companies. They are:

- A private company.
- A public company.

A private company may have a maximum of 50 shareholders and no shares may be sold to the public. A public company may have unlimited shareholders and may sell shares to the public through the Johannesburg Stock Exchange. (A private company needs to trade for at least three years before listing on the Stock Exchange as a public company.)

The shareholders of a private company appoint from amongst themselves or even non-shareholders persons to act as directors. All directors are collectively called the board of directors. The board of directors is responsible for the management of the company.

The formation of a company, known as a (Pty) Ltd company is more complicated and costly than setting up a CC and an attorney or an auditor specialising in this field should be appointed to set up and register (float) the company. As with a CC, the company is registered with the Registrar of Companies and Close Corporations.

The accounting/financial books of a CC may be prepared by a financial accountant whereas the accounting/financial books of a (Pty) Ltd **must** be prepared by an auditor.

The Companies Act, No 61 of 1973 imposes personal liability on directors where in common law such liability may not exist or be difficult to prove. Any person, not only a director, who is knowingly a party to the carrying on of a business in a reckless (gross carelessness or gross negligence) or fraudulent manner can be personally liable for all or any of the debts of the company.

Private companies may have a larger shareholding than CCs and as such may have a larger capital base.

The accounting officer must be registered with one of the following institutions:

- The Institute of Administration and Commerce of Southern Africa.
- Accountants and auditors registered in terms of the Public Accountants' and Auditors' Act, 1951.
- The Chartered Institute of Management Accountants.
- The Southern African Institute of Chartered Accountants.
- The Southern African Institute of Chartered Secretaries and Administrators.
- The Chartered Association of Certified Accountants.
- The Southern African Institute of Business Accountants.
- The Institute of Commercial and Financial Accountants of Southern Africa.

A company is a legal person who has capacity and powers to act on its own.

The main reason to register a Close Corporation, or a Company, is to separate the individual from the business in terms of the law, thereby safeguarding the individual, under most circumstances, from the loss of personal assets in the case of problems in the business.

It is a relatively easy operation to convert from a CC to a (Pty) Ltd as a business grows.

The differences between a private company and a Close Corporation may be summarised as follows:

Private Company	Close Corporation
Can have a maximum of 50 members	Can have a maximum of 10 members
Companies can be shareholders	Companies cannot hold a member's interest
Comprise of directors and shareholders	Comprise of members
Has a memorandum	Has a founding statement
Registered articles of association	Articles of association are not required
Compulsory annual return to be lodged	No annual return to be lodged
Has a share capital	Has member's contributions
Has an auditor	Has an accounting officer
Convenes an annual general meeting	Annual general meeting not required
Members hold shares	Members hold member's interest
Can acquire its own shares under certain circumstances	Can purchase a member's interest
Directors are responsible for the day-to-day management	Members are responsible for the day-to-day management
Register of members	No register of members
Audited financial statements	No financial statements needed
Prohibition to provide financial assistance for the acquisition of its own shares	No prohibition to provide financial assistance for the acquisition of a member's interest

Section 1.4: Taxes

Government's primary revenue streams

Without the revenue from tax, the government cannot perform its duties. Government needs taxes to fund social and economic programmes, and to provide public goods and services, such as schools, universities, hospitals, clinics and roads, as well as defence and security. Every year, the minister of finance presents the budget, which outlines the total government expenditure for the following financial year and the ways in which this expenditure will be financed.

Government collects taxes from two main sources:

- Value Added Tax.
- Income Tax.

Taxes on income and profits are levied by the National Government in terms of the Income Tax Act, 1962. Provincial and local governments do not levy taxes on income nor do they levy value-added tax (VAT) or any other form of general sales tax. Each person earning over a certain amount, and each organisation that is making a profit, **must** pay taxes.

Value Added Taxes apply to all people buying goods and services.

Value Added Tax (VAT)

Several countries collect money from individuals and companies from a system of Value Added Tax. When you buy goods from a shop you pay VAT. The shopkeeper then "looks after" the money for South African Revenue Services (SARS) for a period of up to two months, and then adds up all the VAT amounts collected, and sends this amount to SARS. The shopkeeper collects VAT on behalf of SARS. The VAT is never his money. The shopkeeper is known as a **VAT Vendor**.

In South Africa, every business with a turnover of R300 000 per annum and more **must** register as a VAT vendor. However, the South African Revenue Service proposed that the threshold be increased from an annual turnover of R300 000 to R1 million.

Any business operating within a turnover from R20 000 to R300 000 per annum **may** apply to become a VAT vendor. The SARS may or may not agree to register such an enterprise.

The first step of registration is to obtain a VAT101 Form from a SARS office or the internet (www.sars.gov.za) and to complete this form.

Successful applicants will then be sent a "Notice of Registration" form which will indicate the following:

- **VAT Registration number:** The VAT registration number is a unique number assigned to a business. All correspondence relating to VAT, therefore, must contain that number. The business' VAT number **must be stated on every invoice**.
- **Period payments:** VAT is generally paid by the business to SARS every two months except where the business' turnover is less than R1 million or greater than R39 million. Businesses with a turnover of less than R1 million are only required to submit every four months and businesses with a turnover exceeding R39 million, every month.

