

PROVISIONAL REPORT OF THE PUBLIC PROTECTOR IN TERMS OF SECTION 182(1)(b) OF THE CONSTITUTION OF THE REPUBLIC OF SOUTH AFRICA, 1996 AND SECTION 8(1) OF THE PUBLIC PROTECTOR ACT, 1994



PUBLIC PROTECTOR
SOUTH AFRICA

"Lack of Oversight"

THIS REPORT IS CONFIDENTIAL AND IS MEANT FOR THE PARTIES TO WHOM IT IS SUBMITTED. THE REPORT MAY NOT IN ANY WAY BE DISSEMINATED OR PUBLISHED BY ANY OF THE PARTIES AND IS MEANT ONLY FOR THEIR COMMENTS IN TERMS OF SECTION 7(9) OF THE PUBLIC PROTECTOR ACT, 1994.

PROVISIONAL REPORT ON A SYSTEMIC INVESTIGATION INTO COMPLAINTS OF MALADMINISTRATION AGAINST THE FREE STATE DEPARTMENT OF AGRICULTURE IN RESPECT OF NON-ADHERENCE TO TREASURY PRESCRIPTS AND LACK OF FINANCIAL CONTROL IN THE ADMINISTRATION OF THE VREDE DAIRY PROJECT

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Executive Summary

- (i) *"Lack of Oversight"* is my provisional report as the Public Protector issued in terms of section 182(1)(b) of the Constitution of the Republic of South Africa, 1996, and section 8(1) of the Public Protector Act, 1994.
- (ii) The report communicates my intended findings and remedial action to be taken following an investigation into the alleged maladministration by the Free State Department of Agriculture and Rural Development in that it did not adhere to treasury prescripts in the administration of the Vrede Dairy Project and lack of financial control in the administration of the Vrede dairy project.
- (iii) The Complainant is Mr R Jankielsohn a member of the Free State Provincial Legislature representing the Democratic Alliance. Mr Jankielsohn submitted a complaint alleging maladministration after visiting the Vrede Dairy Farm and received answers to question posed in the Free State Legislature which was not satisfactorily answered according to the Complainant.
- (iv) In the main, the complaint was that: 1) An agreement between ESTINA/PARAS and the Department in respect of the Project are subject to a confidentiality clause which is contrary to good governance principles as public money funds the project. The Complainant alleges that the National Department of Agriculture invested R30 million (2012/2013) in the Project during the previous financial year and will invest R84 million in this financial year (2013/2014); 2) The Private Company will invest R228 million for a shareholding of 49% and Government will contribute R342 million for a shareholding of 51%, contrary to Treasury Prescripts in respect of Public Private Partnerships; 3) The Private Company contributes only 40% of the funds needed for a 49% share allocation which he alleges is irregular in terms of Treasury Prescripts; 4) That 400 pregnant cows were procured at inflated prices.

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- (v) On 28 March 2014 the Public Protector received a further complaint from the Complainant on the Vrede Dairy Project. The Complainant made the same allegations as the allegations received on 12 September 2013. In the main, the second complaint was: 1) That the prices for goods and services procured by the Private Company were inflated and queried specific alleged expenses in respect of construction, processing equipment, administration costs and the purchase price of cows; 2) That environmental requirements and legislation was not adhered to in the operation of the project; 3) That between 50 and 100 cattle has died since being purchased and request an investigation into the cause of the deaths of the cattle.
- (vi) On analysis of the complaint, the following issues were identified and investigated:
- (a) Whether or not the Treasury prescripts in respect of a Public Private Partnerships were adhered to and whether or not the contribution of 40% of the funds for an allocation of 49% of the shares in the company was contrary to Treasury prescripts;
 - (b) Whether or not the contents of the agreement between the Department and the Private Company were adhered to in that the Department implemented appropriated monitoring and management procedures in respect of financial, performance, budget evaluation and expenditure control;
 - (c) Whether or not the prices for goods and services procured were inflated and specific alleged expenses in respect of construction, processing equipment, procurement of cows and administration costs
 - (d) Whether or not environmental legislation was adhered to during the farming operations?
- (vii) The investigation process commenced with a formal investigation, conducted through meetings and interviews with Complainant and relevant officials of the Department as well as inspection of all relevant documents and analysis and application of all relevant laws, policies and related prescripts, followed.

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- (viii) Key laws and policies taken into account to help me determine if there had been maladministration by the Department were principally those imposing administrative standards that should have been upheld by the Department or its officials when implementing and managing the Vrede Dairy Project.
- (a) Whether or not the Treasury prescripts in respect of a Public Private Partnerships were adhered to and whether or not the contribution of 40% of the funds for an allocation of 49% of the shares in the company was contrary to Treasury prescripts
- (aa) The evidence provided by the Department in respect of the process followed to conclude the agreement with ESTINA supported the conclusion that the prescripts in respect of the procurement of the agreement was not adhered to. This was confirmed by the Accounting General's report dated January 2013 and constitutes maladministration
- (bb) The Accounting General informed the Public Protector that a report on the Vrede Dairy Project was drafted and submitted for comments during January 2013 to the Minister of Finance, the Free State Premier and the Member for the Executive Council: Free State Department of Agriculture and Rural Development. The accounting officer of the Department proceeded after the recommendation of the Accounting General to pay a further R143, 950 million to ESTINA in respect of the project. This amounted to gross irregularity and maladministration.
- (cc) The evidence discussed above, which includes failure to adhere to Treasury prescripts in respect of procurement and specifically the conclusion of a PPP leaves me with no option other than to conclude that the Department did not maintain a procurement system that is fair, equitable, transparent, competitive and cost effective as required by section 217 of the Constitution and Treasury regulations on SCM. It did not comply with the above basic supply chain management requirements, and thus rendered the conclusion of the agreement improper.

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- (dd) The conduct of the accounting officer in concluding the agreement amounts to improper conduct, abuse of power and maladministration. This was confirmed by the report of the Accounting General dated January 2014.
- (ee) The distribution of shares in the Agri-BEE company in relation to the monetary contributions required from the parties to the agreement is irregular and contrary to Treasury prescripts in respect of PPP agreements and this constitutes maladministration.
- (b) Whether or not the contents of the agreement between the Department and the Private Company were adhered to in that the Department implemented appropriated monitoring and management procedures in respect of financial, performance, budget evaluation and expenditure control
- (aa) No documents and/or policies or measures were provided by the Department that proper financial control and risk management of the project were in place. I could find no evidence or indication that the accounting officer invoked the provisions of the agreement in respect of the control over the project and this raises serious concern. This concern was supported by the report of the Accounting General and the lack of controls amounts to gross negligence and maladministration.
- (bb) No supporting evidence in the form of actual invoices/receipts was submitted to substantiate the expenditure as claimed in the financial statements submitted. In fact the payment vouchers for the disbursement of the R173, 950 million to ESTINA were substantiated only by the project proposal of ESTINA/PARAS and the agreement concluded between the Department and ESTINA.
- (cc) From the above it is clear that this amounts to gross negligence, maladministration and ultimately irregular expenditure in terms of Treasury prescripts.

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- (dd) In terms of the Regulations a PPP agreement does not divest the accounting officer of the responsibility for ensuring that the relevant institutional function is effectively and efficiently performed in the public interest. The evidence I have outlined earlier points to gross irregularities in ensuring the effective and efficient performance of the agreement and resulted in irregular and fruitless expenditure.
- (c) Whether or not the prices for goods and services procured were inflated and specific alleged expenses in respect of construction, processing equipment, procurement of cows and administration costs
- (aa) The independent evidence submitted indicates that the prices of the processing equipment and the cows were considerably higher than the current market prices. The evidence further confirms that the accounting officer of the Department had no measures in place to ensure proper procurement procedures in acquiring assets for the project.
- (bb) The evidence submitted by the Department is contradictory in that the MEC submitted that the additional 9% of shares allocated to ESTINA for the management and administration costs of the project. However from the analysis of the financial statements this could not be verified. This would only be determined through a proper accounting forensic investigation and audit.
- (cc) The lack of proper monitoring and control measures to ensure value for public money expended is the reason for the discrepancies and this amounts to gross negligence, maladministration and resulted in irregular and fruitless expenditure.
- (d) Whether or not environmental legislation was adhered to during the farming operations

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- (aa) The Department did submit the necessary environmental authorisations as required by legislation for the activities of the project on the farm Krynaauwslust and the allegation is not substantiated.
- (bb) The environmental incident during February 2014 on the farm Krynaauwslust was addressed by the Department of Water Affairs as required by legislation.
- (ix) The appropriate remedial action I am taking in pursuit of section 182(1)(c) of the Constitution, with the view of addressing systemic procurement management deficiencies in the Department and the irregular expenditure incurred, is the following:
- (a) The Premier of the Free State Province to:
- (aa) The Premier of the Free State Province ensures, in terms of Treasury Regulation 4.1.3, that the Executive Authority of the Department initiates an investigation into the conduct of the accounting officer of the Department.
- (bb) The Premier of the Free State Province ensures the findings of the Accounting General are noted and the recommendations as mentioned in his report of January 2013 are implemented.
- (b) The Member of the Executive Council for the Free State Department of Agriculture and Rural Development to:
- (aa) Initiate an investigation into the conduct of the accounting officer of the Department in terms of Treasury Regulation 4.1.3 with the view of taking disciplinary measures.
- (bb) Ensure that the findings of the Accounting General are noted and the recommendations as mentioned in his report of January 2013 are implemented.

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- (c) The Head of the Free State Department of Agriculture to:
- (aa) Improve the Supply Chain Management System of the Department to ensure that all Treasury legislation and other prescripts are adhered to
 - (bb) Ensure that the officials of the SCM Division and the members of Management of the Department are trained on the prescripts of the National and Provincial Treasuries in respect of procurement and specifically in respect of deviations.
 - (cc) Take corrective measures to prevent a recurrence of the failure in the Management process referred to in this report.
 - (dd) Ensure that all Departmental staff involved in the implementation and execution of projects are properly trained and capacitated to manage projects assigned to them.
 - (ee) Develop a policy for the implementation of internal control measures in line with Treasury Regulation Nr. 3.
- (d) The Head of the Special Investigating Unit to:
- (aa) Conduct a forensic investigation into serious maladministration in connection with the Vrede Dairy Integrated Project of the Free State Department of Agriculture, the improper conduct by officials of the Department and the unlawful appropriation or expenditure of public money or property with the view of the recovery of losses suffered by the State.
- (e) The Auditor-General of South Africa to:
- (aa) Commission a forensic and due diligence audit with a view to verify all the transfers and expenditure of public money in respect of the Vrede Dairy Integrated Project of the Free

State Department of Agriculture in order to determine whether or not value for money was received by the State.

CONFIDENTIAL PROVISIONAL REPORT

PROVISIONAL REPORT ON A SYSTEMIC INVESTIGATION INTO COMPLAINTS OF MALADMINISTRATION AGAINST THE FREE STATE DEPARTMENT OF AGRICULTURE IN RESPECT OF NON-ADHERENCE TO TREASURY PRESCRIPTS AND LACK OF FINANCIAL CONTROL IN THE ADMINISTRATION OF THE VREDE DAIRY PROJECT

1. INTRODUCTION

- 1.1. **“Lack of Oversight”** is my provisional report in terms of section 182(1)(b) of the Constitution of the Republic of South Africa, 1996 (the Constitution) and section 8(1) of the Public Protector Act, 1994 (the Public Protector Act).
- 1.2. In order to afford them an opportunity to respond the provisional findings the relevant parts of the report is submitted, in terms of section 7(9) of the Public Protector Act, to:
- 1.2.1. The Head of the Free State Department of Agriculture, Mr MP Thabethe.
- 1.3. A discretionary provisional notice was provided to the Complainant, Mr R Jankielsohn, Free State Provincial Legislature, Democratic Alliance (the Complainant).
- 1.4. A further discretionary provisional notice was provided to The Premier of the Free State Province, the Honourable Mr. E.S. Magashule and the competent authority The Member of the Executive Council for Agriculture and Rural Development, Free State Provincial Government, Ms M Qabathe, which I am considering requesting to act in terms of the Remedial Action.
- 1.5. A further discretionary provisional notice was provided to The Auditor-General of South Africa Mr T.K. Makwetu and The Head of the Special Investigating Unit,

Advocate V. Soni (SC), which I am also considering requesting to act in terms of the Remedial Action.

- 1.6. The report relates to an investigation into the alleged maladministration by the Free State Department of Agriculture and Rural Development (the Department) in that the Department did not adhere to Treasury Prescripts when the Vrede Dairy Project (the Project) was implemented and the lack of financial control in the administration of the Project.

