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On The Cover

Crippled by compliance

Author: Brian Bakker

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SA companies are overburdened by the cost of compliance. On top of this they worry about a vast body of laws and regulations. It's time to take stock

SBP, a South African section 21 not-for-profit company, earlier this year unveiled the results of its study on the cost of regulatory compliance in SA. Entitled "Counting the cost of red tape", the report finds that it cost SA businesses R79 billion in 2004, equivalent to 6.5% of GDP.

Simon Dagut, SBP research manager, says the study involved well over 1 000 local firms. "If anything, [R79 billion] is probably an underestimation," he says.

Mark Walker, director of BMI-TechKnowledge (BMI-T), puts these figures in perspective: "There's a direct correlation between the cost and speed of setting up a business and the success, as economic entity, [of the country in which it operates]."

This is confirmed by an annual World Bank report, entitled: "Doing Business in 2005: Removing Obstacles to Growth". Researchers found that Slovakia and Colombia were the most successful investment climate reformers over the past year: creating electronic one-stop shops for new businesses, shrinking regulatory delays by weeks, improving credit registries and increasing the flexibility of labour laws.

The World Bank found that reform took place mainly in countries that faced competition and had incentives to measure regulatory burdens. In the enlarged European Union, accession countries reformed in anticipation of new competitive pressures on businesses; and existing members reformed to maintain their advantage.

How does SA stack up against these countries?

SBP's Dagut: "There's no dispute that well-established firms in SA's first economy operate in a reasonably well-run regulatory environment, compared to many other middle-income countries," he says.

"But the survey revealed two other important facts. First, while it may be quite efficient for big companies, it is also very expensive. R79 billion is a great deal of money, a lot of which could be spent in far more productive ways than complying. Second, the regulatory system looks very different from the perspective of small and informal firms, which often face crippling high costs," adds Dagut.

"As the World Bank emphasises, there's no room for complacency," he notes. "We're dealing with a huge accumulated pile of regulation, much of which was inherited, but nobody has done a regulatory impact assessment of the local market."

Dirty Sox

Adding more fuel to the slow-burning fire of discomfort is an AMR Research study: "Spending in the Age of Compliance, 2005", which finds that companies will spend nearly \$15.5bn on compliance-related activities this year (a portion of which will go to the Sarbanes-Oxley Act (Sox)).

AMR stresses that Sox is but one of a myriad compliance requirements that companies face across the globe (see chart below). Walker is succinct on the reasons for Sox being on top of the list: "That's where they see they're going to get burnt first."



Simon Dagut

Mike Davis, senior research analyst with the Butler Group, notes: "Compliance requires adherence to the raft of legislation, regulation and standards that are applied to organisations of all complexions. Adherence requires that organisations record, store and be able to retrieve information securely and efficiently as required," he says.

Davis believes it is critical to not only have an appreciation of the relevance of compliance issues to the organisation but to develop a strategy for addressing them in a manner that adds value to the business. "Compliance is not a 'fire and forget' issue. Compliance is now a firm part of the business environment and organisations, whatever their type, must recognise not only the challenges but also the opportunities compliance presents; to the organisation and to the IT function in particular," he adds.

While little of this regulation is of direct relevance to SA companies, it does have indirect consequences. BMI-T's Walker illustrates the regulatory burden faced by an unnamed multinational: "I was speaking to the head of marketing for Africa and she said 50% of their marketing energy is now being wasted on compliance and similar issues," he says.

In real terms, Walker acknowledges that most problems now faced by his marketing acquaintance are a result of Sox - which he describes as an intelligence gathering exercise. "If you're an American shareholder or investor, you now have transparency right down the chain," he notes.

The impact of this locally is that previously a marketing budget was allocated by head office and dispensed to SA. The local operation then used this at its own discretion in a wide variety of marketing activities with little or no accountability for anything other than sales figures.

Walker again: "This was both a good thing and a bad thing. The good part was you could run local events, commission market research or run advertising campaigns, for instance. The bad side is you could use that marketing budget to bribe somebody; or use it as a slush fund," he says.

Another factor raised by AMR Research is that a large chunk of the anticipated \$15.5bn will be spent on technology - good news for some readers. Across the raft of US regulations, AMR expects 34% to be spent on technology, 24% on services, 40% on human resources and 2% in other areas.

Butler's Davis notes that most IT vendors are reacting to the hype by packing the compliance label on their products in order to sell them. "The compliance agenda has come along at just the right time and it's a must do," he says.

He recounts a tale involving a large American organisation that shall likewise remain nameless: "They called their lawyers in for something and one of them turned around and said compliance is like Y2K, except there's no end-date."

Davis is quite illuminating on the subject of the cost of compliance when he asks a rhetorical question: "What is the cost of non-compliance?"

Talk about the devil and the deep blue sea ...

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