All contractors have to be in "good standing" insofar as their tax and service charge obligations are concerned in order to contract with government.

SARS

TAX EVASION is a serious crime. A business should approach SARS if it has problems in paying its taxes as arrangements can be made to pay SARS over time.

Value Added Tax (VAT) is levied at a standard rate of 14% on all goods and services subject to certain exemptions, exceptions, deductions and adjustments provided for in the VAT Act 89 of 1991, as amended.

It is the government's second biggest source of income.

The owners of Sole Proprietorships and Partnerships must register as VAT vendors under their own names.

The owners of a CC or a Private Company must register as a VAT vendor in the name of the business.

- **Category:** In order for SARS to "stagger" their workload, some tax periods end on the last day of January, March, May, July, September and November, referred to as Category A (odd months of the year). Category B tax periods end on the last day of February, April, June, August, October and December (even months of the year).

  (The date on which an application is made will generally determine which category a business falls into. Other than the date of submission, all other aspects are identical between the two categories.)

Registered VAT vendors are required to:

- Provide correct and accurate information to SARS.
- Submit returns and payments on time.
- Include VAT in their prices, advertisements and quotes.
- Keep accurate accounting records for five years.
- Produce relevant documents when required by SARS.
- Notify SARS about any changes in their business - especially its address, trading name, partners, members or shareholders, bank details and tax periods.
- Issue tax invoices, debit and credit notes.
- Notify SARS of any changes of the details of the person representing the vendor.

One of the underlying principles of the South African VAT system is that it is an invoice-based tax. This means that vendors are generally required to account for VAT on the basis of invoices being issued or received. This method of accounting is referred to as the "**invoice basis**". However, vendors who are sole proprietors and partnerships whose turnover is less than R2,5 million, may qualify to use a different method referred to as the "**payment basis**" of accounting.

In the **invoice basis** methods, vendors must account for the full amount of output tax on any supplies invoiced in the tax period, even where payment has not yet been received. Similarly, the full amount of input tax may be claimed on supplies received in the tax period, even where payment has not yet been made.

In the **payment basis**, vendors must account for the VAT on actual payments made and actual payments received in respect of taxable supplies during the period.

A vendor is liable to pay the tax only on the "Value" that has been "Added" by the business.

In a construction works project value is added to the purchases of materials, hire of equipment etc.,that have been bought for the works. If the construction works contract is worth R100 000 (excluding VAT) then the VAT that the employer will be charged is R14 000 (14% of R100 000). This R14 000 is held by the contractor on behalf of SARS until the due date for payment. This tax is known as the "output tax."

Before paying the tax to SARS, the contractor is allowed to deduct from this amount, the amount of VAT that is paid to VAT vendors in purchases of materials, hire of equipment etc. This tax is known as input tax.

Every invoice issued must:

- Include the business' VAT number.
- State the business' registered name and address.
- Give the date.
- Include a serial number, i.e. invoice number with the numbers on each project being consecutive and each invoice having its own unique number.
- Have the words "TAX INVOICE" stated somewhere on your invoice (The words "VAT invoice" or "invoice" are unacceptable).
- Show the VAT amount separately (Using the words "VAT is included at 14%" is not acceptable).

The amount payable to SARS is the difference between the "**output tax**" and the "**input tax**".

As an example, if in the two month VAT period the business has produced invoices to an amount of R325 000 excluding VAT. Your total invoices including VAT will be:

Total invoices for 2 month period (excl. VAT)	R 325 000
VAT @ 14% (output tax) (14 ÷ 100 x R325 000)	R 45 500
Total invoices (including VAT)	**R 370 500**

During the same two month period, the business can claim for all materials, plant, services etc., purchased from VAT vendors that you have been invoiced (for **invoice basis** payers) or paid (for **payment basis** payers). If in the same two month period, amounts totalling R150 000 + VAT (14% x R150 000 = R21 000), i.e. R171 000 was paid out to VAT vendors, a deduction of R21 000 is permitted.

Output tax	R 45 500
Less input tax	R 21 000
Total to be paid to SARS	**R 24 500**

The penalties for late payment of VAT are heavy, i.e. 10% of the money that you should have paid even if one day late. In addition, interest is payable on late payments until the date that you make the payment.

Failure to submit VAT returns and to pay the VAT due is a criminal offence.

There is a booklet issued by SARS called **" Value Added Tax Guide for Vendors (VAT404)"**. It is available free of charge from their offices and clearly lays out your responsibilities in terms of VAT.

There are some payments that businesses make that may not be claimed as input tax. These are described in SARS's Value Added Tax Guide for Vendors (VAT404). Input claims cannot be made for purchases from anyone who is not a VAT Vendor.