2. THE COMPLAINT

- 2.1. The Complainant approached the Public Protector on 12 September 2013 with allegations of maladministration in respect of the Project implemented by the Department. The following allegations were made;

- 2.1.1 An agreement between ESTINA/PARAS and the Department in respect of the Project are subject to a confidentiality clause which is contrary to good governance principles as public money funds the project. The Complainant alleges that the National Department of Agriculture invested R30 million (2012/2013) in the Project during the previous financial year and will invest R84 million in this financial year (2013/2014);

- 2.1.2 The Private Company will invest R228 million for a shareholding of 49% and Government will contribute R342 million for a shareholding of 51%, contrary to Treasury Prescripts in respect of Public Private Partnerships; and

- 2.1.3 The Private Company contributes only 40% of the funds needed for a 49% share allocation which he alleges are irregular in terms of Treasury Prescripts;

- 2.1.4 That 400 pregnant cows were procured at inflated prices

2.2. On 28 March 2014 the Public Protector received a further complaint from the Complainant on the Vrede Dairy Project. The Complainant made the same allegations as the allegations received on 12 September 2013. The Complainant however submits the following further allegations:

2.2.1 That the prices for goods and services procured by the Private Company were inflated and queried specific alleged expenses in respect of construction, processing equipment, administration costs and the purchase price of cows.

2.2.2 That environmental requirements and legislation was not adhered to in the operation of the project; and

2.2.3 That between 50 and 100 cattle has died since being purchased and requested an investigation into the cause of the deaths of the cattle.

3. POWERS AND JURISDICTION OF THE PUBLIC PROTECTOR

3.1. The Public Protector was established under section 181(1)(b) of the Constitution to strengthen constitutional democracy through investigating and redressing improper conduct in state affairs.

3.2. Section 182(1) of the Constitution provides that I have the power to investigate any conduct in state affairs, or in the public administration in any sphere of government, that is alleged or suspected to be improper or to result in any impropriety or prejudice, to report on that conduct and take appropriate remedial action. Section 182(2) directs that I have additional powers prescribed in legislation.

3.3. I am further empowered by the Public Protector Act to investigate and redress maladministration and related improprieties in the conduct of state affairs and to

resolve the disputes through conciliation, mediation, negotiation or any other appropriate alternative dispute resolution mechanism.

3.4. The Free State Department of Agriculture and Rural Development is an organ of state and its conduct amounts to conduct in state affairs, as a result the matter falls within my ambit.

3.5. My jurisdiction to investigate was not disputed by any of the parties.

4. THE INVESTIGATION

4.1. Methodology

4.1.1. The investigation was conducted in terms of section 182 of the Constitution and sections 6 and 7 of the Public Protector Act.

4.1.2. The Public Protector Act confers on the Public Protector the sole discretion to determine how to resolve a dispute of alleged improper conduct or maladministration.

4.2. Approach to the investigation

4.2.1. Like every Public Protector investigation, the investigation was approached using an enquiry process that seeks to find out:

- What happened?
- What should have happened?
- Is there a discrepancy between what happened and what should have happened and does that deviation amount to maladministration?

- In the event of maladministration what would it take to remedy the wrong or to place the Complainant as close as possible to where they would have been but for the maladministration or improper conduct?
- 4.2.2. The question regarding what happened is resolved through a factual enquiry relying on the evidence provided by the parties and independently sourced during the investigation. In this particular case, the factual enquiry principally focused on whether or not the Department acted improperly in relation to adherence to Treasury Prescripts in respect of the implementation of the Project and whether adequate control was exercised over the project in terms of legislative prescripts.
- 4.2.3. The enquiry regarding what should have happened, focuses on the law or rules that regulate the standard that should have been met by the Department or organ of state to prevent maladministration and prejudice.
- 4.2.4. The enquiry regarding the remedy or remedial action seeks to explore options for redressing the consequences of maladministration. Where a Complainant has suffered prejudice the idea is to place him or her as close as possible to where they would have been had the Department or organ of state complied with the regulatory framework setting the applicable standards for good administration.
- 4.3. **On analysis of the complaint, the following were issues considered and investigated:**
- 4.3.1. Whether or not the Treasury prescripts in respect of a Public Private Partnerships were adhered to and whether or not the contribution of 40% of the funds for an allocation of 49% of the shares in the company was contrary to Treasury prescripts;
- 4.3.2. Whether or not the contents of the agreement between the Department and the Private Company were adhered to in that the Department implemented

appropriated monitoring and management procedures in respect of financial, performance, budget evaluation and expenditure control;

4.3.3. Whether or not the prices for goods and services procured were inflated and specific alleged expenses in respect of construction, processing equipment, procurement of cows and administration costs;

4.3.4. Whether or not environmental legislation was adhered to during the farming operations?

4.3.5. The following issues were not investigated:

4.3.5.1 The cause of the deaths of the cattle alleged. The photographs submitted in respect of the death of the cattle indicated that the deaths did not occur recently.

4.3.5.2 Whether or not value for money was obtained by the Government in terms of the agreement. This issue was investigated by National Treasury: Accounting General.

4.4 The Key Sources of information

4.4.1 Documents

4.4.1.1 Undated – Vrede Integrated Dairy Agribusiness Project Proposal – Free State Department of Agriculture and Rural Development, PARAS and ESTINA;

4.4.1.2 Undated – Beneficiary List for Agri-BEE that contains 80 names of beneficiaries. ID number for 15 beneficiaries was not on the list and 62 copies of ID's of beneficiaries were submitted for verification;

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- 4.4.1.3 Undated - Beneficiary Agreement signed by one beneficiary on behalf of the 80 beneficiaries;
- 4.4.1.4 22 March 2012 - Budget Vote Speech of the Free State Department of Agriculture and Rural Development tabled by the Honourable MJ Zwane, Member of the Executive Council for Free State Agriculture and Rural Development;
- 4.4.1.5 5 July 2012 – Agreement entered into and between The Free State Department of Agriculture and ESTINA (Pty) Ltd;
- 4.4.1.6 October 2012 - Vrede Dairy Project: Feasibility Study;
- 4.4.1.7 January 2013 - Report on the investigation into the Vrede Integrated Dairy Farm Project, National Treasury;
- 4.4.1.8 18 January 2013 - Notarial Lease Nr K000000024/201 - Lease for the farm Krynaauwslust Lust, 275 district Vrede, Free State (4439,5122 Hectares) Phumelela Municipality and Department of Rural Development and Agriculture: Cession and assignment signed on 14 December 2012 in terms that Municipality ceded and assigned all rights, title, interest and obligations to Department;
- 4.4.1.9 21 February 2013 - State of the Province Address by Honourable E.S. Magashule Premier of the Free State Province;
- 4.4.1.10 12 May 2013 - Authorisation register number of DETEA EMB/4,11(iii)(iv)(xi),22,23(ii)/12/65, Activity Location: Establishment of Dairy Farm near the town of Vrede in the Free State;
- 4.4.1.11 30 June 2013 – Submission by ESTINA to Free State Department of Agriculture on the timelines and milestones for phases 2 and 3 of the Project;

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- 4.4.1.12 10 July 2013 - Report on Vrede Integrated Dairy Project dated 10 July 2013, drafter Member of the Executive Council, Free State Department of Agriculture and Rural Development addressed to the Chairperson, Portfolio Committee on Agriculture and Rural Development;
- 4.4.1.13 29 July to 02 August 2013 - Report of the Portfolio Committee on Agriculture, Forestry and Fisheries on the Oversight Visit to the Free State Province;
- 4.4.1.14 13 August 2013 - Free State and KwaZulu-Natal on 2012/13 budget performance: briefing by National and Provincial Treasuries: South African Parliament;
- 4.4.1.15 8 October 2013 - Auditor-General on Key Challenges in Agriculture Department's Audit Report 2013: South African Parliament;
- 4.4.1.16 13 November 2013 - Written response of Member of the Executive Council of Agriculture to Question in Free State Provincial Legislature;
- 4.4.1.17 11 February 2014 - Third quarter 2013/14 expenditure: National Treasury, Provincial Treasuries of Gauteng & Free State briefings: South African Parliament;
- 4.4.1.18 4 March 2014 - Department of Water Affairs: Letter addressed to ESTINA-approval and registration of the water use;
- 4.4.1.19 1 April 2014 - ESKOM electricity agreement with ESTINA;
- 4.4.1.20 25 April 2014 - Letter from ESTINA to the Free State Department of Agriculture referring to a letter dated 24 April 2014 cancelling agreement in terms of clause 15.3 of the Agreement. Clause 15.3 indicates that ESTINA shall be entitled to

payment in full for the services delivered. The letter demands payment of R136, 252, 652.00;

- 4.4.1.21 19 May 2014 – Submission to the Free State Executive Council to transfer the Vrede Integrated Dairy Project to the Free State Development Corporation by the Member of the Executive Council of the Free State Department of Agriculture and Rural Development;
- 4.4.1.22 22 May 2014 – Letter from the Head of the Free State Department of Agriculture to the Chief Executive Officer of the Free State Development Corporation referring to EXCO resolution 62/2012 dated 13 June 2012 to implement project. The letter submits that after EXCO revisited project it was decided on 16 April 2014 that the project must be transferred to the Free State Development Corporation;
- 4.4.1.23 27 May 2014 - Free State Development Corporation Board Meeting minutes, Item 01/2014/80. The Board approves the take-over. The Company Secretary and Acting Chief Financial Officer instructed to conduct a high-level due diligence of the project and table a report at the next Board meeting. The Board will then decide on an appropriate project business model;
- 4.4.1.24. April 2014 – Feasibility Study and Business Plan for ESTINA (Pty) Ltd for the farm Krynaauwslust.
- 4.4.1.25 Monthly Financial reports submitted by ESTINA to the Free State Department of Agriculture for the months of July 2012 up to and including February 2013, April 2013 up to and including July 2013, September 2013 up to and including December 2013;

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- 4.4.1.26 Cash Flow Projection of ESTINA for the project – For the period August 2012 to September 2013;
- 4.4.1.27 Quarterly progress reports of the Project submitted by ESTINA to the Free State Department of Agriculture for the periods March 2013, June 2013 and September 2013;
- 4.4.1.28 26 November 2014 - General Report on the Audit outcomes of the Free State: PMFA 2013-14; and
- 4.4.1.29 26 November 2014 – Media release by Auditor General – Free State PFMA 2013-14 audit outcome highlights.
- 4.4.2 Interviews conducted**
- 4.4.2.1 17 September 2013 – Manager in the Head of the Free State Department of Agriculture and Rural Development; and
- 4.4.2.1 30 September 2014 – Chief Executive Corporate Services: Free State Development Corporation;
- 4.4.3 Correspondence sent and received**
- 4.4.3.1 26 September 2013 – Email to Head of the Free State Department of Agriculture;
- 4.4.3.2 21 March 2014 – Response from the Member of the Executive Council of the Free State Department of Agriculture and Rural Development
- 4.4.3.3. 6 June 2014 – Letter to the Head of the Free State Department of Agriculture.

4.4.3.4 11 July 2014 - Letter to the Head of the Free State Department of Agriculture – submission of documents requested.

4.4.4 Inspections *in loco* conducted

4.4.4.1 4 September 2014 – visit to the Vrede Dairy Project – access denied.

4.4.5 Websites consulted/ electronic sources

4.4.5.1 www.cipc.co.za/ : 16 April 2014 CIPC search on Company Mohoma Mabung Dairy Project;

4.4.5.2 www.gov.za/ : 25 March 2014: Budget Votes Free State Department of Agriculture and Rural Development 2012/2013 and State of the Province Address by the Free State Premier on 21 February 2013;

4.4.5.3 http://archive-za.com/page/1678019/2013-03-20/http://www.ard.fs.gov.za/?page_id=1256: 25 March 2014 - Mohoma Mobung;

4.4.5.4 <http://www.saholstein.co.za/Shows-Results.htm>: 25 March 2014 – Sale prices of Holstein Breed Heifers;

4.4.5.5 <http://www.ppp.gov.za/Pages/projectlist.aspx>: 25 March 2014 - PPP Projects approved, finalised and in preparation, registered in terms of Treasury Regulations; and

4.4.5.6 <http://www.agsa.co.za/Documents/Auditreports.aspx>: 27 November 2014 General Report on the Audit outcomes of the Free State: PMFA 2013-14

4.3.6. Legislation and other prescripts

- 4.3.6.1. The Constitution of the Republic of South Africa, 1996;
- 4.3.6.2. The Public Management Finance Act, 1 of 1999;
- 4.3.6.3. Regulations in terms of the Public Finance Management Act, 2005;
- 4.3.6.4. National Treasury PPP Practice Note Nr 02 of 2004;
- 4.3.6.5. National Treasury Practice Note Nr 11 of 2008/2009;
- 4.3.6.6. National Treasury Practice Note No 8 of 2007/08;
- 4.3.6.7. Supply Chain Management: a Guide for Accounting Officers /Authorities, February 2004: National Treasury;
- 4.3.6.8. Allpay Consolidated Investment Holdings (Pty) Ltd and Others v Chief Executive Officer of the South African Social Security Agency and Others (2014 (1) SA 604 (CC); and
- 4.3.6.9. The Chief Executive Officer of the South African Social Security Agency N.O. v Cash Paymaster Services (Pty) Ltd (90/10) [2011] ZASCA 13 (11 March 2011).

