

Solving for SMME's and Sole Proprietors

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SMALL BUSINESS AND ENTREPRENEURSHIP CRITICAL TO EMPLOYMENT AND ECONOMIC GROWTH

This colloquium was underscored by the message: “the right enabling environment is needed if small business is to realise its huge potential for transforming South Africa’s economy.” It closed with some resolutions to inform government’s policies on small business development. These resolutions included:

- > a call for government’s tendering and procurement procedures to be redrafted so small businesses could do business with the state and thereby play a greater role in the economy
- > amending the taxation and accounting rules for small businesses
- > urging SARS to improve communication with small businesses and offer a service matching that given to large business
- > intervention into the non-payment and late payment by government to small businesses
- > introducing entrepreneurship into the curriculum of schools, colleges and universities

Three years into the current government’s term of office, we take a look at developments in the world of small, medium and micro-sized enterprises (SMMEs) in South Africa.

Is government putting money where their mouth is?

One of the first signs that government was taking small business development seriously came in the 2015 national budget. Then-Minister of Finance Nhlanhla Nene announced that R3.5 billion would be spent on mentoring and training for small businesses by Minister Zulu’s department over the medium term.

Taxation of micro enterprises

The environment enabling small business development was further assisted by a reduction in taxation on micro businesses, proposed by the Davis Tax Committee as follows:

Table 1: Taxation of micro enterprises (2014 to 2015)

Turnover (R)	Rate of tax
0–150 000	0% of taxable turnover
150 001–300 000	1% of taxable turnover over R150 000
300 001–500 000	R1 500 + 2% of taxable turnover over R300 000
500 001–750 000	R5 500 + 4% of taxable turnover over R500 000
750 001+	R15 500 + 6% of taxable turnover over R750 000

Table 2: Taxation of micro enterprises (2015 to 2016)

Turnover (R)	Rate of tax
0–335 000	0% of taxable turnover
335 001–500 000	1% of taxable turnover over R335 000
500 001–750 000	R1 650 + 2% of taxable turnover over R500 000
750 001+	R6 650 + 3% of taxable turnover over R750 000

In effect, Minister Nene halved the taxation on micro enterprises with effect from the 2015/16 tax year. The two budgets that have followed the 2015 budget have maintained the taxation of micro enterprises at these rates.

Initiatives of the Department of Small Business Development

According to the website of the Department of Small Business Development (DSBD), its mandate is to “support the radical transformation of the economy through the promotion and development of sustainable and competitive entrepreneurs, small businesses and co-operatives, that contribute to job creation and economic growth”.

The DSBD’s key service offerings are:

1 The Black Business Supplier Development Programme

This programme offers a cost-sharing grant to black-owned small enterprises to help them improve their competitiveness and sustainability so they can become part of the mainstream economy and create employment.

It provides grant funding of up to R1 million for majority black-owned businesses, with 20% being allocated to training and development and 80% allocated to the acquisition of tools and machinery.

2 The Co-operative Incentive Scheme

The Co-operative Incentive Scheme (CIS) is a 100% grant for registered primary cooperatives with five or more members to improve their viability and competitiveness by lowering their cost of doing business. The incentive also supports broad-based economic empowerment, as it favours historically disadvantaged individuals (women, youth and people with disabilities).

3 The Shared Economic Infrastructure Facility

The Shared Economic Infrastructure Facility, managed by the Department of Trade and Industry, is offered on a 50/50 basis. This facility aims to leverage public sector investment to provide infrastructure for businesses, mostly in townships, rural areas and inner cities where economic activity is taking place. The Department of Trade and Industry funding is limited to R5 million and applicants are municipalities, municipal entities and provincial government entities. Although the direct beneficiaries of this programme are not small businesses themselves, the programme aims to create an environment in which small businesses can operate, trade and grow.

4 National Informal Business Upliftment Strategy

The National Informal Business Upliftment Strategy (NIBUS) is driven by the DSBD to address the development of SMMEs, particularly at the lower end. The DSBD has identified five priorities in its strategy:

- > retail
- > manufacturing
- > services
- > agriculture
- > construction and maintenance

Five strategic pillars govern the kind of support given to entrepreneurs:

- > **Strategic Pillar One:** Creating an enabling legal and regulatory environment
- > **Strategic Pillar Two:** Upliftment through enterprise development
- > **Strategic Pillar Three:** Facilitate intergovernmental relations for delivery
- > **Strategic Pillar Four:** Partnership and stakeholder management, for example through business and civil society associations
- > **Strategic Pillar Five:** Empowerment through information (knowledge) management The DSBD reported that it trained 1 037 informal traders during the 2015/16 financial year. It also established five centres for entrepreneurship at technical and vocational educational training colleges with the aim of developing entrepreneurs and small business owners.

In addition to its key programmes, the DSBD is supported by its two agencies, the Small Enterprise Finance Agency and the Small Enterprise Development Agency.

The role of SARS

The role of the South African Revenue Service (SARS) in the life of a small business cannot be over-emphasised, particularly as the business grows or attempts to grow. In conjunction with reducing taxation on micro enterprises, SARS introduced a number of guides on its website to assist owners of businesses to understand taxation for businesses. More importantly, the SARS eFiling system was made available to business owners so they can file their own tax returns. The benefits to small businesses include a reduction in accounting costs and valuable operating time. One area in which government has not stood out in assisting small businesses is in paying its creditors. Then-Minister of Finance Pravin Gordhan bemoaned the slow rate of payment by state departments in his budget speech of 2017, insisting that creditors be paid within 30 days of invoice.