Income tax

Income tax is levied on South African residents' income earned worldwide, with appropriate relief to avoid double taxation. Non-residents are taxed on their income from a South African source. Tax is levied on taxable income that, in essence, consists of gross income less allowable deductions as per the Act.

The lower income earners pay a smaller percentage of their income in tax than higher income earners. The income earned by sole proprietors and each partner in a partnership forms part of their personal income and is taxed as such.

Income tax is the government's main source of income and is levied in terms of the Income Tax Act 58 of 1962.

Tax threshold is the amount a person must earn before they must pay tax. In this tax year, it is R40 000 for individuals under 65 years and R65 000 for individuals 65 years or older.

Income tax returns are issued to registered taxpayers every year. The year of assessment for individuals covers 12 months, beginning on 1 March and ending on the last day of February the following year. Companies are permitted to have a tax year ending on a date that coincides with their financial year. The Act also provides for certain classes of taxpayers to have a year of assessment ending on a day other than the last day of February.

Tax returns must be submitted to SARS on the date given. A taxpayer may apply for extension.

Employee tax

A business that pays salaries, wages and other remuneration above the tax thresholds must register with SARS for employees' tax. This is done by completing and submitting an EMP101 form to SARS. Once registered, the employer will receive a monthly return (an EMP201) that must be completed and submitted together with the deducted tax within seven days after the end of the month for which the amount was deducted.

Employees' tax is the tax that an employer, as an agent of the government, deducts from the earnings of employees and pays over to SARS every month. This monthly deduction serves as credit that is set off against the final tax liability of an employee, which is determined once a year. Employees' tax consists of SITE (Standard Income Tax on Employees) and PAYE (Pay As You Earn). The remuneration of directors of private companies (including individuals in close corporations performing similar functions) is subject to employees' tax paid twice a year as provisional tax.

Private companies and close corporations need to register as taxpayers. These companies are taxed at a flat rate of 29%. In addition to this, secondary tax (STC) on companies is levied on companies at a rate of 12,5% on all company after tax profits distributed by way of dividends.

Small-business corporations (those with an annual turnover of less than R6 million) benefit from a graduated tax rate of 0% on the first R35 000 taxable income, 10% from R35 001 to R250 000 taxable income and 29% in excess of R250 001 taxable income, are allowed to write off certain investment expenditure in the year in which it is incurred.

It is beyond the scope of most contractors, and indeed businesses in general, to be able to submit Company Tax Returns without appointing specialists to help them. (Pty) Ltd companies are required by law to appoint an auditor. Sole proprietor, partnerships or CCs do not have to appoint an auditor. It is, however, recommended that these forms of businesses appoint an auditor, an accounting officer, or a company tax expert to complete these returns. Such experts will advise on what deductions are permitted from the gross income to determine company profits.

Businesses are advised to calculate their tax obligations based on profits before tax at regular intervals so that provision can be made to meet tax obligations which are to be paid twice a year.

Section 1.5: Compliance with statutory requirements

Operating a construction business

Laws are sets of rules and regulations **(statutory requirements)** established by a government. Law affects everyday life and society in a number of ways. They regulate the rights and actions of people and organisations. Failure to comply with statutory requirements may result in fines or penalties being imposed and in extreme cases the imposition of jail terms. Failure to comply with statutory requirements can easily result in the failure of a business.

South African law is established in Acts of Parliament and Regulations issued by ministers in terms of an Act of Parliament.

There are many laws that are applicable to the construction industry. The cidb has identified 128 laws that might apply (see cidb compendium of legislation on www.cidb.org.za). Not all of these laws apply to a construction business or all construction businesses.

Ignorance of the law is no defence.

Failure to comply with certain statutory requirements can disqualify a construction business from contracting with clients.

Construction businesses are not permitted by law to contract with any client if they:

- Are not in good standing with the Compensation Fund or with a licensed compensation insurer (Federated Employers Mutual Assurance (FEM) for the building industry).
- Cannot reasonably satisfy the client that they have the necessary competencies and resources to carry out the work safely.
- Wish to construct a house and they are not registered as a home builder with the National Home Builders Registration Council.

The law furthermore prohibits a government department, a provincial department, a municipality or a state owned enterprise from entering into a contract with a construction business to undertake construction works if that business:

- Is not registered with the Construction Industry Development Board.
- Is not in possession of a Tax Clearance Certificate of Good Standing issued by the South African Revenue Services (SARS).

SARS will only issue a business with a Tax Clearance Certificate if the business has not contravened the provisions of the Income Tax Act (1962), Employees Tax (PAYE as contained in the Income Tax Act), Skills Development Act (1999) or Unemployment Insurance Contributions Act (2002) as at the date of the certificate. Tax clearance certificates are valid for a period of one year, provided that no taxes, levies or duties become due and outstanding during this period.

Unemployment insurance

Just over one in four people in South Africa who are economically active (people who are at a stage of their lives that they need to work) are unemployed. Many have had jobs, but through no fault of their own have lost their jobs. The government has established a fund that will help such people. This fund is called the Unemployment Insurance Fund (UIF).