5. APPLICABLE LAW AND RELATED PRESCRIPTS

5.1. The Constitution of the Republic of South Africa

- 5.1.1. Section 195 of the Constitution provides that the public administration must be governed by principles, which include a high standard of professional ethics, efficient, economic and effective use of resources, and the impartial provision of services.
- 5.1.2. This refers to elements of the principle of integrity which require that public officials should take cognisance of the values of society and its communities and

not substitute their own value choices for those of the society; in other words, they should in all respects be publicly accountable for their actions.

- 5.1.3. Section 217 of the Constitution provides that organs of state (and this includes municipalities and municipal entities¹) must agreement for goods or services in accordance with a system that is fair, equitable, transparent, competitive and cost-effective.
- 5.1.4. With the adoption of the final Constitution in 1996, it was a constitutional prerequisite that procurement must take place in terms of a system, which is fair, equitable, transparent, competitive and cost effective. The Constitution itself made provision for procurement policy framework legislation.
- 5.1.5. To give effect to these constitutional requirements, framework legislation was enacted by means of the PFMA to regulate public procurement in national and provincial government.
- 5.1.6. Section 217 and 195 of the Constitutions create the basis for a public procurement framework aimed at ensuring equity, good governance and administration, fair dealing in administrative context, enhancing protection of the individual against abuse of state power, promoting public participation in decision-making, and strengthening the notion that public officials are answerable and accountable to the public they are meant to serve.²
- 5.1.7. Administrative justice imposes a range of obligations arising from section 33(1) of the Constitution to effect citizens' rights to fair administrative action. These values are lawfulness, reasonableness and procedural fairness.

¹ See s 217(1) which refers to organs of state in the national, provincial and local sphere of government. See also s 239 of the Constitution for the definition of an organ of state.

² Devenish, Govender and Hulme *Administrative Law* 14-16

5.1.8. Each administrative action in a procurement process must be in accordance with the law and prescribed procedures; there must be accountability, responsiveness and openness in the decision-making of the institution; all bidders at each stage of a procurement process must have an equal chance of competing for the agreement; and no action taken by government may prejudice their competitiveness.

5.2. **The Public Finance Management Act**

5.2.1. Section 38(1)(a) and (b) of the Public Finance Management Act (PMFA) requires accounting officer of departments to ensure that an effective, efficient and transparent financial and risk management systems are in place.

5.2.2. Section 38(1)(b) of the PMFA makes the accounting officers of departments responsible for the effective, efficient, economical and transparent use of the department's resources. Section 38(1)(c)(iii) and 51(b)(iii) of the PMFA requires accounting officers to take appropriate steps to efficiently manage the department's capital.

5.2.3. Government has a responsibility towards its citizens to expend public finances in an effective, efficient and economic manner. In order to do so, sound financial management practices are required in terms of legislation, thus placing a high burden of accountability on all civil servants and specifically accounting officers.

5.2.4. In terms of section 81(1)(b) and 83(1)(b) of the PFMA, an accounting officer and accounting authority shall commit an act of financial misconduct if that accounting officer or accounting authority makes or permits irregular expenditure.

- 5.2.5. Section 1 of the PMFA defines irregular expenditure, as *“expenditure other than unauthorised expenditure, incurred in contravention of or that is not in accordance with a requirement of any applicable legislation, including –*
- (a) This Act; or ...*
- (c) Any provincial legislation providing for procurement procedures in that provincial government...”*
- 5.2.6. Sound financial management and good corporate governance form the foundation of the Act, as do transparency and the drive to eliminate waste and corruption in the use of limited resources.
- 5.2.7. In determining whether irregular expenditure has taken place, there must have been a transgression of a provision contained in any applicable legislation which shall include the PFMA, Treasury Regulations, National Treasury Instruction, issued in terms of section 76 of the PFMA and a Provincial Treasury Instruction issued in terms of section 18(2)(a) of the PFMA.
- 5.2.8. Section 6 of Public Finance Management Act (PMFA) entrust National Treasury with custodianship of the PMFA and National Treasury monitor and assess implementation of the PMFA.
- 5.2.9. National Treasury is empowered to investigate financial management and investigate financial management and internal control and may do anything further that is necessary to fulfill its responsibilities effectively.
- 5.2.10. The PMFA establishes provincial treasuries, which are responsible for preparing and managing provincial budgets, and enforcing uniform treasury norms and standards as prescribed by the National Treasury and this Act.

5.3. National Treasury Regulations, 2005

- 5.3.1. There are certain requirements before a government can successfully use Public-Private-Partnerships (PPP) to procure public services infrastructure. A detailed legislative framework is in place through the PMFA and PFMA regulation 16 of the Treasury Regulation (Regulations).
- 5.3.2. Only an accounting officer may enter into a PPP agreement on behalf of the department, and only with the prior written approval of the national Treasury.
- 5.3.3. To determine whether a proposed PPP agreement is in the best interests of a department, the accounting officer must prepare a feasibility analysis. It should, among other things, explain the strategic and operational benefits of the PPP agreement and assess how the agreement will assist in meeting the department's strategic objectives. The details of the processes to be followed are specified in regulation 16 of the Regulations.
- 5.3.4. Regulation 3.2.1 of the Regulations addresses risk management and the accounting officer must ensure that a risk assessment is conducted regularly to identify emerging risks for the institution. The risk management strategy, which must include a fraud prevention plan, must be used to direct internal audit effort and priority and to determine the skills required of managers and staff to improve controls and to manage these risks.
- 5.3.5. An effective financial management system is inclusive of, but not limited to the implementation of financial management policies and procedures, an effective supply chain management system, internal control mechanisms and anti-corruption measures and ensures compliance to the financial management legislative framework.

- 5.3.6. Irregular expenditure incurred as a result of institutions procuring goods or services by means other than through competitive bids and where reasons for deviating from inviting competitive bids have not been recorded and approved by the functionary to whom the power has been delegated by the accounting officer or accounting authority. (Contravention of Treasury Regulation 16A6.4).
- 5.3.7. Treasury Regulation 16A6.4 determines that institutions procuring goods or services by means other than through competitive bids and where reasons for deviating from inviting competitive bids have not been recorded and approved by the functionary to whom the power has been delegated by the accounting officer or accounting authority results in irregular expenditure.
- 5.3.8. Treasury Regulation 4.1.3 provides that, if an accounting officer is alleged to have committed financial misconduct, the relevant treasury, as soon as it becomes aware of the alleged misconduct, must ensure that the relevant executive authority initiates an investigation into the matter and if the allegations are confirmed, holds a disciplinary hearing in accordance with the prescripts applicable and agreements applicable in the public service.

5.4 National Treasury PPP Practice Note Nr 02 of 2004

- 5.4.1 National Treasury PPP Practice Note Nr 02 (Practice Note 2) states that the way that a PPP is defined in the regulations makes it clear that a PPP is not a simple outsourcing of functions where substantial financial, technical and operational risk is retained by the institution or a donation by a private party for a public good or the privatisation or divesture of state assets and/or liabilities. PPP's may involve a degree of capital contribution by the institution to the initial costs of the project.

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- 5.4.2 Practice Note 2 further states that the regulation sets out clear PPP procurement steps that must be followed by institutions, and prescribes distinct treasury approvals that must be obtained in this phase.
- 5.4.3 Practice Note 2 further requires that effective monitoring should provide the basis for reviewing actual private party performance against the output specifications and other obligations contained in the agreement.
- 5.5 National Treasury Practice Note Nr 11 of 2008/2009**
- 5.5.1 National Treasury Practice Note Nr 11 (Practice Note 11) states that institutions are not obliged to consider an unsolicited proposal but may consider such a proposal only if it meets the following requirements:
- 5.5.1.1 A comprehensive and relevant project feasibility study has established a clear business case; and
- 5.5.1.2 The product or service involves an innovative design; or
- 5.5.1.3 The product or service involves an innovative approach to project development and management; or
- 5.5.1.4 The product or service presents a new and cost-effective method of service delivery.
- 5.6 National Treasury Practice Note No 8 of 2007/08**
- 5.6.1 The National Treasury Practice Note No 8 of 2007/08, which came into effect on 1 December 2007 prescribes the following in paragraph 3.4 regarding any transaction which exceeds R500 000. (VAT included):

“3.4.3 Should it be impractical to invite competitive bids for specific procurement, e.g. in urgent or emergency cases or in case of a sole supplier, the accounting officer / authority may procure the required goods or services by other means, such as price quotations or negotiations in accordance with Treasury Regulation 16A6.4. The reasons for deviating from inviting competitive bids should be recorded and approved by the accounting officer / authority or his / her delegate. Accounting officers /authorities are required to report within ten (10) working days to the relevant treasury and the Auditor-General all cases where goods and services above the value of R1 million (VAT inclusive) were procured in terms of Treasury Regulation 16A6.4. The report must include the description of the goods or services, the name/s of the supplier/s, the amount/s involved and the reasons for dispensing with the prescribed competitive bidding process.”

5.6.2 The purpose of the reporting requirement is clearly to provide the National Treasury, as the custodian of public funds, with an opportunity to note, evaluate and, if necessary, intervene in the procurement process. The failure to report the deviation therefore accordingly deprived the National Treasury from the intended opportunity.

5.7 Supply Chain Management: a Guide for Accounting Officers /Authorities

5.7.1 The SCM Guide at paragraph 4.7.5.1 notes that in urgent and emergency cases, an institution may dispense with the competitive bidding process but must act in a manner that is in the best interest of the State.

5.7.2 The SCM Guide defines an “emergency case” as –

“A case where immediate action is necessary in order to avoid a dangerous or risky situation or misery.” (Emphasis added).”

5.7.3 Organs of state should, where urgency dictates a deviation from procurement procedures, carefully consider the value and lengths of contracts concluded in

order to address only the immediate urgency. In this way on-going needs and requirements must as far as possible and where appropriate, be met by way of public tender procedures.

5.8 Jurisprudence

5.8.1 The Constitutional Court in the case of Allpay Consolidated Investment Holdings (Pty) Ltd held that *“the materiality of compliance with legal requirements depends on the extent to which the purpose of the requirements is attained.”*³

5.8.2 The Court indicated that the mandatory and material procedure or condition approach... *“undermines the role procedural requirements play in ensuring even treatment of all bidders. Second, it overlooks that the purpose of a fair process is to ensure the best outcome; the two cannot be severed. On the approach of the Supreme Court of Appeal, procedural requirements are not considered on their own merits, but instead through the lens of the final outcome. This conflates the different and separate questions of unlawfulness and remedy. If the process leading to the bid’s success was compromised, it cannot be known with certainty what course the process might have taken had procedural requirements been properly observed.”*

5.8.3 In the Chief Executive Officer of the South African Social Security Agency N.O. v Cash Paymaster Services (Pty) Ltd⁴ the court dealt with the mandatory and material procedure or condition prescribed by an empowering provision in respect of procurement requirements. The court held that *“it’s important to mention that the mere failure to comply with one or other administrative provision does not mean that the whole procedure is necessarily void. It depends in the first instance*

³ Allpay Consolidated Investment Holdings (Pty) Ltd and Others v Chief Executive Officer of the South African Social Security Agency and Others (2014 (1) SA 604 (CC))
⁴ The Chief Executive Officer of the South African Social Security Agency N.O. v Cash Paymaster Services (Pty) Ltd (90/10) [2011] ZASCA 13 (11 March 2011)

on whether the Act contemplated that the relevant failure should be visited with nullity and in the second instance on its materiality." The court further referred to a decision in *Moseme Road Construction CC & Others v King Civil Engineering Agreementors (Pty) Ltd & Another* 2010 (4) SA 359 (SCA) where it was held that *"not every slip in the administration of tenders is necessarily to be visited by judicial sanction"*. The court held that consideration of public interest, pragmatism and practicality should inform the exercise of a judicial discretion whether to set aside administration or not.

