

## CHAPTER 10

### REPORT ON THE SELECTION OF SUBCONTRACTORS AND CONFLICT OF INTEREST

	<i>INDEX</i>	<i>PAGE</i>
10.1	Background	266
10.2	Selection of subcontractors	267
10.3	Conflict of interest	271
10.4	Alleged conflict of interest of Mr S Shaik	275

## CHAPTER 10

### THE SELECTION OF SUBCONTRACTORS AND CONFLICT OF INTEREST

This matter was mainly investigated by the Office of the Auditor-General. The allegations of a conflict of interest in respect of the Combat Suite of the Corvettes that were investigated during the public phase of the investigation are referred to and discussed in Chapter 11 of the report.

#### 10.1 BACKGROUND

- 10.1.1 The Auditor-General's report on the Special Review of the SDP indicated that the role players in the acquisition process were subjected to a security clearance process. However, potential conflicts of interest that could have existed were not adequately addressed by the process. Certain officials of DoD allegedly had interests in companies that were bidding for the SDP and such interests were apparently not disclosed.
- 10.1.2 In its response to the said report SCOPA expressed concern about *"the possible role played by influential parties in determining the choice of subcontractors by prime contractors."* SCOPA was furthermore concerned *"...that government had no influence in the appointment of subcontractors"*.
- 10.1.3 SCOPA recommended a forensic investigation that had to include a review of the selection of subcontractors and conflict of interest.

## 10.2 SELECTION OF SUBCONTRACTORS

### 10.2.1 DoD and Armscor policy regarding selection of subcontractors

10.2.1.1 The following policy documents were perused and contained relevant information:

DoD instruction no ACQ/1/98	Policy on the acquisition of armaments
K-STD-0020	Armscor's general conditions of contract
K-STD-0010	Rules applicable to prospective contractors
A-POL-1000	Armscor's policy: Acquisition and weapon system management support
A-PRAC-1011	Supplier registration
KP 021	Practice for the request of proposals, quotations, submissions and orders
KP 009	Practice for baseline review boards and authorisation committees
VB 1000	General policy for the management of category 1 materiel acquisition process
KB 1400	Policy on affirmative procurement
KB 1000	Armscor policy: Acquisition
A-Proc -008	Defence Industrial Participation procedure

10.2.1.2 A subcontractor is defined as *"the PERSON named in the ORDER for the performance of any part of the ORDER, or the person to whom any part of the ORDER has been granted by the CONTRACTOR, and includes the successors and assigns of such PERSON."* (Paragraph 3.24 of K-STD-0020 - Armscor's general conditions of contract).

10.2.1.3 The acquisition policies of Armscor and DoD as well as the Defence Review stipulate that the prime responsibility for the selection of subcontractors rests with the main contractor. However, Armscor was not precluded from contracting subcontractors directly if this proved to be more cost-effective (K-STD-0020 - Armscor's general conditions of contract).

- 10.2.1.4 Armscor is primarily responsible for all the contractual aspects during the armaments acquisition process, i.e. the drafting of tender documents and contracts (Refer paragraph 36 of the Defence Review).
- 10.2.1.5 The standard "*general conditions of contract*" which were included in the contracts between Armscor and the main contractors stipulate that the main contractors were responsible for (and accountable to Armscor) the due performance of any subcontractor except if the contract expressly stipulated otherwise.
- 10.2.1.6 According to Armscor's accreditation policy any company, both local and foreign, must be accredited or registered as a defence supplier to Armscor. Only accredited defence suppliers should be allowed to compete for defence contracts. Any company may apply to Armscor to be added to the list of accredited suppliers. Companies should meet certain criteria to qualify for accreditation. A potential supplier's technical and security competence, work force, quality system, financial soundness and technologies offered would be assessed against standards in order to identify risks to Armscor. The assessments are submitted to the Accreditation Board for final adjudication. However, paragraph 3.4 of the policy states that it is not necessary to be an accredited Armscor supplier to perform subcontract work on an Armscor contract. It is the responsibility of the nominated prime contractor to ensure that such work complies with the required quality standards. Subcontractors to the main contracting company should, however, conform to the same principles as mentioned above to ensure the cascading of competition to lower levels in the acquisition hierarchy.