The Unemployment Insurance Act, 2001, establishes the Unemployment Insurance Fund.

The Unemployment Insurance Contribution Act, 2002, provides for the imposition and collection of contributions for the benefit of the Unemployment Insurance Fund.

This fund was established to assist those who lose their jobs or stop receiving a salary for a period of time as a result of pregnancy, illness, adopting a child under the age of two years, as well as upon the death of the breadwinner of the family.

See the Department of Labour's website for more information - www.labour.gov.za

It is possible to register on-line, via e-mail, telephone, fax or mail. Employers may also register at a labour centre.

Each employer deducts 1% of an employee's wage/salary earned from the employee for this fund and adds the same amount (another 1%), and sends the total to the fund as a contribution from the employee to the UIF or South African Revenue Services before the 7th of every month.

If an employee is earning a total wage of R3 000 per month, the deduction is R30 (1% of R3 000) from his wages each month. The employer adds R30 and sends R60 to the Unemployment Insurance Fund on his behalf.

Credits are given to the worker as they work and contribute to the fund. For every six days worked, one day's credit is granted up to a maximum of 238 days. To build up the maximum credits an employee has to work for four years. If an employee has worked for less than 238 days, only the number of day credits that have been built up may be claimed. The benefits are calculated on a sliding scale dependent on the employee's salary and range from 38% for the highly paid workers (earning more than R8 099 per month) to 58% for the lowest paid workers.

If an employer comes to the end of a contract and there is not enough work to carry on employing an employee, the services of the employee may be terminated. The employee may then claim from the fund if he has been contributing to the fund.

Each employer **must** register with the Unemployment Insurance Commissioner by completing form UF1. The Unemployment Insurance Fund is administered by the Department of Labour.

Skills development levies

The Skills Development Act, 1998, provides for the financing of skills development by means of a levy-financing scheme and a National Skills Fund.

The Skills Development Act, 1998, makes the Sector Education and Training Authority responsible to manage and promote education and training within a sector. This includes approving skills plans, disbursing monies for training, ensuring quality, promoting leadership and offering advice to companies.

The Skills Development Levies Act applies to all construction businesses except those businesses whose annual payroll is less than R500 000. Employers must register with the South African Revenue Services (SARS). When they register, employers must inform SARS that they belong to the Construction SETA, called the Construction Education and Training Authority (CETA).

Employers must pay 1% of their workers' pay to the skills development levy every month. The money goes to the CETA (80%) and the Skills Development Fund (20%) to pay for training.

See the Department of Labour's website - www.labour.gov.za

or the CETA's website - www.ceta.org.za for more information.

If an employee is earning a total wage of R3 000 per month, the amount payable to SARS per month is R30 (1% of R3 000).

The levy may not be deducted from the worker's pay. Employers must pay the levy to the South African Revenue Services (SARS) by the 7th day of each month. Employers who do not pay will have to pay interest on the money they owe and may also have to pay a penalty.

Skills programmes involve training that:

- Is based on a job.
- Counts as credits towards a registered qualification.
- Uses accredited training providers.

Any employer who develops a workplace skills programme can apply for grants from a SETA (such as the CETA) or subsidies from the Department of Labour (see www.ceta.org.za).

Compensation for occupational injuries and diseases

Government has established a fund to compensate casual and full-time workers who, as a result of a workplace accident or work-related disease become ill, are injured, disabled, or killed. Workers who are **injured on duty** can **claim compensation** for temporary or permanent disablement. If workers die as a result of an injury on duty, their dependants can claim compensation.

Workers who are temporarily or partially disabled receive 75% of their pay from the date of the accident or disease diagnosis until their condition is stabilised or they are fit to go back to work. Employers must pay compensation for three months from the accident or diagnosis date and then claim these payments back from the Compensation Fund.

Compensation is payable for any impairment of function, loss of limb or any permanent defect as a result of the injury or disease. Depending on the degree of disablement, compensation may take the form of lump sum or monthly pension payments.

Employers are protected against civil claims if a worker is injured on duty. The Fund also covers the cost of transporting workers to a hospital or doctor and medical aid expenses for a period of up to two years, and in certain circumstances for longer periods.

The Fund does not cover workers who are totally or partially disabled for less than three days. It also does not cover any worker guilty of wilful misconduct, unless they are seriously disabled or killed.

Anyone who employs one or more workers must register with the Compensation Fund and pay annual assessment fees. A separate registration is necessary for each separate branch of a business, unless an arrangement for combined registration has been made.

Before 31 March each year, all employers (including contractors) must submit a statement of earnings paid to all their workers from the beginning of March the previous year to the end of February. The annual assessment fee is calculated on workers' earnings and an assessment tariff based on the risks associated with the type of work being done. Employers fall into one of over a hundred subclasses, each with its own assessment tariff.

Assessment fee = total workers' pay ÷ 100 x assessment tariff.

Occupational injuries are injuries sustained by workers in the workplace or while performing any activities related to the business of the employer.

An occupational disease is a disease caused by a worker's job.