6. EVIDENCE AND INFORMATION OBTAINED

6.1 INTRODUCTION

- 6.1.1 Mohoma Mobung is the Free State Provincial Government initiative in line with the Zero Hunger Strategy. Mohoma Mobung is a multi-year mega Public and Private Partnership business concept, which revolves around income generation through farming in the rural area of the province, and the creation of on and off-farm agribusiness, value chain enterprises and Black Economic Empowerment.
- 6.1.2 It is a strategic approach that aims at addressing low household incomes by increasing agricultural production, value and profitability of household agricultural production, Agro-processing and Marketing.
- 6.1.3 It is reported that the initiative includes crop, fisheries and livestock, related agro-processing and agribusiness enterprises and market access concerns.
- 6.1.4 Eligible entities are Cooperatives, Companies, Partnership and Proprietary farms, Agricultural produce marketing committees/boards, Cottage-industries and Growers associations. Agro-processing has been identified by the government as a key driver of job creation in the agriculture sector as identified in the New Growth Path document.

- 6.1.5 The initiative will bring more enterprises and investors into agriculture in order to stimulate competition and demand for agricultural products for the domestic and export markets. The initiative has the potential of creating more than 10 000 decent permanent jobs and more than 100 000 indirect jobs.⁵
- 6.1.6 During the 2012 Budget Vote Speech of the Free State Department of Agriculture and Rural Development tabled by the Honourable MJ Zwane, MEC for Agriculture and Rural Development it was reported that

“In line with the value adding approach, the Free State Provincial Government introduced Mohoma Mobung as the Provincial Growth and Development Strategy for the agriculture and rural development sector. It is a multi-year mega Public and Private Partnership business concept that deals with income generation through farming in the rural area of the province, the creation of on- and off-farm agri-business, value chain enterprises and Black Economic Empowerment. This overarching strategic intent is underscored by a dedication to make the long term more urgent. To give effect to our strategic intent as encapsulated in Mohoma Mobung for the financial year 2012/13 we allocated R131.8 million to projects. With this investment we want to break the back of unemployment, poverty and food insecurity.

Honourable Speaker, the department has identified Thabo Mofutsanyane as a dairy hub and an amount of R17.0 million is allocated for this development. Vrede, QwaQwa and Ficksburg towns will benefit from this initiative. Production and processing plants will be established, and this will create 150 jobs within the value chain.”⁶

⁵ http://archive-za.com/page/1678019/2013-03-20/http://www.ard.fs.gov.za/?page_id=1256

⁶ 22 Mar 2012

- 6.1.7. During the 2013 State of the Province Address by Honourable E.S. Magashule Premier of the Free State province: 21 Feb 2013 the Premier remarked on the project as follows:

“Vrede Dairy Project: The Department of Agriculture is establishing an Integrated Dairy Project at Vrede in the Eastern Free State under the Mohoma-Mobung initiative in partnership with the private sector.

The project is unfolding in phases. This state of the art certified facility will be constructed with the initial processing capacity of 100,000 litres per day and an initial targeted milk intake of 40,000 litres per day. Products to be produced at the Vrede Dairy project will include liquid milk, UHT milk, cheese and other products.”⁷

- 6.1.8 The Mail & Guardian newspaper reported the following:

“Seemingly conceptualised during the first half of last year, the project started taking off when the Phumelela local municipality, which includes Vrede, ceded the Krynaauwslust farm outside the town to the province last December. The provincial agriculture department, which will fund the project, immediately handed it to Estina under a 99-year rent-free lease. The plan is for Krynaauwslust’s 4400ha to house a large herd of cows and a huge processing plant for milk from the farm and beyond...

A second proposal document hails the technical prowess of Paras. It calls Estina “the local representative company which has been appointed by Paras” to engage with the provincial agriculture department on the dairy project. Both documents carry Estina and Paras logos. But this week a Paras spokesperson in India, Bharti Singh, repeated the company’s denial that it knows of Estina or the Vrede project. Singh said she had circulated amaBhungane’s query to all Paras directors. “We

*have no businesses in South Africa. We don't know Estina. There is nothing that connects Paras dairy to South Africa," she said."*⁸

6.2. Complainant's Case

6.2.1. Whether or not the Treasury prescripts in respect of a Public Private Partnerships were adhered to and whether or not the contribution of 40% of the funds for an allocation of 49% of the shares in the company was contrary to Treasury prescripts

6.2.1.1. The Complainant alleged that the project was approved based on the proposal by PARAS. It appears, however, that ESTINA is the only private sector partner with a 49% share in the venture. It was also alleged that ESTINA would only make capital contributions "*if needed.*"

6.2.1.2. The Complainant further submitted that in terms of the agreement ESTINA will require 49% of the shares in the Agri-BEE company and only contribute 40% of the capital for the project.

6.2.1.3. The Complainants further alleged that it is also clear that the Free State Department of Agriculture, together with the Office of the Premier, designed the agreement to benefit ESTINA and must have been aware that PARAS would not be involved.

6.2.1.4. The Complainant submitted that the feasibility study for the project was carried out after the project was approved and the agreement blatantly benefits the private sector partner, ESTINA, to the detriment of taxpayers and beneficiaries. The Complainant was further concerned that an Indian company, who is supposed to supply the expert advice to the Vrede dairy project and milk

processing plant, denied, in the press, that they have any involvement in the project.

6.2.2. Whether or not the contents of the agreement between the Department and the Private Company were adhered to in that the Department implemented appropriated monitoring and management procedures in respect of financial, performance, budget evaluation and expenditure control

- 6.2.2.1. The Complainants submitted that in terms of the Proposal and Agreement the provincial government has no guarantees that ESTINA will meet its obligations to invest R228 million in addition to the R342 million allocated by the provincial government.
- 6.2.2.2. The Complainants further submitted that the contact indicates that ESTINA will only invest their money if necessary and that the whole project will be transferred to a private company registered as Mohoma Mobung Dairy Project with Mr. Kamal Vasram who has a background in IT as the sole director. The provincial government will receive no benefit from this.
- 6.2.2.3. The Complainants submitted that ESTINA as implementing agent of the project are using public money and profiting from government's R342 million contributions. In the 2012 alone R114 million was given to ESTINA. ESTINA is acting as the partner, implementing agent, and supplier in this project. Even though government money is being used, it appears that normal procurement procedures have been by-passed.
- 6.2.2.4. The Complainant submitted that the current private sector partner in the project, ESTINA, appears to have no background in the dairy industry. When this project was initiated, it was indicated that an Indian company with experience in this industry, namely PARAS, would partner with ESTINA.

6.2.3. Whether or not the prices for goods and services procured were inflated and specific alleged expenses in respect of construction, processing equipment, procurement of cows and administration costs

6.2.3.1 The Complainant alleged that funds allocated by the provincial government for various goods and services indicate that prices have been hugely inflated. Some of these include, among others construction of a silage bunker for R5 million, 2km gravel access road for R1,2 million, security gate and guard house for R2,6 million, cattle feed plant for R7,350 million, milking parlour and milk processing plant for R30,050 million and 351 dairy cows for R6,212 million.

6.2.3.2 The Complainant further indicated that an amount of roughly R12 million was spent on administrative, legal, account and other consulting fees.

6.2.3.3 The Complainant further submitted that the following cattle was purchased and indicated alleged prices according to market prices of the Holstein Friesland stud association:

Types of Heifers Purchased	Number Purchased	Market price of Friesland/Holstein Stud Heifers	Total Cost
Pregnant Heifers	62	R15,000 per heifer	930,000
Breeding Cows	57	R16,000 per cow	912,000
Calves 12 months+	70	R8,000 per heifer	560,000
Heifers 9 – 12 mths	77	R6,000 per heifer	462,000
Heifers 6 – 9 mths	85	R4000 – R6000 per heifer	510,000 (max)
TOTAL			R3,374,000

6.2.3.4 The Complainant further alleged that the National Department of Agriculture supplied the provincial government with equipment that included tractors and related equipment for planting and maintaining crops to the value of R40+ million. The Complainant submitted that additional cost on these items for the project amounted to R5, 867, 494.00.

6.2.3.5 The Complainant made a press release on 2 May 2013 stating the following:

“The DA will submit questions to the MEC for Agriculture and Rural Development in the Free State, Ms. M. Qabathe, about a large number of tractors and farm implements worth millions of rand that are gathering dust at the Vrede show-grounds. The implements and tractors were donated to the province by the national government for distribution to various beneficiaries within the Free State. These implements and tractors have been gathering dust for a year at the Vrede show-grounds and are already showing signs of neglect. I visited the terrain yesterday (2 May 2013) to inspect the implements and tractors. I found 24 Massey Ferguson Tractors (628’s and 290’s), 6 trailers (6 ton), 16 planters, 8 ploughs, and about 46 other pieces of tractor drawn farm equipment (see attached photographs). All the implements and tractors are new. These implements and tractors could already have been utilized to assist farmers to plant crops in the last planting season.”

6.2.4. Whether or not environmental legislation was adhered to during the farming operations

6.2.4.1 The Complainant submitted that the agreement between the Department and ESTINA provides for the latter to ensure compliance with environmental legislation.

6.2.4.2 The Complainant alleges that the environmental legislation has been breached in that ESTINA has indiscriminately ploughed natural fields and wetlands.

6.2.4.3 The Complainant submitted that this cannot be done without the legislative requirement of an Environmental Authorisation from the Department of Environmental Affairs.

6.3. Department's Case

6.3.1. Whether or not the Treasury prescripts in respect of a Public Private Partnerships were adhered to and whether or not the contribution of 40% of the funds for an allocation of 49% of the shares in the company was contrary to Treasury prescripts

- 6.3.1.1. The Department submitted that an agreement was entered with ESTINA for the construction and implementation of the project. The first phase of the project involves a parlour with the capacity to milk 1000 cows.
- 6.3.1.2. The Department submitted that the second phase will involve the implementation of a processing plant to produce packaged milk and other dairy products.
- 6.3.1.3. The Department submitted that ESTINA agreed to the formation of a new legal entity Mohoma Mobung Dairy Project (Pty) Ltd wherein ESTINA will hold 49% shares and beneficiaries of the project will hold 51% of the shares in the company.
- 6.3.1.4. The MEC for the Department informed the Public Protector that The total project cost is R570 million of which Estina/Paras will contribute R228 million (40% of total cost) and the Department will contribute R342 million. The Department has secured 51% of the shareholding for 100 beneficiaries. Estina/Paras will obtain 49% of the shareholding and will provide services and professional fees. Management and administration costs of the project amounts for the difference of 9%.
- 6.3.1.5. The MEC reported that the Department will contribute the R342 million in yearly R114 million contributions over a period of 3 years and the R30 and R84 million is the contribution for the year. As on 21 March 2014 the Department had contributed R114 million.

- 6.3.1.6. The Department submitted an undated Project Proposal named “Vrede Integrated Dairy project: Proposed integration of Dairy and other elements of production and processing with the emphasis on value-addition and beneficiation, such as a range of processed dairy products” was submitted by the Department to the Public Protector.
- 6.3.1.7. The document (8 pages in total) refers to PARAS and their history. The document further contains the proposals in respect of the viability of the projects. The proposal states that the project will require an initial fixed capital of R500 million to make it viable and projected a turnover is R80 million with a net profit of R16 million. The project proposal also indicates employment opportunities as 600 employees.
- 6.3.1.8. According to the proposal lists the budget values but indicate the initial R500 million needed includes R40 million as working capital. A phased approach is recommended indicating a project over 5 years.
- 6.3.1.9. The Department further submitted a document named “Vrede Dairy Project: Feasibility Study” dated October 2012. The objective of the project contained in the document is to Utilise existing natural and other resources to create agro-industrial enterprise;
- 6.3.1.9.1 Broaden the agro-industrial production base in the area;
 - 6.3.1.9.2 Improve food security for rural communities;
 - 6.3.1.9.3 Create number of small enterprises; and
 - 6.3.1.9.4 Alleviate poverty in surrounding communities.
- 6.3.1.10. Breakdown of costs are listed and assumptions on profit are made in the document. It is noted from the document that milk production will start in April-

May 2013. Projections of costs are submitted for the years 2012/2013 up to and including 2017/2018.

