



Rationalisation of Gambling and Liquor Boards (NC)

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1. Background & Introduction

Public entities undoubtedly play an important economic role in pursuit of development objectives. This is because of the targeted approach they contribute towards job creation, economic infrastructure and economic growth, logically based on their respective mandates. Provincial Public entities were created as an extension of government, with the mandate to fulfil a specific economic or social responsibility of government and fall within Schedule 3C¹ of the Public Finance Management Act.

There may be variances between terms of establishment, the purpose and mandate for creation of public entities (provincial in this case) brought about amongst others, by changes in economic environment, global economy, technology as well as socio-economic and political imperatives. Despite such changes, government must ensure that public entities remain centrally coordinated, with shared vision and comprehensively aligned with policies and government led processes. One such method, is a phenomenon called Rationalisation of Entities.

Rationalisation of entities means reorganisation of entities to increase their efficiency. Reorganisation may lead to expansion (mergers or acquisitions) or reduction in size, a change in policy or alteration of strategies. One of the recommendations of the Presidential Committee on State Owned Entities, is that mandates of entities should be subject to critical strategic review every five years. In addition, the current fiscal space necessitates reforms and methods to ensure public entities are not merely a funding burden to government.

In a strategic session held by the Department of Economic Development and Tourism (DEDaT), a decision was taken for Programme 4 (**Business Regulation and Governance**) to investigate the possible rationalisation of Northern Cape Gambling Board (NCGB) and the Northern Cape Liquor Board (NCLB) entities. The implications are that liquor, gambling and betting regulation are important functions of the department and whether the current model(s) of performing these functions are optimal or if there are more effective and efficient ways of performing those functions warrants assessment.

¹ Rely on government funding and public money, either by means of a transfer from the Revenue Fund or through statutory money. these Provincial Public entities have the least autonomy as compared to those that fall under Schedule 1, 2, 3B and 3D, (National Treasury, 2013).

The exercise would investigate overall contribution or value added by these entities to overall promotion of economic development and industry regulation towards socially responsible gambling and liquor consumption. The main elements the investigation needed to cover include research work on the best model for rationalisation of these entities, a financial due diligence, a legal and tax due diligence as well as commercial due diligence.

A task team was subsequently established to cover the investigation areas. The Research and Development (R&D) subprogramme was tasked with researching the rationalisation models drawing lessons from the Free State and Gauteng provinces. This report discusses the findings specifically on the scope of work that was assigned to R&D, research work on models, areas of focus and benefits of rationalisation of entities.

2. Methodology

Both primary and secondary research methods were used to investigate rationalisation of entities and possible methods. A questionnaire was designed for telephonic surveys with the Chief Executive Officers managing the two entities nation-wide. The questionnaire covered questions on the rationalisation model used, advantages and disadvantages of the merger (lessons learnt).

Although all provinces were interviewed, only Free State has actually merged the two entities, and therefore offered valuable responses in to the exercise. Gauteng, on the other hand, has taken a different approach to rationalisation of entities. Gauteng Provincial Government contemplates having one regulative agency that would oversee all provincial entities, and not only the Liquor and Gambling Boards. And this process is unfolding still and therefore responses were provided based on the milestones in the process.

3. Rationalisation Models

Literature reviewed mentions two traditional approaches to rationalisation (simplification) of entities, which is **dormant first** and **outside-in** approaches. It is indicated that entities can choose either or a combination the two approaches. A third approach has since evolved, called the Straw man approach.

3.1 Dormant First

This approach is mostly used to assess whether an entity is dormant or not. Rationalisation processes recognise that the dormant entities are easier to eliminate and hence focus is directed there first. The advantage of the dormant model is that it often possibly affords a quick start and progress is certain. Progress in the dormant approach is often measured by the number of entities detached or discontinued.

Amongst others, the real need that rationalisation of entities is supposed to address is excess cost and risk. The primary drawback of the dormant approach is that it possibly allows for very small savings, safe to conclude it misses addressing this need.

3.2 Outside- In

The Outside-in is also known as the trial and error approach. The approach attempts to decide, on a one-off basis whether entities are a good fit for combination. The advantage with the approach is that it affords the reduction of excess costs and risks associated with complexity. The only challenge is that the rationalisation process can be slow, thus creating a host of challenges.

3.3 The Straw Man Approach

Under this approach, the existing legal entity structure is ignored, at least in the beginning stage. The process begins by developing a structure, called a straw man structure, an initial starting point for the process or discussion. As the process progresses, it is established if the entities simply cannot be combined due to existing legal liabilities, regulatory constraints, labour issues and so on.