The Federated Employers' Mutual Assurance Company Limited (FEM) was established as a mutual insurer in 1936 and on the introduction of the Workmen's Compensation Act 1941 was granted a licence to continue to transact workmen's compensation insurance for the building industry.

Its business operations are essentially confined to the insurance of employers against their liabilities under the Compensation for Occupational Injuries and Diseases Act 1993.

FEM is a licensed compensation insurer. Construction businesses, instead of paying contributions to the Compensation Fund, may take out insurance with FEM (Tel. 011-359-4300). The assessment rates are the same as those applied by the Compensation Commissioner. No-claim bonuses are paid out.

FEM has regional offices in major centres.

The assessment tariff varies between the different sectors and sub-sectors of industry; for example, the 2006 tariffs were as follows:

• All building operations.	2,20
• Any tunneling, rock drilling and/or blasting.	8,26
• Operations of civil engineers.	2,42

If the total of all workers' pay is R1 000 000 and an assessment tariff of 2,2 applies, then the amount due to the Compensation Fund is R22 000.

Workers, or someone on their behalf, must immediately report an accident and any injuries, verbally or in writing, to the employer. If a worker does not report an injury to his employer, the Commissioner or mutual association within 12 months of being injured, he will lose any right to benefits. All employers must report any accidents that result in medical expenses and/or a worker's absence from work for longer than three days by submitting the required documents to the Compensation Fund within seven days. Employers who delay in reporting an accident are guilty of a criminal offence and will have to pay a penalty.

A worker, or someone on his behalf, must report in writing to the employer as soon as possible after a doctor's diagnosis if he has contracted a disease. If a worker does not report a disease to his employer, the Commissioner or mutual association within 12 months of being diagnosed, he will lose any right to benefits. Employers must fill in the required forms and submit them to the Compensation Commissioner within 14 days.

Taxes

Section 1.4 addresses the issues related to Value Added Tax, Company Tax and Employees Tax.

Safety on site

Section 3.8 address the issues related to safety on site.

Basic conditions of employment

The Basic Conditions of Employment Act, 1997, give effect to the right to fair labour practices referred to in section 23(1) of the Constitution by establishing and making provision for the regulation of basic conditions of employment.

In order to assist employers and employees to determine what is fair, government has set standards that are determined by them to be fair. These standards are described in what is known as the Basic Conditions of Employment Act.

The Basic Conditions of Employment Act applies to all employers and workers and regulates employment conditions such as leave, working hours (ordinary time and overtime, Sundays and public holidays), employment contracts, employee records, deductions, payslips, overtime, and termination. In addition to the Basic Conditions of Employment Act, the Department of Labour has also issued Sectoral Determinations which set employment conditions for vulnerable sectors of the workforce. Special conditions of employment are applicable to employers and workers in the civil engineering sector.

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The Basic Conditions of Employment Act requires that:

- Workers get a minimum of 21 consecutive days of annual leave each year. Employers can only pay workers instead of granting annual leave when employment is terminated. A public holiday cannot be counted as annual leave.
- Pregnant women may take four months of maternity leave, starting one month before their due date.
- Employers give workers details of their employment in writing at the start of employment including the employer's full name and address, the worker's name, occupation or a brief description of the work, place/s of work, date of employment, working hours and days of work, salary or wage or the rate and method of calculating wages, rate for overtime, any other cash payments, any payments in kind and their value, frequency of payment, any deductions, any leave to which the worker is entitled, period of notice required for termination, or period of contract.
- Certain procedures must be followed when either an employer or worker wishes to terminate employment.
- Each time workers are paid, employers must give them a payslip containing the employer's name and address, the worker's name and occupation, the period for which payment is made, total salary or wages, any deductions, the actual amount paid, if relevant to the calculation of pay, the employee's pay and overtime rates, number of ordinary and overtime hours worked, number of hours worked on a Sunday or public holiday, and the total number of ordinary and overtime hours worked in the period of averaging, if a collective agreement to average working time has been concluded.
- Workers may take the number of days they would normally work in a six-week period for sick leave on full pay in a three-year period. Employers may insist on proof of illness before paying a worker for sick leave.
- An employer may not require or permit an employee to work more than 45 hours per week and nine hours in any day for an employee who works five days or less per week, or eight hours in any day for an employee who works more than five days a week.
- Workers may agree, in writing, to work up to 12 hours a day without getting overtime pay. However, these workers may not work more than 45 ordinary hours a week, 10 hours' overtime a week and five days a week.
- A collective agreement may allow for working hours to be averaged over a period of up to four months. However, workers may not work more than an average of 45 hours a week and an average of five hours overtime a week.
- Workers must have a meal break of 60 minutes after five hours' work. A written agreement may reduce meal intervals to 30 minutes or eliminate meal intervals for workers who work less than six hours a day.
- Workers must have a rest period of 12 hours each day and 36 consecutive hours each week (must include Sunday, unless otherwise agreed).
- Workers working between 18:00 and 06:00 must get an allowance or work reduced hours, and have transport available to them.
- Workers may not work more than 10 hours' overtime a week, (unless by agreement - collective agreement may increase this to 15 hours per week for up to two months a year) and more than 12 hours on any day. Workers must get 1,5 times their normal hourly pay or paid time off in exchange for overtime.
- Workers my take up to three days of paid leave a year to attend to certain family responsibilities.