- 6.3.1.11. A copy of the agreement concluded between ESTINA and the Free State Department of Agriculture was submitted. The Agreement was concluded on 5 July 2012. In terms of the agreement a project plan in line with ESTINA proposals which must have milestones and timelines for phase 2 as approved by Department must be submitted by ESTINA to the Department.
- 6.3.1.12. The Department submitted documentation that indicate that the farm, Krynaauwslust Lust, 275 district Vrede, Free State (4439, 5122 Hectares) was leased from the Phumelela Local Municipality for the project. Phumelela Local Municipality and the Department signed a cession and assignment on 14 December 2012 in terms of which the Phumelela Local Municipality ceded and assigned all rights, title, interest and obligations to Department.
- 6.3.1.13. The document further states that the Department then leases the farm to ESTINA. The lease is for a period of 99 years with option to renew for another 99 years. Cancellation of the lease is by mutual agreement. The use of the property is to conduct an integrated dairy project and any other purpose needs the consent of the Department. On termination of the lease the Department has to compensate the lessee at market value for the improvements made by the lessee. The lease is rent free.
- 6.3.1.14. The Department submitted a letter dated 22 May 2014 from the Head of the Free State Department of Agriculture and Rural Development addressed to the Chief Executive Officer of the Free State Development Corporation. The letter referred to the Executive Committee of the Free State Government (EXCO) resolution nr 62/2012 dated 13 June 2012 to implement project. The letter

further states that after EXCO revisited the project a decision was taken to transfer the project to the Free State Development Corporation.

6.3.1.15. The Free State Development Corporation Board at their board meeting of 27 May 2014 (Item 01/2014/80) approved the take-over. The Company Secretary was instructed to conduct a high-level due diligence of the project and table a report at the next Board meeting. The Board will then decide on an appropriate project business model.

6.3.2. Whether or not the contents of the agreement between the Department and the Private Company were adhered to in that the Department implemented appropriated monitoring and management procedures in respect of financial, performance, budget evaluation and expenditure control

6.3.2.1. The Department submitted a letter dated 4 March 2014 from the Department of Water Affairs that letter refers to a request of 73,000 cubic meters of water from boreholes for stock watering. The letter indicates approval and registration of the water use.

6.3.2.2. The Department also submitted an electricity agreement between ESTINA and ESKOM signed on 1 April 2014 for the supply of electricity to the farm Krynaauwslust.

6.3.2.3. The Department submitted an undated list of 80 names of beneficiaries. The list contains the names, identity numbers (15 beneficiaries' identity numbers were not filled in on the list) and addresses for the beneficiaries. Only 62 copies of the beneficiary's identity documents were attached to the list.

6.3.2.4. An AGRIBEE entity (Mohoma Mobung CIPC Registration Number 2013/189418/07) was only incorporated on 11 October 2013; the only director

registered in the entity is Mr. Vasram from Estina. None of the current beneficiaries are listed as directors of the AGRIBEE entity.

- 6.3.2.5. An AGRI-BEE company was registered originally as Zayna Investments Pty Ltd (CIPC Registration Number 2012/037526/07) with Mr. Frans Oupa Mokoena as custodian of 51% shareholding. The name was changed in August 2012 to Mohoma Mobung Dairy Project (Pty) Ltd.
- 6.3.2.6. A copy of the agreement concluded between ESTINA and the Free State Department of Agriculture was submitted. The Agreement was concluded on 5 July 2012. The agreement *inter alia* provides for the following:
- 6.3.2.6.1 ESTINA is obligated in terms of the agreement to conclude Phase 1 of the project. This is described in Annexure A to the agreement and the following must be concluded:
- (i) Land Acquisition;
 - (ii) Environmental Impact Assessment;
 - (iii) Feasibility Study;
 - (iv) Water Reticulation;
 - (v) Electricity Connection;
 - (vi) Set up AGRIBEE entity; and
 - (vii) Include identified beneficiaries in AGRIBEE entity.
- 6.3.2.6.2 In terms of the agreement a project plan in line with ESTINA proposals, which must have milestones and timelines for phase 2 as approved by Department, must be submitted by ESTINA to the Department.

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- 6.3.2.6.3 ESTINA is obliged in terms of clause 6.12 of the agreement to carry out its entire obligation in line with the Department's policies, procedures, protocols and directives.
- 6.3.2.6.4 In terms of clause 7.3 of the agreement the Department will identify the beneficiaries of the project.
- 6.3.2.6.5 Clause 8.1.1 of the agreement states that ESTINA warrants that it is a partner to PARRAS (India).
- 6.3.2.6.6 The agreement in clause 9.1 states that the Department will implement appropriate monitoring and management procedures.
- 6.3.2.6.7 In terms of clause 9.3 of the agreement ESTINA must submit on a monthly basis financial reports and on quarterly basis performance reports must be submitted.
- 6.3.2.6.8 In terms of clause 13.1 of the agreement an amount of R30 million to execute phase 1 is allocated to the project.
- 6.3.2.6.9 In terms of clause 13.4 of the agreement ESTINA must prepare a budget to be approved by Department and budgets should be revised and updated on a quarterly basis and submitted for approval to the Department.
- 6.3.2.6.10 Clause 13.5 of the agreement prescribes that ESTINA to submit all invoices to Department together with reports in line with Project plan to be paid by the Department within 30 days.
- 6.3.2.7. The Department submitted monthly financial statements drafted and submitted by ESTINA for the periods of August 2012 to February 2013, April to July 2013 and September – December 2013.

- 6.3.2.8. The Department further submitted quarterly financial statements drafted and submitted by ESTINA for the periods of July 2012, March 2013 and September 2013 as well as a Cash flow report for August to September 2013.
- 6.3.2.9. The Department was requested to submit documents in respect of the capital injection by ESTINA as per clause 6.2 of the agreement that states R228 million as obligation of ESTINA. The Department did not submit any documentation to substantiate whether or not the agreement was adhered to.
- 6.3.2.10. The financial statements submitted were analysed. No supporting documentation was submitted to verify the correctness of the financial statements. However from the financial statements the analysis of the statements indicated that ESTINA made the following investments

Date of Transaction	Investment/ Withdrawal
September 2012	250,000.00
October 2012	3,750,000.00
November 2012	850,000.00
December 2012	250,000.00
January 2013	650,000.00
February 2013	223,0000.00
April 2013	4,650,000.00
May 2013	2,000,000.00
June 2013	875,000.00
July 2013	5,444,000.00
August 2013	3,513,300.00
September 2013	7,698,000.00
October 2013	4,500,000.00
November 2013	5,704,999.00
TOTAL	42,365,999.00

December 2013 (Withdrawal ESTINA)	(21,200,000)
TOTAL	21,165,999

6.3.2.11. The Department was requested to submit documents relating to the implementation of appropriate monitoring and management procedures. The agreement further stated that ESTINA must carry out their obligations in line with the Department's policies, procedures, protocols and directives. The Department was requested to indicate the measures in place to ensure adherence to the clause in the agreement. The Department did not submit any documentation to substantiate whether or not the measures are in place.

6.3.2.12. The Department was requested to submit copies of all invoices submitted by ESTINA to the Department with reports in line with the Project plan and payment documentation for the invoices paid. The department submitted documentation on 6 bulk payments made to ESTINA. The substantiating documentation attached to the payment authorisation included only the project proposal and agreement signed between ESTINA and the Department. The following payments were by the Department to ESTINA made:

Nr	Authorisation Date	Payment Date	Amount
1	11 June 2012	11 June 2012	30000000.00
2	16 April 2013	16 April 2013	34950000.00
3	25 April 2013	25 April 2013	30000000.00
4	29 April 2013	29 April 2013	19050000.00
5	10 December 2013	10 December 2013	29950000.00
6	21 July 2014	21 July 2014	30000000.00
	TOTAL		173950000.00

6.3.2.13. The Department did submit a letter from ESTINA dated April 2014 claiming an amount of R136, 252, 652 as the shortfall which according to the letter they are entitled to as a result of the cancellation of the agreement. Clause 15.3 of the agreement states that ESTINA shall be entitled to payment in full for the services delivered. The shortfall was explained in the letter as follows:

Date	Commitment	Received	Outstanding
9 July 2012	114,000,000.00	30,000,000.00	84,000,000.00
18 April 2013	114,000,000.00	113,950,000.00	50,000.00
1 April 2014	114,000,000.00	0	114,000,000.00
Total	342,000,000.00	143,950,000.00	198,050,000
Invoices submitted for payment	280,202,652.00	143,950,000	136,252,652.00

- 6.3.2.14. The agreement states that ESTINA must carry out their obligations in line with the Department's policies, procedures, protocols and directives. The Department was requested to submit proof of measures in place and executed to ensure adherence to the agreement as well as adherence to the Treasury requirement of value for money during procurement of state assets. No supporting evidence in any form was submitted by the Department.

6.3.3. Whether or not the prices for goods and services procured were inflated and specific alleged expenses in respect of construction, processing equipment, procurement of cows and administration costs

- 6.3.3.1. The Department submitted the following expenditure in terms of the Project agreement:

Expenditure	Submitted by MEC Written response to questions in Free State Legislature
Planting input	319,290.00
Labour Cost	1,309,097.00
Silage Bunker	5,000,000.00
Gravel Road	1,200,000.00
Cattle Shed	500,000.00
Security Gate and House	2,600,000.00
Veterinary Laboratory	300,000.00

Cattle Feed Plant	7,350,000.00
Milking Parlour: 72 point rotary including processing plant for 20,000 litres per day	30,050,000.00
Purchase of Farm Equipment	8,380,494.00
Dairy Cows (351 animals consisting of 57 Breeding cows, 62 pregnant heifers, 70 heifers 12 months+, 77 heifers 9-12 months, 85 heifers 6-9 months)	6,212,000.00
Dairy Equipment, Pasteurizer, Irrigation Equipment	37,779,613.00
Land Surveyor, Agriculturists, Accounting Fees, Office Equipment, Insurance, Salaries and Wages	12,000,000.00
TOTAL	113,000,494.00

6.3.3.2. The Department was further requested to submit documentation on measure in place to ensure acquisitions are in line with treasury prescripts relating to value for money but no documentation to substantiate any measures were submitted.

6.3.3.3. An analysis of the financial statements submitted by the Department reveals that the following Director's and other salaries were paid from September 2012 to December 2013. The incorporation documents list one director.

Date	Directors	Salaries other
September 2012	48,351.38	
October 2012	96,702.76	
November 2012	48,351.38	3,960.00
December 2012	23,721.28	7,460.00
January 2013	23,721.28	
February 2013	2,3721.28	3,500.00
April 2013		8,000.00

May 2013		27,721.28
June 2013		27,721.28
July 2013	100,000.00	27,721.28
August 2013	123,721.28	50,248.32
September 2013	23,721.28	24,131.00
October 2013	23,721.28	80,309.56
November 2013	23,721.28	50,500.00
December 2013		129,156.28
TOTAL	559454.48	440429.00

- 6.3.3.4. An analysis of the financial statements submitted by the Department reveals that the following that the following consultancy fees were paid. No explanations were submitted for the services delivered.

Date	Professional	Agriculture	Surveyor	Legal
September 2012				1,500.00
October 2012	100,000.00	36,480.00	94,711.20	3,780.00
November 2012	130,000.00	72,960.00	48,080.00	46,590.00
December 2012	70,000.00	36,480.00		
January 2013	170,171.00			
February 2013	95,122.27	32,745.36	22,386.38	
April 2013	33,386.10	63,745.00		
May 2013	227,320.00	33,858.00		
June 2013		48,800.54	57,000.00	
July 2013	100,000.00			
August 2013	210,854.41	54,042.00		
September 2013		45,000.00	13,680.00	
October 2013	60,000.00			
November 2013	60,664.62			
December 2013	65,000.00			

TOTAL	1,322,518.40	424,110.90	235,857.58	51,870.00
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- 6.3.3.5. An analysis of the financial statements submitted by the Department reveals that the following reveals that the following assets were acquired:

Date	Tractors	Equipment	Vehicles
October 2012	2,359,800.00	51,3000.00	
November 2012		42,846.79	
December 2012		471,007.40	
January 2013		1,558,352.51	
February 2013	411,540.00		
April 2013		663,952.28	
May 2013		113,430.00	538,537.00
June 2013		35,883.47	172,436.11
July 2013		3,599.89	
August 2013	112,860.00	16,847.77	
September 2013		694,959.63	
October 2013		436,745.87	
November 2013			
December 2013	17,978.29		
TOTAL	2,902,178.29	4,550,625.61	710,973.11

6.3.4. Whether or not environmental legislation was adhered to during the farming operations

- 6.3.4.1 The Department submitted Environmental Authorisation [EA] from the Department of Environmental Affairs dated 12 May 2013. The EA indicates the activity as the establishment of Dairy Farm near the town of Vrede in the Free State. The activities approved in the EA are:

- 6.3.4.1.1 Construction of infrastructure for the concentration of animals for the purpose of commercial production;
 - 6.3.4.1.2 Construction of a road outside urban areas;
 - 6.3.4.1.3 Construction of bridges, dams and infrastructure within 32 meters of a watercourse; and
 - 6.3.4.1.4 Transformation of vacant land to residential, retail, commercial, recreational, industrial or institutional outside an urban area.
- 6.3.4.2 The Department also submitted Environmental Authorisation [EA] from the Department of Environmental Affairs dated 28 October 2013. The EA indicates the activity as permission to cultivate 1000ha of virgin soil for dry land. Permission is subject to the implementation of soil conservation works, a proper runoff to control storm water furrows and contour banks.