There are distinct advantages of the straw man approach. Firstly, straw man approach focuses on the actual goal it drives and provides clarity. Thereby making it is easier to get support from supporting constituencies, such as legal, regulatory, human resources, accounting, information technology, and finance and so on.

Secondly, the approach tends to result in structures that are much closely aligned to entity operations. Structures that are aligned to operations are

cheaper to explain to executives and employees. This is especially important for the implementation stage. Also, aligned structures are more likely to be respected going forward. Thirdly, the change in the entity or entities can make a significant impact.

In the main all approaches to rationalisation (simplification) of entities have costs and disruptions associated with them, but the benefits are often significant. Use of the straw man approach in particular, often affords entities to achieve benefits more quickly and in measurably larger amounts than the traditional approaches.

4. Potential Benefits and Focus Areas

Literature reviewed clearly points out the potential benefits of rationalisation and areas of focus in the process. The key benefits of rationalisation are cited as increase in operational efficiency, improved strategic agility and reduction in costs. Table 1 below outlines benefits and focus areas as follows

Potential Benefits		Areas of focus
Operational synergies	Rationalization can result in synergies through entity-specific operational integration and thoughtful placement of each target entity's human capital, assets and operations	Focus on: <ul style="list-style-type: none"> ▪ People — rationalized responsibilities ▪ Process — streamlined to help increase efficiency, revenue and cost savings ▪ Technology — common set of applications, simplified accounting codes and reporting and consolidated maintenance and management of entities ▪ Third parties — consolidated contracts, volume discounts, simplified vendor feeds, and reduced contract management support.
Cost avoidance	Avoid plugging entities to be eliminated into performance improvement agendas,	<ul style="list-style-type: none"> ▪ Identify entities to be maintained versus those to be eliminated early in the process, so clients can build business performance initiatives on

	e.g., global finance transformation, accounting and business systems, cash management, etc.	top of a streamlined structure
Structural alignment	<p>Opportunity to concurrently:</p> <ul style="list-style-type: none"> ▪ Better take advantage of changing market conditions and customer needs ▪ Understand new, emerging markets, product portfolios and address customer needs. 	<ul style="list-style-type: none"> ▪ Assess business strategy, analyse core/new markets, review competition and help align legal entities with changing industry conditions ▪ Provide fresh thinking around how to structure the realigned organization to take advantage of market opportunities and operate effectively.
Governance and control	<ul style="list-style-type: none"> ▪ Increased transparency ▪ Better management of legal entity populations ▪ Risk architecture that distinguishes high-risk entities from low-risk entities 	<ul style="list-style-type: none"> ▪ Focus on population management — recommendations for legal entity procedures, manuals and committees designed to meet organizational objectives ▪ Recommend risk architecture and tiering, as well as efficient control framework to help save costs and resources

4.1 Potential cost benefits

From a cost reduction standpoint, rationalisation ensures savings in both support and operations sides of the entities. Table 2 below, provides some of the more common savings by functional areas:

Function	Potential sample savings
Legal and regulatory	<ul style="list-style-type: none"> • Reducing fees and costs relating to redundant minimum taxes, licensing,

Finance and treasury	<p>permitting, registration, registered agent, public notices filing, record maintenance, tax compliance and other filing.</p> <ul style="list-style-type: none"> • Reduction in bank account service fees, transaction charges, capital costs associated with minimum deposit requirements, debt covenant compliance, and cash forecasting.
Accounting	<ul style="list-style-type: none"> • Reduction in fees and costs relating to statutory audit, redundant and inefficient shared services resources, monthly/quarterly/annual reporting, intercompany accounting (e.g., streamlining voluminous intercompany journal entries and reconciliations) and IFRS implementation.
Operations	<ul style="list-style-type: none"> • Reduction in external spend through vendor rationalization. • Reduction in costs that resulted from duplicative administrative/shared services, misaligned operating model, duplicative insurance policies/premiums, and intercompany accounting. • Reduction in lost sales/revenue resulting from artificial barriers to doing business.
Information technology	<ul style="list-style-type: none"> • Reduction in costs relating to general ledger input/coding, system configuration, incremental system capacity.
Human resources	<ul style="list-style-type: none"> • Reduction in costs relating to administrative and shared services, insurance/premium, vendor rationalization, and redundant compensation and benefits programs. • Managing loss of employee mobility.