See the Department of Labour's website - www.labour.gov.za for more details.

Sections of the Act that relate to working hours do not apply to:

- Workers in senior management.
- Sales staff that travel and regulate their own working hours.
- Workers who work less than 24 hours in a month.
- Workers who earn more than R115 572 per year.
- Workers engaged in emergency work.

Employers who employ five or more workers must:

- Provide workers with the following documents:
  - Written particulars of employment.
  - A payslip each time they are paid.
- Maintain an employee record for each worker.
- Display a summary of the Basic Conditions of Employment Act in the workplace.

- Employers may only deduct money from a worker's pay if the worker agrees or if they are required to do so.
- Workers must get paid time off for public holidays, but if they agree to work, they must be paid double their normal daily wage.
- Workers must be paid a higher wage or receive paid time off in exchange for working on a Sunday.
- Employers must maintain a record of certain information for each worker. These records must be kept for three years after termination.
- In the interest of protecting children, employing anyone under the age of 15 is illegal, except for children in the performing arts. Children aged 15 to 18 may not be employed to do inappropriate work.

Employers may offer employees wages and conditions more favourable than the minimum but not less than the minimum.

A sectoral determination issued in terms of the Act for the civil engineering sector establishes minimum wages for workers which vary according to their task grade, occupational group or geographic regions.

All employers must in terms of the law:

- Set working hours in line with labour laws.
- Follow the law with regard to overtime, public holidays and working on Sundays.
- Give workers annual leave, sick leave, maternity leave and family responsibility leave.
- Only make deductions from a worker's pay allowed for by law.
- Provide workers with written particulars of employment.
- Terminate the employment contract appropriately.

Employers who reduce staff may be liable for retrenchment pay. As a guide, workers are paid the equivalent of one week's pay for each year worked. One way of overcoming retrenchment payments is to appoint workers for a specified period.

Labour relations

The Labour Relations Act, 1995, governs labour relations.

Every employee has the right:

- To participate in forming a trade union or federation of trade unions.
- To join a trade union, subject to its lawful activities.

The Labour Relations Act, 1995, applies to all construction businesses, workers, trade unions and employers' organisations. Trade unions and employers' organisations may form bargaining councils. Bargaining councils deal with collective agreements (a written agreement on workers' terms and conditions of employment, or any matter of mutual interest), solve labour disputes, establish various schemes and make proposals on labour policies and laws.

A number of regional bargaining councils have been established for the building industry. These councils establish minimum wages.

This law also provides that every employee has the right not to be unfairly dismissed and subjected to unfair labour practices. Unfair dismissals can result in construction businesses paying compensation up to 24 months wages.

Registration as a home builder

The National Home Builders Registration Council (NHBRC) is a housing consumer protection body created in terms of the Housing Consumers' Protection Measures Act. The Council is mainly established to protect the interest of housing consumers and to regulate the home building industry.

Any construction business who builds a home is required by law to register with the NHBRC. Failure to register constitutes an offence and, on conviction, the home builder/developer is liable for a fine of up to R25 000 or a one-year prison term on each charge.

Registration requires an application fee of R750 plus R600 initial registration fee and an annual renewal fee of R600. To qualify for registration the home builder must have the required financial, technical, construction and managerial capacity which will be evaluated by the Council. A home builder may be registered provisionally or conditionally and the Council may limit the number of homes that may be enrolled. The status of the home builder is subject to review and change at any time. The registration of a homebuilder remains valid for one year.

Registered home builders are required to:

- Conclude a written agreement for the construction or sale of any new home, which sets out all the material terms including the financial obligations of the housing consumer.
- Enrol homes with the NHBRC at least 15 days before construction begins.
- Construct homes in accordance with the NHBRC's Home Building Manual.
- Respond promptly to complaints notified by the housing consumer or the NHBRC.
- Honour the following deemed warranties in relation to the home that is:
  - built in a workmanlike manner;
  - fit for habitation; and
  - built in accordance with the NHBRC Technical Requirements and the terms, plans and specifications of the agreement.
- Honour the post-occupation warranties to:
  - rectify any major structural defect caused by non-compliance with the NHBRC Technical Requirements notified to him within a period of not more than five years;
  - repair any roof leak attributable to the workmanship, design or material occurring and notified to him within a period of not more than one year; and
  - rectify any non-compliance with the terms, plans and specifications of the agreement or any deficiency related to design, workmanship or material occurring and notified to him within a period of not more than three months.

The NHBRC may suspend a home builder's registration or its rights to enrol a home where it has information that the home builder has failed to comply with the Act.

The Housing Consumers Protection Measures Act, 1998, provides for the protection of housing consumers.