An enabling environment, what more?

It would seem that government has made significant advances in improving the environment in which small businesses operate since 2014:

- > Tax has been reduced significantly.
- > Training has been provided in some areas.
- > Infrastructure is being developed.
- > Financing is made available from various sources.
- > SARS has reduced the administrative burden.

In her 2014 speech to the Industrial Development Corporation (IDC), Minister Zulu said, “Our country has yet to see the true value and benefits of SMMEs.” After three years of improving the environment in which SMMEs operate, one wonders whether some of the value and benefits have started to emerge. More importantly, whether the vision of the National Development Plan – that 90% of new employment will be created by SMMEs by 2030 – is realistic.

According to Statistics South Africa, the South African economy grew by approximately 8% in real terms between March 2014 and December 2016 (or 2.8% a year). Unemployment in the first quarter of 2017 stood at 27.7% compared to 25.2% in the first quarter of 2014. The key indicators suggest that despite efforts to create an environment in which SMMEs would create jobs and contribute to economic growth, this has not happened. In fact, research conducted by Professor Christian Friedrich of the University of the Western Cape (UWC) and his team revealed that 70% to 80% of small businesses fail within five years¹.

Friedrich also noted that only 1% of small businesses that started with fewer than five employees grew beyond 10 employees. This means not only that these businesses never meaningfully contribute to the tax base but also, more importantly, that the National Development Plan’s (NDP’s) goal of job creation by SMMEs is not being realised.

What can be done to help entrepreneurs?

Skills development

The DSBD has done and is doing extensive work to development entrepreneurial skills at Technical and Vocational Education and Training (TVET) colleges. These programmes are in their infancy and their results are yet to be seen. Are they enough and should they be extended to other institutions of higher learning, such as universities? Otherwise we run the risk of demoting entrepreneurship and small business ownership to second-rate status.

The research done by Friedrich and his colleagues found that one of the largest factors which contribute to the success of a small business is the business owner themselves. Traits such as being a self-starter, being proactive and being persistent were indicators of success. Friedrich writes that “other factors found in our research strongly influencing success of smallscale entrepreneurs were innovativeness, learning orientation, achievement orientation. Furthermore, planning strategies, including goal setting, have a high and positive correlation to success”. In response, Friedrich and his colleagues developed a three-day training programme for entrepreneurs. This programme focuses on the different skill sets they believe are necessary for entrepreneurs to succeed in South Africa:

- > personal initiative
- > how to be proactive
- > how to actively set and implement goals for one’s business and plan with a longterm focus
- > being innovative
- > generating and implementing new ideas

According to research conducted by UWC, participants in the programme saw an increase in turnover and profitability while being able to employ more staff than a control group that did not attend the programme.

Skills acquisition

The development stage of an SMME may also be a guide for the help offered to the entrepreneur. As businesses grow there is a need to attract and retain skills and staff. Small businesses will compete with large businesses for talent and will need more than just the skills of the owner. According to Old Mutual’s SME Employee Benefits Monitor 2017, 65% of small business owners and 70% of staff employed by SMMEs believe that the employee benefits offered by a company affect employees’ decisions to work for the company or not. More importantly, 71% of small business owners believe they are unable to offer the same benefits that large companies offer.

With advances in financial solutions such as umbrella funds and medical aids, it’s not clear whether this is only a perception or if a gap really does exist in the employee benefits market. However, when one considers that in an SMME the decision on what benefits to offer is most often left to the owner, financial manager and HR manager (if these are employed), it’s understandable that they may not have full knowledge of what is required for their employees. The financial services sector needs to assist with transparent and easy-to-understand products that are friendlier to SMMEs.

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A safety net to encourage entrepreneurship

With the failure rate of small businesses as high as it is, one wonders whether more needs to be done to provide a safety net to encourage entrepreneurship. For most business owners, retirement annuities present their only form of retirement savings, as most pension and provident funds do not cater for employers with fewer than five employees. Retirement annuities do not provide a safety net for business owners should their businesses fail, as these savings are available only in the form of an annuity on retirement.

It is debatable whether retirement savings should be used for this purpose anyway. In fact, the Income Tax Act frowns upon the use of retirement savings other than for the said purpose of providing an income in retirement. This then leaves a void in the provision of a safety net for aspiring entrepreneurs and small business owners.

Small business ownership and retirement

Having said this, very few retirees are likely to retire with more than 75% of their pre-retirement income. Small business ownership presents retirees with the possibility of a second career and an opportunity to earn an income after retirement. Retirees may bring their own capital, experience and will to succeed, but the same risks and challenges await them. The need for a safety net is even greater than for those who may have more time to recover from business failure.

The DSBD has a number of structured programmes, as do a number of private sector organisations, which guide small business owners in setting up their operations. When these programmes are combined with personal traits such as tenacity and self-belief, retirees can become successful small business owners.

Current retirement legislation provides tax incentives for retirees only when annuities are purchased after retirement. Alternative models such as structured small business ownership could be considered by Treasury. If successful, these small businesses could address gaps in the post-retirement income model and gaps in the job creation market, and stimulate GDP growth as envisioned in the NDP.

More attention needs to be given to providing a safety net for all small business owners to encourage entrepreneurship at any age.

References¹

1 Friedrich C. 2016. *Why do 70% to 80% of small businesses fail within five years?* <https://www.moneyweb.co.za/mybusiness/why-do-70-to-80-of-small-businesses-fail-within-five-years/>.

SMME'S

ENTREPRENEURSHIP

SMALL BUSINESS DEVELOPMENT