6.4. Independent Evidence Obtained

6.4.1. Whether or not the Treasury prescripts in respect of a Public Private Partnerships were adhered to and whether or not the contribution of 40% of the funds for an allocation of 49% of the shares in the company was contrary to Treasury prescripts

- 6.4.1.1. During a briefing by National and Provincial Treasuries to Parliament on Free State and KwaZulu-Natal 2012/13 budget performance the following was presented in respect of the Vrede Dairy Project:

“Mr. Lees said that one of the “own revenue enhancement initiatives” referred to the production of dairy facilities and other agricultural products, and asked for an explanation of what that meant. Ms. Rockman said this referred to the Vrede

dairy, where the Department of Agriculture was contributing R347m in three equal installments over three years. Further details could be provided, if required.

Ms. Rockman said that both she, as Director General in the office of the Premier, and the Acting Director General of COGTA, had signed off on the project as accounting officers. The total expenditure to date was R44m. The Auditor-General and Public Protector were looking into the matter, and should be allowed to complete the process.”⁹

- 6.4.1.2. During a briefing by National and Provincial Treasuries to Parliament on Free State and KwaZulu-Natal on third quarter 2013/14 expenditure the following was presented in respect of the Vrede Dairy Project

“There had been under-spending on the conditional grants by the Department of Agriculture, with only 52.4% of the R207.4 million budget spent, with very little on the Comprehensive Agricultural Support Programme (CASP).

Mr. Lees indicated that no mention was made of in the Free State report on wasteful expenditure for the Vrede Dairy Project. He asked what it was costing the province, and if it was included in the figures presented.

Mr. Mahlatsi stated that roughly R140 million had been spent on the Vrede Dairy Project. He visited the Vrede Dairy farm and stated that the media reports had not provided a complete picture of what was happening, as there was activity, although he could not comment on all issues.”¹⁰

- 6.4.1.4 The National Treasury: Accounting General’s (Accounting General) draft report dated January 2013 was received by the Public Protector on 24 July 2014. The Accounting General’s mandate was the following:

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- 6.4.1.4.1 Establish if the project was an approved PPP arrangement or a sole provider engagement;
- 6.4.1.4.2 Verify the supply chain management process followed in appointing the service provider, Estina/Paras;
- 6.4.1.4.3 Verify how much the Free State Department of Agriculture committed to the project and the source of the funds, and if there was any capital injection by the service provider;
- 6.4.1.4.4 Investigate the reasons and supporting documentation for the BAS payments made in excess of the R30 million, which was said to be available from the department;
- 6.4.1.4.5 Verify if there were any beneficiaries identified for the AGRIBEE and if so, who they were;
- 6.4.1.4.6 Establish through liaising with AGRI SA whether there is value for money to the State on this project; and
- 6.4.1.4.7 Establish the current state of the project and provide recommendations.
- 6.4.1.5 The Accounting General's draft report dated January 2013 found that the feasibility of the project as set out in the feasibility study, and project plan submitted by ESTINA that all three documents lacked the information required to carry out a proper analysis of the project; for example, information on the detailed costing for equipment. This feasibility study is more an academic study than a feasibility study and therefore contains a significant amount of jargon.
- 6.4.1.6 The Accounting General found that the agreement between the Department and ESTINA was neither a PPP nor a sole provider arrangement. The Accounting General found that the accounting officer did not follow any supply chain management process. The accounting officer signed an authorisation to deviate from the prescribed contrary to prescripts.

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- 6.4.1.7 The Accounting General made the following recommendations to the Department:
- 6.4.1.7.1 That disciplinary action is taken against Mr Thabethe (the Accounting Officer) for his part in concluding this agreement with Estina/Paras. Mr Thabethe did not adhere to the requirements of the PFMA and no supply chain management process was followed prior to entering into the agreement with Estina. Further, Mr Thabethe committed the department financially without ensuring that the department had the funds available to fund this project. The effect of this is that the department is currently struggling to meet its financial commitments in respect of this project.
- 6.4.1.7.2 That disciplinary action is taken against Ms. Dlamini the Chief Financial Officer of the Department. As the head of the Department's finance division, Ms. Dlamini should have ensured that she did not disburse funds to Estina without ensuring that the proper financial oversight controls were in place.
- 6.4.1.7.3 That no further funds are invested in the project until all of the risk factors set out in this report are addressed.
- 6.4.1.8 The Auditor General's media release on 26 November 2014 on the Free State PFMA 2013-14 audit outcome highlights remarks as follows:
- "The financial health of the province has deteriorated since the previous years. Due to inadequate budgetary controls, nine auditees (50%) encountered serious concerns relating to their financial sustainability."*
- 6.4.1.9 The Auditor General's report: General Report on the Audit outcomes of the Free State: PMFA 2013-14 in respect of the Department reported an unqualified audit with 10 findings.

- 6.4.1.10 The Auditor General also reported that the Department had material findings on supply chain management and regressed from having not material findings in the prior year to material findings on supply chain management in the current year.¹¹
- 6.4.1.11 The Auditor General reported that the main reason for incurring irregular expenditure is that credible procurement plans are not in place. This results in *inter alia* invalid deviations utilised. As a result there is a lack of transparency during the procurement process and no competitiveness.¹²
- 6.4.1.12 The Auditor General reported that the Department did report that irregular expenditure is still being investigated and this may result in the Department's irregular expenditure being significantly higher than those disclosed.¹³
- 6.4.1.13 The Auditor General also reported¹⁴ the following:
- "There is an increasing trend where auditees employ the strategy of delegating their functions to another entity, appointing them as implementing agents. Fair, equitable and transparent procurement processes are not always followed to appoint these implementing agents."*
- 6.4.2. Whether or not the contents of the agreement between the Department and the Private Company were adhered to in that the Department implemented appropriated monitoring and management procedures in respect of financial, performance, budget evaluation and expenditure control**
- 6.4.2.1. The Mail & Guardian newspaper reported the following in respect of the identification of beneficiaries for the project¹⁵:

¹¹ General Report on the Audit outcomes of the Free State: PMFA 2013-14 page 27

¹² General Report on the Audit outcomes of the Free State: PMFA 2013-14 page 31

¹³ General Report on the Audit outcomes of the Free State: PMFA 2013-14 page 31

¹⁴ General Report on the Audit outcomes of the Free State: PMFA 2013-14 page 31

¹⁵ 7 February 2014

“Local chair of the African Farmers Association of South Africa (Afasa) in Vrede, Ephraim Dlamini, told amaBhungane an urgent meeting was called in October last year by Mosebenzi Zwane, the former agriculture MEC. The hall was full of people, most I didn't know who they are. We were told to bring a copy of our IDs and you submitted names and addresses. Zwane gave a good speech about how we are going to be owners of this farm because we will own 51%. He begged us not to sell shares to anyone even if they offer millions. I warned people not to sign anything without fully understanding what is going on. What breaks his heart, Dlamini said, is that people who had few cows sold them because they were promised they were going to get cows from the dairy, "but so far not a single person has received anything. He said beneficiaries appeared to have been "already chosen" by the politicians.”

- 6.4.2.2. The Auditor-General reported on Key Challenges in Agriculture Department's Audit Report 2013 to Parliament as follows:

“The internal audit function was a critical area for the Department. Intervention was required for the drivers of internal controls; these being Leadership, Financial and Performance Management, and Governance...The AGSA had established that in terms of the generic indicators, there was no alignment between national and provincial departments...”¹⁶

- 6.4.2.3. The Accounting General informed¹⁷ the Public Protector that a report on the Vrede Dairy Project was drafted and submitted for comments during January 2013 to the Minister of Finance, the Free State Premier and the Member for the Executive Council: Free State Department of Agriculture and Rural Development.

¹⁶ 8 October 2013 Minutes of the Meeting

¹⁷ Email from Treasury: Accounting General dated 25 April 2014

- 6.4.2.4. Department of Agriculture and Rural Development 2012/2013 Annual Report dated 31 May 2013 the Department reported that the Vrede Dairy project was 25% implemented and that no challenges were experienced.¹⁸ The Department further reported that an amount of R30 million was transferred to the project during the 2011/2012 financial year.¹⁹
- 6.4.2.5. The Accounting General's draft report dated January 2013 found that contrary to section 38(2) of the PFMA, the accounting officer of the Department committed the department to a liability for which funds had not been appropriated prior to implementation.
- 6.4.2.6. The Accounting General further supported the finding of the Free State Auditor General that the accounting officer of the Department did not maintain appropriate measures to ensure that funds transferred to entities are applied for their intended purposes. The Accounting General was not able to ascertain whether or not ESTINA has made any financial contribution towards this project.
- 6.4.2.7. The Auditor General in his General Report on the Audit outcomes of the Free State: PMFA 2013-14 found in respect of the Department that annual reports and performance reports on programmes and objectives were not useful or reliable.²⁰
- 6.4.2.8. The Auditor General reported that the most common findings on the usefulness of the information as information not being relevant to service delivery objectives, not measurable or well defined.
- 6.4.2.9. The Auditor General reported that the most common findings on the reliability of the information as the information not being accurate, complete or valid.
- 6.4.2.10. The Auditor General also reported²¹ the following:

18 Page 98

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20 General Report on the Audit outcomes of the Free State: PMFA 2013-14 page 23

21 General Report on the Audit outcomes of the Free State: PMFA 2013-14 page 31

“There is an increasing trend where auditees employ the strategy of delegating their functions to another entity, appointing them as implementing agents. Fair, equitable and transparent procurement processes are not always followed to appoint these implementing agents. Furthermore, once payments are made no further monitoring is done by auditees to ensure that fair, equitable and transparent procurement processes are followed by the implementing agents so that the best price is paid when they spend money on behalf of the auditee. The use of implementing agents is especially of concern in light of the poor financial health of the province since the best prices are not always paid for goods and services. In addition, management fees have to be paid although more than half (57%) of the provincial budget is already spent on employee cost, while it is expected that government employees should perform the duties delegated to implementing agents. This matter is currently disclosed as possible irregular expenditure under investigation at the departments of Agriculture and Rural Development, Education and Economic Development, Tourism and Environmental Affairs.”

6.4.2.11. The Auditor General reported that key control areas that require attention is the review and monitoring of compliance at financial statement level, the annual performance report as well as compliance with legislation.²² The root causes of audit findings were based on identifying the internal controls that failed to prevent or detect non-compliance.

6.4.3. Whether or not the prices for goods and services procured were inflated and specific alleged expenses in respect of construction, processing equipment, procurement of cows and administration costs

²² General Report on the Audit outcomes of the Free State: PMFA 2013-14 page 36

6.4.3.1. According to the website²³ of the SA Holstein Breeders Association the sale results during 2013 for two separate auctions for stud animals were the following:

Pregnant Heifers: between R11, 280 and R14, 651 per heifer; and

Breeding Cows: between R13, 196 and R17, 702.

6.4.3.2. According to the SA Holstein Breeders Association the prices of heifers older than 12 months average at R8000 per heifer, heifers between 9 and 12 months average at R6000 per heifer and heifers between 6 and 9 months average at R5000 per heifer.

6.4.3.3. The SA Holstein Breeders association indicated that currently the price for a breeding cow from the top 10% of the gene pool is approximately R18, 000.00 per cow.

6.4.3.4. According to the SA Holstein Breeders Association the pricing for milking parlours are calculated per milking point at a maximum of R100, 000.00 per milking-point at current value. A 72 point milking parlour should be a maximum price of R7, 2 million.