The NHBRC has the right to carry out a technical evaluation of the home builder by means of:

- A technical interview to determine the ability of a home builder to comply with the guidelines set out in the Home Building Manual.
- Site visits or inspections to examine homes or other construction work already completed or under construction by the home builder.

The NHBRC may require personal sureties from partners, directors, members, shareholders and/or trustees if the construction business has limited capital, fixed assets or active trading history.

cidb Code of Conduct for all parties involved in Construction Procurement:

1. Behave equitably, honestly and transparently.
2. Discharge duties and obligations timeously and with integrity.
3. Comply with all applicable legislation and associated regulations.
4. Satisfy all relevant requirements established in procurement documents.
5. Avoid conflicts of interest.
6. Not maliciously or recklessly injure or attempt to injure the reputation of another party.

Registration with the Construction Industry Development Board

The Construction Industry Development Board Act of 2000 requires the cidb to establish a national register of contractors and prohibits the award of a construction works contract by a national or provincial government department, a municipality or a state-owned enterprise to an unregistered contractor (see www.cidb.org.za).

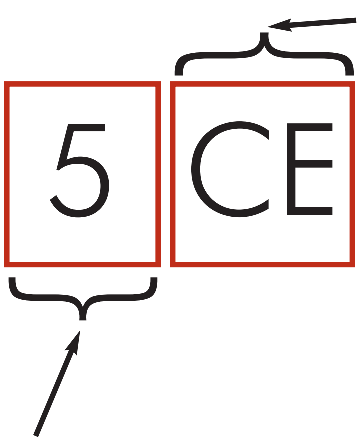
Only prime or main contractors must be registered. Subcontractors need not be registered. Labour-only contractors and those contractors who are provided with the bulk of the materials required for construction works by the employer or an agent of the employer need not to register. Once-off joint ventures do not have to register, provided that each partner of the joint venture is separately registered.

A contractor's grading designation is determined by the financial and works capability of the business. Financial capability relates to financial history (turnover), the highest value recently completed contracts and the amount of working capital that can be mustered to sustain a contract. Works capability is determined by the highest value of contract recently completed in a class of construction works, the number of professionals employed, and the fulfilment of relevant statutory requirements.

Newly established businesses are assessed on the amount of working capital that they can muster to sustain a contract. No financial or works capability requirements apply to the entry level, i.e. in contractor grading designation one.

The contractor's grading designation is used by government and provincial departments, municipalities and state owned enterprises to decide if a registered contracting business will be considered for a particular construction works contract. For example, a contracting business registered as a 5CE, will be considered for a civil engineering works contracts having a value not exceeding R6,5 million.

Describing contractor grading designations



Two letters depicting the **class of construction works** (general building, civil engineering, electrical engineering, mechanical engineering or specialist category) in which the contractor is registered.

Single number representing a registered contractor's capability to undertake a contract in a particular **class of construction works** within a specified **tender value range**

Tender Value Range Designation	Range of Tender Values	
	Greater than	Less than or equal to
1	R0	R200 000
2	R200 000	R650 000
3	R650 000	R2 000 000
4	R2 000 000	R4 000 000
5	R4 000 000	R6 500 000
6	R6 500 000	R13 000 000
7	R13 000 000	R40 000 000
8	R40 000 000	R130 000 000
9	R130 000 000	No Limit

Construction businesses may register for different classes of works. For example, a construction business may be registered as a 5CE and as an 8ME. This means that the business will also be considered for public sector mechanical engineering works contracts having a value not exceeding R130 million.

Construction businesses are required to abide by a code of conduct and are registered for a period of three years.

Section 1.6: Growing a construction business

The benefits of growing a construction business

Once a construction business has been established and is operating comfortably, the owner may decide that it is time to expand. A larger business can offer a wider range of services and can engage in more activities at the same time. If it is carefully controlled and managed, the larger turnover will also mean that there is a greater possibility of larger profits. However, the opposite is also true; a larger business that is poorly managed has a greater opportunity for making a loss.

Before a decision is made to grow the business, the reasons for needing to grow must be carefully understood, as well as the impact it may have on the opportunities that are currently available and may be available to the business in the future.

Larger businesses can leverage better prices and payment terms from suppliers as they have more buying power. This makes such businesses more competitive as they are able to offer lower prices. They also have more scope to make a bigger profit on existing projects since their costs are lower. Larger buyers can also demand faster delivery of goods.

When a contractor tenders for work, the client will always investigate the contractor's capability and capacity to do the work. Larger contractors have more options available to them, since they have a proven track record of successfully completing large projects. This is most visible in the contractor's grading designation on the cidb Register of Contractors.

With a larger business, there is a need to employ more staff, especially for administrative purposes. Once administrative systems have been established, then it is a good idea to employ other people to run and manage these systems. This will free up senior management to control and direct operations, giving better control of the business.

Larger businesses generally have:

- **More buying power.**
- **More work opportunities.**
- **More control.**
- **Employ more people.**
- **Enjoy more client confidence.**

Grow a business or expand it?