5. TELEPHONIC SURVEY FINDINGS

5.1 Free State²

Free State is currently the only province³ to have merged the two Entities. The process commenced during the 2008/09 fiscal year wherein the Free State Liquor Board, as constituted by the Free State Liquor Act 3 of 2007, was de-established and its functions absorbed in terms of the Free State Gambling and Liquor Authority Act 6 of 2010 [the FSGLAA] which commenced on the 11th of June 2010. In terms of the FSGLAA the Liquor Board and Gambling Authority entities were amalgamated.

Posed with the question on why the merger?

Amongst other reasons, the province cites three paramount reasons for the merger of the two entities. Firstly, to ensure reasonable and sound regulation of the two entities. Secondly, to ensure sound and prudent public finance management. Thirdly, to lessen the bureaucratic upheavals thus offering a one-stop shop for Businesses aiming to participate in the Liquor and Gambling space. Important to note that the Free State Provincial Government and the entity could not provide a mapping process in terms of how it went about merging the two entities.

Posed with the question on what were the challenges of the process?

The Free State respondent indicated that merging process was not without hiccups. Key challenge was the **organizational reengineering process**, each entity had its own organogram whilst merging implied infusing these to one organogram. The complexities around organograms led to civil litigation against the merged Free State Gambling and Liquor Authority and the MEC: Free State Department of Economic Development and Tourism (see; Free State High Court, Bloemfontein Republic of South Africa; Case number: 2023/2012).

Funding requirements as well as **consensual agreements** between parties involved in the merger were also cited as challenges in the merging of the two entities.

Posed with the question on the actual benefits of the merger?

According to the respondent the benefits of the merger outweigh the challenges. Merging the two entities has **minimized the regulatory burden**. The merger has allowed for **centralization and management of activities** relating to interventions within the single entity. This relates to interventions that the single entity manages such as ensuring **appropriate licencing**

² The respondent did not refer or share any specific mapping process of model used in merging the entities.

³ This is based on the responses during the telephonic survey.

inspections for Gambling and Liquor industry in the Free State are coordinated as well as effective stakeholder management. The entity also has a **well-coordinated approach to clamping down on illegal gambling and liquor operators.** Another benefit related to **financial resource management, as there is no duplication of functions.**

5.2 Gauteng

Telephonic interviews conducted with the Gauteng respondent revealed that the provinces' merging model is completely different to that of Free State and perhaps the one envisaged by the Northern Cape. Gauteng Provincial Government contemplates having one regulative agency that would oversee all provincial entities, and not only the Liquor and Gambling Boards. The respondent indicated for crucial aspects towards its approach, namely, **Human resources, Legal Matters (Legalities of the merger), Financial and Fiscal resources and Accommodation.**

Whilst the province had not yet merged entities at the time of the interview, the respondent indicated that **the rational for merging stems from a significant supposition that entities would operate/function at an optimal level once merged.** The respondent further indicated that the merging process is rather tedious and requires caution processing/implementation.

5.3 Other Provinces

The six provinces, namely KwaZulu Natal, Eastern Cape, Western Cape, Mpumalanga, Limpopo and North West indicated that the two entities are currently operating independently. Whilst some of the respondents were open to the possibility merging the two entities, given their interdependence, the respondents unanimously felt the risks outweighed the possible benefits.

Respondents stated that merging the two has not been considered in their provinces, given that the two entities have differentiated mandates, and are currently operating optimally. Further, challenges facing the two entities were cited as another reason why merging these would not be ideal. In consideration of how tedious the process of merging the two entities would be, the general conclusion was that it does not make financial and business sense to merge the entities in the six provinces.

6. Conclusion

Research conducted shows the Straw Man Method as the most appropriate for possible consideration by the department in rationalisation of the Gambling Board and Liquor Authority entities. This is because of the potential benefits it provides as opposed to the Outside in approach. More

importantly, the Free State did not refer to any specific model that it followed in merging the two entities. The Outside Approach appears risky given the trial and error methods it employs, whilst the domain first is only relevant if either of the entities is considered obsolete.

Most important benefits of rationalisation include reduction in costs, increased operation efficiency and improved strategic agility. The areas of focus include amongst others, the legislation, human resources and finances. Caution on the process of merging the entities was pointed out as very crucial by both Free State and Gauteng respondents.

It must be noted that this report forms part of the investigation necessary prior the actual recommendations can be made on whether rationalisation of the Gambling Board and Liquor Authority entities ought to be considered or not. Necessarily, the rest of the task team must submit findings on the Financial Due Diligence, the Legal Due Diligence as well as the Commercial Due Diligence of the two entities from the respective members or subsections.