#### 10.2.2 Armscor requirements imposed on the main contractors

10.2.2.1 The RFOs that were sent out during 1997 to the preferred bidders, stipulated, *inter alia*, the following general requirements:

- (a) Bidders were required to submit a list of the subcontractors they proposed to use to Armscor for its approval.
- (b) All the bidders had to provide proof of the required experience and expertise pertaining to the management of major subcontractors.
- (c) A memorandum of understanding or letter of intent between the bidder and his proposed subcontractors.

10.2.2.2 In terms of its policy, Armscor was entitled to make it mandatory for the prime contractors at higher levels on the system hierarchy, to subcontract with enterprises owned by designated groups to the maximum possible extent without unduly compromising on cost and time. Depending on the extent and nature of any acquisition programme, Armscor reserved the right to require that a predetermined percentage of the contract value be subcontracted to enterprises owned and staffed by designated groups.

#### 10.2.3 Local defence industry

The local industry was involved in the process, mainly as subcontractors, except for the Corvettes programme where ADS was regarded as a member of the consortium i.e. main contractor.

### 10.2.4 Requirements for an open, fair and competitive procurement process

10.2.4.1 The Defence Review stipulated that competition should be fair and open as far as is practicable in the procurement of armaments.

10.2.4.2 Armscor, as the contracting party, did not expressly impose such a requirement on the main suppliers to ensure fair competition between subcontractors; nor did Armscor prescribe to the main bidders any specific procedure for the selection of subcontractors.

10.2.4.3 The main contractors did not follow a formal process for the selection of subcontractors in all instances. Instead, they embarked on teaming arrangements and joint ventures with the local defence industry.

10.2.4.4 In at least two instances where a tender process was followed, the basic principles of fairness and open competition appear not to have been followed. i.e.:

- The selection of the supplier of the engines for the LUH.
- The selection of the supplier of the gearboxes for the Corvettes.

10.2.4.5 The entire process pertaining to the abovementioned instances, from soliciting through to adjudication of the relevant tenders can be criticized. The facts and circumstances show that the project teams and senior personnel in the employ of Armscor and DoD played a significant role in these instances of the selection of subcontractors, apparently because of technical and strategic considerations. Complaints were lodged by the competitors against the process followed for the selection of these subcontractors. Another such instance, the selection of the subcontractors for the supply of the SMS and NDSS, is discussed separately in chapter 11 of this report.

10.2.4.6 Strategic considerations in some cases also led to Programme Managers having to accept technical values that were lower than the parameters set in the user specifications and which carried higher risks. For example, the Turbomeca engine posed more risks and was more expensive than the engine proposed by another bidder. Armscor and DoD, however, considered it strategically more important for Denel Aviation that Turbomeca should get the contract.

### 10.3 CONFLICT OF INTEREST

#### 10.3.1 Definition

10.3.1.1 Conflict of interest can be defined as *"a situation in which a person, such as a public official, an employee, or a professional, has a private or personal interest sufficient to appear to influence the objective exercise of his or her official duties. "*

10.3.1.2 There are three key elements in this definition:

(a) A private or personal interest

It is often a financial interest, but it can also be another interest, such as providing a special advantage to a relative.

(b) An official duty

This refers literally to the duty that an official or employee has by virtue of holding a particular public office or acting in his official capacity. The official assumes certain official responsibilities and he acquires obligations to his employer and/or the general public. These obligations are supposed to override private or personal interests.

(c) Interference with objective professional judgement

Conflicts of interest interfere with official or professional responsibilities in a specific way, namely an interference with the official's objective judgement. Government officials and employees serve the general public and they are expected to be objective and independent. Factors, such as private and personal interests, *that either interfere or appear likely to interfere with objectivity* are then a matter of legitimate concern to those who rely on these employees or officials. It is also important to avoid apparent or potential as well as actual conflicts of interests. An apparent conflict of interest is one that causes a reasonable person to think that the employee's or official's judgement is likely to be compromised. A potential conflict of interest involves a situation that may develop into an actual conflict of interest. Private and personal interests can cloud a person's objectivity.

10.3.1.3 An employee shall be considered to have a possible conflict of interest if he has an existing or potential financial or other interest, which impairs or appears to impair his ability to exercise independent and unbiased judgement in the discharge of his/her responsibilities.

10.3.1.4 The mere appearance of a conflict may be as serious and potentially damaging as an actual conflict of interest. Reports of conflicts based on appearances can undermine public trust in ways that may not be restored adequately even when the mitigating facts of a situation are brought to light. Apparent conflicts should therefore be evaluated and managed with the same vigour as known conflicts.