6.4.3.5. The Accounting General's draft report dated January 2013 found the following in terms of the projected costs of items in the feasibility study and project plan:

"If the processing plant relies solely on its own production, it is not worth the capital outlay projected in the costing. Even if the production is as assumed in the project, namely 22 500 litres per day, a batch pasteurizer can be installed for approximately R450 000, which is substantially less than the R60 million envisaged;

²³ <http://www.saholstein.co.za/Shows-Results.htm>

The same applies to the other dairy equipment – the projected costing is far too high for the quantity of milk to be processed;

In terms of the UHT milk plant budgeted for in the project proposal, this plant will not be viable for the production of the dairy project alone (less than 30 000 litres per day). Research indicates that a plant able to process 120 000 l/day would require an investment of approximately R65 million in equipment and R30 million in buildings and stores, totalling R95 million. For a further R20 million investment, an additional line could be installed, doubling the production capacity to 240 000 l/day. These figures demonstrate that the R149 million budgeted in the project for the envisaged UHT plant is substantially above cost”

6.4.3.5 The Daily News reported on 13 March 2013 as follows:

“Tractors worth millions stand “baking in the sun” and being stripped of their parts instead of helping poor households increase food production as they were supposed to do, MPs heard on Tuesday. The Department of Agriculture, Forestry and Fisheries came in for a mauling as it presented its quarterly performance report in Parliament. It was accused of vague reporting and failing to verify that money spent had resulted in concrete benefits and physical delivery. ANC MP Salam Abram kick-started the grilling of officials by saying the quarterly report they had presented was “unacceptable” and that it “naturally asks more questions than the answers that are supposed to have been provided”. He had been to a showground in the agricultural hub of Vrede in the Free State, where he had found the tractors standing idle. “I counted 24 Massey Ferguson 268s, the smaller version, 290, the medium version, and I think the largest one is 470 – 24 of them. It’s in a camp where any person can walk through, any person can take from it whatever they want to take and I was told a good few of the batteries of those tractors have already gone,” a fuming Abram said. Prices for these tractors,

obtained on the internet, range from R268 000 to R435 000 each. Abram said he had seen trailers, ploughs, fertiliser distributors and “everything that a poor person would have loved to have”. They had been there since October 2012.”

- 6.4.3.6 The Report of the Portfolio Committee on Agriculture, Forestry and Fisheries on the Oversight Visit to the Free State Province on 29 July to 02 August 2013 states the following:

“On 5 March 2013, the Department of Agriculture, Forestry and Fisheries (hereinafter referred to as the Department) were requested by the Portfolio Committee on Agriculture, Forestry and Fisheries to present its progress report regarding the implementation of the Mechanisation Programme and the allocation of tractors in the various Provinces. The purpose of the oversight visit was inter alia to determine the effectiveness in which the Department’s Mechanisation Programme funds were utilised in the Free State Province.

The Mechanisation Implementation Plan was approved by the Accounting Officer of the national Department of Agriculture, Forestry and Fisheries on 30 March 2012. It was reported that 72 Massey Ferguson tractors inclusive of implements (350 implements, e.g. trailers, ploughs, discs, planters, fertiliser spreaders and chemical sprayers) were delivered, assembled and signed off for inspection by 23 August 2012. Tractor packages were allocated to the different provincial Districts through established criteria that are linked to arable land on land reform farms, commonages, Ilima/letsema projects and in communal lands.”

- 6.4.4. **Whether or not environmental legislation was adhered to during the farming operations**

- 6.4.4.1 The Accounting General found that environmental issues were not addressed in the feasibility study of October 2012.

- 6.4.4.2 The Department submitted a new feasibility study and business plan dated April 2014.
- 6.4.4.3 The Minister of Water Affairs did investigate an environmental issue after members of the public complained to the department about an uncovered mass grave of thirty cattle carcasses that had died of unknown diseases on the bank banks of a river, which exposed the river to serious pollution.
- 6.4.4.4 The Minister issued a press release that the Department of Water Affairs instructed the owners of the Estina Dairy in Vrede, Free State, to exhume an estimated 30 dead cattle they buried on the banks of a local river and incinerate them. The department is also considering laying charges against the dairy for contravening the National Water Act for dumping dead cattle within meters of the stream.

7. MEASURING CONDUCT AGAINST THE RULES

- 7.1 **Whether or not the Treasury prescripts in respect of a Public Private Partnerships were adhered to and whether or not the contribution of 40% of the funds for an allocation of 49% of the shares in the company was contrary to Treasury prescripts**

- 7.1.1 A PPP is a contract between public sector and private sector, where the private sector party performs an institutional function or uses state property in accordance with certain specifications from the public sector institution.
- 7.1.2 There are certain requirements before a government can successfully use Public-Private-Partnerships (PPP) to procure public services infrastructure. A detailed legislative framework is in place through the PMFA and PFMA regulation 16 of the Regulations.
- 7.1.3 With the adoption of the final Constitution in 1996, it was a constitutional prerequisite that procurement must take place in terms of a system, which is fair, equitable, transparent, competitive and cost effective.²⁴
- 7.1.4 Section 195 of the Constitution provides that the public administration must be governed by principles, which include a high standard of professional ethics, efficient, economic and effective use of resources, and the impartial provision of services.
- 7.1.5 Practice Note 2 of National Treasury makes it clear that a PPP is not a simple outsourcing of functions where substantial financial, technical and operational risk is retained by the institution or a divesture of state assets and/or liabilities. PPP's may involve a degree of capital contribution by the institution to the initial costs of the project.
- 7.1.6 Only an accounting officer may enter into a PPP agreement on behalf of the department, and only with the prior written approval of the national Treasury.
- 7.1.7 The evidence show that a tender was never advertised for the establishment of the project and an agreement was concluded on an unsolicited bid received. The

²⁴ Section 217 of the Constitution

lack of due diligence in evaluating the unsolicited bid is also clear from the evidence.

- 7.1.8 To determine whether a proposed PPP agreement is in the best interests of a department, the accounting officer must prepare a feasibility analysis. It should, among other things, explain the strategic and operational benefits of the PPP agreement and assess how the agreement will assist in meeting the department's strategic objectives. The details of the processes to be followed are specified in regulation 16 of the Regulations.
- 7.1.9 The Constitutional Court in the Allpay case²⁵ stressed the importance of procedural requirements and the adherence to these in order to ensure fair, equitable, transparent, competitive and cost effective procurement system.
- 7.1.10. The evidence shows that there was a deviation from the procurement process and this was not reported as required by the legal framework in respect of procurement. The definition of irregular expenditure includes expenditure related to a PPP without obtaining the prior written approval of the relevant treasury, as required by Treasury Regulation 16.4.2
- 7.1.11. The purpose of the reporting requirement is clearly to provide the National Treasury, as the custodian of public funds, with an opportunity to note, evaluate and, if necessary, intervene in the procurement process. The failure to report the deviation therefore accordingly deprived the National Treasury from the intended opportunity.
- 7.1.12. The Department submitted the agreement dated 5 July 2012 entered into and between Department and ESTINA. The feasibility study however is dated October

²⁵ Allpay Consolidated Investment Holdings (Pty) Ltd and Others v Chief Executive Officer of the South African Social Security Agency and Others (2014 (1) SA 604 (CC))

2012. A further and more comprehensive feasibility study dated April 2014 was submitted by the Department.

- 7.1.13. The previous MEC for Agriculture on 22 March 2012 during the 2012 Budget Vote Speech of the Free State Department of Agriculture and Rural Development, reported on the fact that the Thabo Mofutsanyana district Municipality area was identified *“as a dairy hub and an amount of R17.0 million is allocated for this development. Vrede, QwaQwa and Ficksburg towns will benefit from this initiative.”*
- 7.1.14. A feasibility study is needed for the accounting officer to prepare a feasibility analysis to explain the strategic and operational benefits of a proposed agreement and assess how the agreement will assist in meeting the department's strategic objectives.
- 7.1.15. The MEC for the Department explained the discrepancy between the share distribution and the funds to be contributed. The MEC submitted that Estina/Paras will obtain 49% of the shareholding (only contributing 40% of the funds) and will provide services and professional fees. The MEC explained that the management and administration costs of the project contributed for the difference of 9%.
- 7.1.16. The Accounting General informed²⁶ the Public Protector that a report on the Vrede Dairy Project was drafted and submitted for comments during January 2013 to the Minister of Finance, the Free State Premier and the Member for the Executive Council: Free State Department of Agriculture and Rural Development.
- 7.1.17. The accounting officer of the Department proceeded to pay a further R141,950 million to ESTINA for the project in contradiction to the recommendation of the Accounting General.

26 Email from Treasury: Accounting General dated 25 April 2014

- 7.1.16. The Financial Statements and payment vouchers submitted by the Department reveal that the Department has contributed R173, 950, 000 while ESTINA's contribution amounts to R21, 165, 999.00. This could not be verified nor could the Accounting General verify any contribution made by ESTINA.
- 7.1.17. The cession and assignment assigned from the Phumelela Local Municipality of all rights, title, interest and obligations in the Farm Krynaauwslust to Department was signed during December 2012. The Department registered a notarial lease for a period of 99 years to ESTINA and not to the Agri-BEE company, Mohoma Mobung Dairy Project (Pty) Ltd.
- 7.2 Whether or not the contents of the agreement between the Department and the Private Company were adhered to in that the Department implemented appropriated monitoring and management procedures in respect of financial, performance, budget evaluation and expenditure control**
- 7.2.1 Section 38 of PFMA requires that the accounting officer implements and maintains effective, efficient and transparent systems of financial and risk management and internal control. Section 3.1.10 of the Regulations requires risk management to be regularly monitored and monitoring of risks must be part of the normal operating activities of the Department.
- 7.2.2 Regulation 3.2.1 of the Regulations requires the accounting officer to ensure that a risk assessment is conducted regularly to identify emerging risks for the institution.
- 7.2.3 The Department has a responsibility towards its citizens to expend public finances in an effective, efficient and economic manner. In order to do so, sound financial management practices are required in terms of legislation.

- 7.2.4 The public sector institution must ensure affordability, the transfer of risk and value for money. Risks in a farming environment can involve the market risks, demand or volume risks, operating risks, environmental risks, falling prices, no scope for increasing prices and increased costs of inputs
- 7.2.5 Financial management discipline is designed to address risks and to provide reasonable assurance that in pursuit of the department's mission; *inter alia* the following general objectives are being achieved:
- 7.2.5.1 Executing orderly, ethical, economical, efficient and effective operations;
 - 7.2.5.2 Complying with applicable laws and regulations; and
 - 7.2.5.3 Safeguarding resources against loss, misuse and damage.
- 7.2.6 National Treasury Practice Note 2 in respect of PPP's requires that effective monitoring should provide the basis for reviewing actual private party performance against the output specifications and other obligations contained in the agreement.
- 7.2.7 The treasury prescripts clearly require effective monitoring and actual reviewing of performance. No such documents and/or correspondence could be provided and I could find no evidence or indication that a proper monitoring system was in place to evaluate the performance of the project.
- 7.2.10. The evidence submitted by the Department included an undated Project proposal, beneficiary list and beneficiary agreement signed by one beneficiary.
- 7.2.10. The beneficiary documents submitted by the Department was undated and therefore from the documents it could not be determined when the beneficiaries were identified and what criteria was used to identify them. From press reports

mentioned it appeared that the beneficiaries were originally identified during October 2013 and no criteria was used to identify them.