Growing a business means getting more work in the area where it currently operates. This could be a geographical area or a type of work. Typically construction businesses opt for obtaining more work in the same area that they currently operate, and grow to undertake more than one project of a similar nature, often in the same geographical area. Often contractors take on more work to ensure that they have continuity of work ensuring that their workers are occupied. Continuity of work is essential to maintain a sustainable business and the more frequently work is performed, the better, quicker and cheaper it can be done.

Expanding a business involves obtaining work in areas that are new to the business. This diversity of work is healthy and provides a diversity of skills within the business, making it more marketable to a variety of clients.

Experience is the key to determining which approach is most appropriate at a particular time. Many factors need to be taken into account when deciding to expand or grow, such as what the competition is doing and where the gaps are in the market. Experience forms the foundation from which a business can grow.

Growing a business means a bigger business in the current field.

Expanding a business delves into new areas.

Make sure that the benefits in growing the business outweigh the risks that are to be taken.

" No pain, no gain."

Growth: not always a good thing!

Advantages of growing a business include:

- Better buying power from suppliers.
- Better leverage with the banks and financial service providers.
- Better bargaining power for credit.
- Better access to projects.
- Better sustainability of work for employees.
- Better stability of the workforce due to more sustainable work.
- More opportunity to develop employee skills.
- Increased value of the business.

There are also disadvantages:

- Bigger expenses when running a larger business.
- Increased administration costs can erode profitability.
- More pressure to obtain work to sustain a larger workforce.
- More difficult to manage cash-flow requirements.
- The owner is no longer able to oversee all the work and must hire people he can trust to do this for him.
- There are more suppliers to pay and more clients who might not pay (or not pay on time).
- More financial support is needed.
- Banks will require more collateral for loans.

Don't try to grow a business if the risks are high.

If the business is doing well, carry on, but plan for contingencies.

If a business needs to grow, but the risks are high, leave and find employment elsewhere.

When to start growing a business

Very often a contractor will be satisfied with the way the business is going. There is enough work to keep the business going smoothly and there is a good profit coming in. The market is never static and what is good enough now will not be good enough in five or ten years' time.

Clients' circumstances change, and their construction budgets are re-allocated to other areas of the business, forcing the contractor to look for work elsewhere. The contractor's best staff might leave to work elsewhere for a higher wage or due to personal circumstances. Each of these examples will leave the static contractor in a very weak position if there is no forward planning. Often these circumstances can cause a business to close, and the owners being put back into the marketplace as employees.

Where to find opportunities for growth

One of the most important areas to find growth opportunities is in speaking to other contractors. Each contractor goes through different learning experiences on each contract and by sharing these experiences with others, both parties can benefit. Sometimes, it may even lead to a merger of two companies to the benefit of both companies.

A good place to meet other contractors is to become a member of a contractor's organization. Smaller contractors are typically based within a small geographical area, and where there is a lot of work, there will often be many smaller contractors operating. Community contractor organisations are a good place to start investigating what other contractors are doing, how they can help each other, and what their problems are. Often contractors find sub-contracting work through these types of organisations.

Targeting and planning for growth

A business does not grow by itself. In order to grow consistently, the company must have a target and a business plan on what needs to be done in order to achieve that target.

If there is no target, it will not be hit!

A construction business always needs to plan or map out where it is going. This allows changes to be made according to circumstances without a loss of focus.

Setting a target is the starting point. Targets can be set in terms of the company's turnover, the number of projects that are undertaken, the size of contracts that are taken on, the number of jobs created, and lastly, but most importantly, the profit that the company makes in a year. Each of these targets can be difficult to achieve, but by simply thinking of the targets and setting them, the first steps have been taken towards achieving them.

Drawing up a business plan to achieve growth is very similar to the process required when starting up a business. The difference between the two processes is that the startup business plan lacks the frame of reference of the business plan used to achieve growth. Decision making becomes easier once the company's approach to the business details and philosophy has been established, and the work methods and administration procedures have been set up. These can then be used as the baseline for improving and streamlining the business.

Driving the business plan

Monitor progress towards achieving the goals of the business plan. If the progress is not monitored the goals will not be achieved!

The business plan will not grow the business by itself. Once the business plan has been established, it has to be implemented, the progress monitored and the plan revised, as appropriate. It is important to take a step back to check the progress towards those targets at least once a month.

The environment in which the business operates changes continuously, making it necessary to adapt the business plan according to those changes. It is more important, though, to stay focused on the eventual outcome.

Options for growth

The business owner has several options that he can choose from. Each will make the business grow bigger; however, the different options have different outcomes. The business can grow by:

- Taking on progressively larger projects.
- Taking on more of the same size or smaller projects.
- Joining up with other contractors to undertake joint ventures.
- Contracting directly with the client instead of acting as subcontractors.
- Merging with other contractors to combine resources and capability immediately.

Each of these options has advantages and disadvantages that need to be carefully considered before they are undertaken.