- 7.2.12. The Department further submitted a document drafted by ESTINA and dated June 2013 projecting milestones for phases 2 and 3 of the project. A cash flow projection by ESTINA for the period August 2012 to September 2013 was submitted. Quarterly progress reports by ESTINA for periods March 2013, June 2013 and September 2013 was submitted and monthly financial statements received from ESTINA for the period July 2012 to December 2013 was submitted by the Department.
- 7.2.13. No supporting evidence in the form of actual invoices/receipts was submitted to substantiate the disbursements as claimed on the invoices submitted.
- 7.2.14. The Financial Statements as submitted by the Department were analysed and converted to accounting statements. It should be noted that the figures could not be verified as no documentation in respect of expenses were submitted. As indicated the payment vouchers of the Department did not contain any supporting documentation such as invoices, proof of purchase, etc. The Financial Statements drafted by ESTINA and submitted by the Department reveal the following accounting balances:

Trial Balance: 1 April 2013 to 31 March 2014			
2012/2013	Account	Debit	Credit
-61901800.00	Sales		
-30000000	Grant Received		113,950,000.00
-7980000	Estina Investment		13,185,299.00
61901800.00	Cost of Sales		
6507.80	Accounting Fees	2,050.00	
11765.26	Bank Charges	12,786.36	
60293.47	Admin Expenses	709,446.45	
51870.50	Legal Fees		
11484.47	Service Fees	10,992.04	
0.00	Electricity and Utilities	99,998.95	

9218.41	Insurance	84,835.93	
240848.08	Directors Salaries	318,606.40	
0.00	Mechanise Implementation	91,690.46	
0.00	Office Equipment	256.00	
178665.36	Consultant Agriculture	245,445.54	
163177.58	Consultant Surveyor	70,680.00	
284290.73	Seed and Fertiliser	1,463,107.46	
71000.00	Diesel	907,753.95	
565293.27	Professional Fees	757,225.13	
14920.00	Salaries	425,509.00	
36857.11	Travel Local	183,850.05	
110930.96	Travel Overseas	7,422.64	
-36162877.96	Net Profit	121,743,642.64	
	TOTAL	127135299.00	127135299.00
-36,162,877.96	Net Profit	0.00	121743642.64
0.00	Accumulated Surplus/Deficit	0.00	36162877.96
	Assets	0.00	0.00
2,892,180.00	Tractors	3378301.11	0.00
2,585,206.70	Farm Equipment	4306404.18	0.00
39,275.34	Office Equipment	115680.64	0.00
	Motor Vehicles	710973.11	0.00
	Bank Account		142,889,124.64
	Investment		2,150,820.19
	Inventory	183,890,000.00	0.00
	Live-Stock	247,156.34	0.00
499137.33	Creditors	110,297,950.05	0.00
		302,946,465.43	302,946,465.43

7.3 Whether or not the prices for goods and services procured were inflated and specific alleged expenses in respect of construction, processing equipment, procurement of cows and administration costs

7.3.1 Section 81(1)(b) of the PFMA prescribes that “An accounting officer ... commits an act of financial misconduct if that accounting officer willfully or negligently- ... makes or permits an unauthorized expenditure, an irregular expenditure or a fruitless and wasteful expenditure.”

7.3.2 Government has a responsibility towards its citizens to expend public finances in an effective, efficient and economic manner. In order to do so, sound financial

management practices are required in terms of legislation, thus placing a high burden of accountability on all civil servants and specifically accounting officers.

- 7.3.3 The summary of the evidence obtained in respect of the breeding cows and heifers procured indicate that actual payment was R6, 212 million. The complainant submitted that the amount could maximum be R3, 374 million.
- 7.3.4 The SA Holstein Breeders association agreed in principle with the Complainant. They indicated that currently the price for a breeding cow from the top 10% of the gene pool is approximately R18, 000.00 per cow.
- 7.3.5 The animals bought for the project ranging from 6 month old animals to breeding cows were bought at an average price of R17, 698.00 per animal.
- 7.3.6 The Complainant further alleged that the National Department of Agriculture supplied the provincial government with equipment that included tractors and related equipment for planting and maintaining crops to the value of R40+ million. This was substantiated with independent evidence.
- 7.3.7 The Department submitted that expenses were incurred in respect of farm equipment procured.
- 7.3.8 The Department submitted that a milking parlour with a 72 point rotary including processing plant for 20,000 litres per day were procured for the amount of R30, 050, 000.00. The SA Holstein Breeders Association submitted that the pricing for milking parlours are calculated per milking point at a maximum of R100, 000.00 per milking point at current value. A 72 point milking parlour should be a maximum price of R7, 2 million. The Accounting General found in his report that a batch pasteuriser pricing is a maximum of R450, 000.00.

7.3.9 The Department further submitted that labour costs amounted to R1, 309, 097.00. This figure was submitted to the Legislature during November 2013 in reply to a question asked. The financial statements submitted by the Department up to December 2013 only indicate Director's salaries and other salaries in the amount of R999, 883.48.

7.3.10 The Department further submitted that Land Surveyor, Agriculturists, Accounting Fees, Office Equipment, Insurance, Salaries and Wages: amounted to R12, 000, 000.00. This figure was submitted to the Legislature during November 2013 in reply to a question asked. The financial statements submitted and analysed indicate the following amounts:

Expense	Amount
Accounting Fees	8,557.80
Bank Charges	24,551.62
Admin Expenses	769,739.92
Legal Fees	51,870.50
Service Fees	22,476.51
Electricity and Utilities	99,998.95
Insurance	94,054.34
Directors Salaries	559,454.48
Consultant Agriculture	424,110.90
Consultant Surveyor	233,857.58
Professional Fees	1,322,518.40
Salaries	440,429.00
Travel Local	220,707.16
Travel Overseas	118,353.60
Director's and other salaries	999,883.48
	5,390,564.24

7.3.5 No supporting evidence in the form of actual invoices/receipts was submitted to substantiate the disbursements as claimed on the financial statements drafted by ESTINA and submitted to the Department.

7.4 Whether or not environmental legislation was adhered to during the farming operations

- 7.4.1 Environmental Authorisation was obtained by ESTINA from the Department of Environmental Affairs for the construction of infrastructure for the concentration of animals for the purpose of commercial production, bridges and dams.
- 7.4.2 Environmental Authorisation was also obtained by ESTINA from the Department of Environmental Affairs to cultivate 1000ha of virgin soil subject to certain conditions.
- 7.4.3 The Minister of Water Affairs did issue a press release after investigating an uncovered mass grave of thirty cattle carcasses that had died of unknown diseases on the bank banks of a river, which exposed the river to serious pollution.
- 7.4.4 The Minister instructed the owners of the Estina Dairy in Vrede, Free State, to exhume an estimated 30 dead cattle and incinerate them.
- 7.4.5 The Minister also indicated that the Department of Water Affairs is considering criminal charges against the dairy for contravening the National Water Act for dumping dead cattle near the stream.

8 FINDINGS

Having considered the evidence uncovered during the investigation against the applicable law and prescripts, I intend to make the following findings:

- 8.1 **Whether or not the Treasury prescripts in respect of a Public Private Partnerships were adhered to and whether or not the contribution of 40% of the funds for an allocation of 49% of the shares in the company was contrary to Treasury prescripts**

- 8.1.1 The evidence provided by the Department in respect of the process followed to conclude the agreement with ESTINA supported the conclusion that the prescripts in respect of the procurement of the agreement was not adhered to. This was confirmed by the Accounting General's report dated January 2013 and constitutes maladministration
- 8.1.2 The Accounting General informed the Public Protector that a report on the Vrede Dairy Project was drafted and submitted for comments during January 2013 to the Minister of Finance, the Free State Premier and the Member for the Executive Council: Free State Department of Agriculture and Rural Development. The accounting officer of the Department proceeded after the recommendation of the Accounting General to pay a further R143, 950 million to ESTINA in respect of the project. This amounted to gross irregularity and maladministration.
- 8.1.3 The evidence discussed above, which includes failure to adhere to Treasury prescripts in respect of procurement and specifically the conclusion of a PPP leaves me with no option other than to conclude that the Department did not maintain a procurement system that is fair, equitable, transparent, competitive and cost effective as required by section 217 of the Constitution and Treasury regulations on SCM. It did not comply with the above basic supply chain management requirements, and thus rendered the conclusion of the agreement improper.
- 8.1.4 The conduct of the accounting officer in concluding the agreement amounts to improper conduct, abuse of power and maladministration. This was confirmed by the report of the Accounting General dated January 2014.
- 8.1.5 The distribution of shares in the Agri-BEE company in relation to the monetary contributions required from the parties to the agreement is irregular and contrary

to Treasury prescripts in respect of PPP agreements and this constitutes maladministration.

8.2 Whether or not the contents of the agreement between the Department and the Private Company were adhered to in that the Department implemented appropriated monitoring and management procedures in respect of financial, performance, budget evaluation and expenditure control

8.2.1 No documents and/or policies or measures were provided by the Department that proper financial control and risk management of the project were in place. I could find no evidence or indication that the accounting officer invoked the provisions of the agreement in respect of the control over the project and this raises serious concern. This concern was supported by the report of the Accounting General and the lack of controls amounts to gross negligence and maladministration.

8.2.2 No supporting evidence in the form of actual invoices/receipts was submitted to substantiate the expenditure as claimed in the financial statements submitted. In fact the payment vouchers for the disbursement of the R173, 950 million to ESTINA were substantiated only by the project proposal of ESTINA/PARAS and the agreement concluded between the Department and ESTINA.

8.2.3 From the above it is clear that this amounts to gross negligence, maladministration and ultimately irregular expenditure in terms of Treasury prescripts.

8.2.4 In terms of the Regulations a PPP agreement does not divest the accounting officer of the responsibility for ensuring that the relevant institutional function is effectively and efficiently performed in the public interest. The evidence I have outlined earlier points to gross irregularities in ensuring the effective and efficient performance of the agreement and resulted in irregular and fruitless expenditure.

8.3 Whether or not the prices for goods and services procured were inflated and specific alleged expenses in respect of construction, processing equipment, procurement of cows and administration costs

8.3.1 The independent evidence submitted indicates that the prices of the processing equipment and the cows were considerably higher than the current market prices. The evidence further confirms that the accounting officer of the Department had no measures in place to ensure proper procurement procedures in acquiring assets for the project.

8.3.2 The evidence submitted by the Department is contradictory in that the MEC submitted that the additional 9% of shares allocated to ESTINA for the management and administration costs of the project. However from the analysis of the financial statements this could not be verified. This would only be determined through a proper accounting forensic investigation and audit.

8.3.3 The lack of proper monitoring and control measures to ensure value for public money expended is the reason for the discrepancies and this amount to gross negligence, maladministration and resulted in irregular and fruitless expenditure.

8.4 Whether or not environmental legislation was adhered to during the farming operations

8.4.1 The Department did submit the necessary environmental authorisations as required by legislation for the activities of the project on the farm Krynaauwslust and the allegation is not substantiated.

8.4.2 The environmental incident during February 2014 on the farm Krynaauwslust was addressed by the Department of Water Affairs as required by legislation.

9. REMEDIAL ACTION

The appropriate remedial action I am taking in pursuit of section 182(1)(c) of the Constitution, with the view of addressing systemic procurement management deficiencies in the Department and the irregular expenditure incurred, is the following:

9.1.1 The Premier of the Free State Province to:

9.1.1.1 The Premier of the Free State Province ensures, in terms of Treasury Regulation 4.1.3, that the Executive Authority of the Department initiates an investigation into the conduct of the accounting officer of the Department.

9.1.1.2 The Premier of the Free State Province ensures the findings of the Accounting General are noted and the recommendations as mentioned in his report of January 2013 are implemented.

9.1.2 The Member of the Executive Council for the Free State Department of Agriculture and Rural Development to:

9.1.2.1 Initiate an investigation into the conduct of the accounting officer of the Department in terms of Treasury Regulation 4.1.3 with the view of taking disciplinary measures.

9.1.2.2 Ensure that the findings of the Accounting General are noted and the recommendations as mentioned in his report of January 2013 are implemented.

9.1.3 The Head of the Free State Department of Agriculture to

- 9.1.3.1 Improve the Supply Chain Management System of the Department to ensure that all Treasury legislation and other prescripts are adhered to.
- 9.1.3.2 Ensure that the officials of the SCM Division and the members of Management of the Department are trained on the prescripts of the National and Provincial Treasuries in respect of procurement and specifically in respect of deviations.
- 9.1.3.3 Take corrective measures to prevent a recurrence of the failure in the Management process referred to in this report
- 9.1.3.4 Ensure that all Departmental staff involved in the implementation and execution of projects are properly trained and capacitated to manage projects assigned to them;
- 9.1.3.5 Develop a policy for the implementation of internal control measures in line with Treasury Regulation Nr. 3

9.1.4 The Head of the Special Investigating Unit to:

- 9.1.4.1 Conduct a forensic investigation into serious maladministration in connection with the Vrede Dairy Integrated Project of the Free State Department of Agriculture, the improper conduct by officials of the Department and the unlawful appropriation or expenditure of public money or property with the view of the recovery of losses suffered by the State.

9.1.5 The Auditor-General of South Africa to:

- 9.1.5.1 Commission a forensic and due diligence audit with a view to verify all the transfers and expenditure of public money in respect of the Vrede Dairy Integrated Project of the Free State Department of Agriculture in order to determine whether or not value for money was received by the State.

10. MONITORING

- 10.1.1 The Premier, MEC and Head of the Department required to take remedial action, must acknowledge receipt and advise on the acceptance of the Public Protector's report within 30 days of the receipt thereof.
- 10.1.2 The Premier, MEC and Head of the Department must present an action plan on the implementation of the Public Protector's report within 60 days of the receipt thereof, and thereafter submit bi-monthly reports on the progress made with the implementation of the above-mentioned corrective measures
- 10.1.3 The referral of the report to the Special Investigation Unit and the Auditor General will be monitored on a bi- monthly basis.

DATE: _____

Assisted by: Erika Cilliers and Tshiamo Mocumi

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