10.3.1.5 Once a conflict of interest situation, actual or potential, is recognised, the ethical responses are straightforward: the person must avoid the conflict by

disclosure and complete recusal. This is, for instance, in line with the State Tender Board Code of Conduct, which stipulates that a member shall, beforehand, declare his interest *vis-à-vis* a matter serving before the Board and the member shall recuse himself during the discussion of the memorandum. No discussion by the member concerned will be allowed prior to or after the serving of the memorandum and such a member may not retain that specific memorandum.

### 10.3.2 Typical examples of conflict of interest

#### 10.3.2.1 *Self-dealing*

For example, an employee works for government and uses his official position to secure a contract for a private consultancy company he or a member of his family owns. Another instance is using his Government position to get part-time employment for family members.

#### 10.3.2.2 *Accepting benefits*

Corruption is one example and accepting substantial non-token gifts is another. For example, when an employee is the purchasing agent for his department and he accepts substantial gifts from a major supplier.

#### 10.3.2.3 *Influence peddling*

Here the professional solicits benefits in exchange for using his influence to advance unfairly the interests of a particular party.

#### 10.3.2.4 *Using an employer's property for private advantage*

This could be as blatant as stealing office supplies for home use. Or it might be more subtle, for instance, using software which is licensed to an employer for private consultancy work. In the first case the employer's permission eliminates the conflict, while in the second, it does not.

#### 10.3.2.5 *Using confidential information*

While working for a private client, an employee learns that the client is planning to buy land in his region. He hurriedly buys the land in his wife's name.

#### 10.3.2.6 *Outside employment or moonlighting*

An example would be establishing a separate business that is in direct competition with his employer. Another example would be accepting so many private clients that he does not have time and energy to devote to his regular employer. In combination with *influence peddling*, it might be that a professional, employed in the public service, sells private consultancy services to an individual with the assurance that they will secure benefits from government: "*If you use my company, I am sure that you will pass the environmental review.*"

#### 10.3.2.7 *Post-employment*

Here the difficult situation might be one in which a person who resigns from public or private employment, goes into business in the same field. For example, a former public servant sets up a practice lobbying the department in which he was formerly employed.

10.3.2.8 The existence of a conflict of interest, whether actual, apparent, or potential revolves around the key question of whether the employee or official was in a situation which was likely to interfere or appear to interfere with the independent judgement that he is supposed to exercise in performing his official duties. The “trust test” could be used to test this. This test implies the following: would others (employer or the general public) trust the official’s judgement if they knew that he was in this particular situation? Trust is the ethical heart or core of this issue. Conflicts of interest involve the abuse, actual or potential, of the trust people have in certain employees or officials. It reduces the trust people generally have in the employer, i.e. the government.

#### 10.4 ALLEGED CONFLICT OF INTEREST OF MR SHAIK

##### 10.4.1 Mr Shaik’s official duties

10.4.1.1 Mr Shaik is a Chief Director in DoD. He was appointed as Chief of Acquisitions in May 1998, although he was designated to take over this post sooner. As such he was the Fund Manager of the Special Defence Account from which the SDP were to be funded. He was also in control of policy matters and planning relating to all acquisition matters.

10.4.1.2 In his capacity as Chief of Acquisitions, he played a pivotal role in the process for the acquisition of the SDP. He occupied the following influential positions:

- Chairperson of the PCB.
- Member of the Defence Staff Council.
- Co-chairperson of the Strategic Offers Committee (SOFCOM).
- Member of the NIP and DIP Consolidation Committee.
- Member of IONT.
- Secretary of the Ministers’ Committee.

### 10.4.2 Private or personal interest

10.4.2.1 Mr Shaik has a brother, Mr Shabir Shaik. The latter, at various times, directly and/or indirectly held interests in the following companies:

- Nkobi Investments (Pty) Ltd.
- Nkobi Holdings (Pty) Ltd.
- Thomson–CSF (Pty) Ltd.
- Thomson CSF Holdings (SA) (Pty) Ltd.
- African Defence Systems (Pty) Ltd (ADS).

10.4.2.2 Before the name was changed, Altech Defence Systems had generally been referred to as ADS. This abbreviated name was later retained when the company changed its name to African Defence Systems.

10.4.2.3 Mr Shabir Shaik's interest in the said companies can be summarised as follows:

(a) Nkobi Investments (Pty) Ltd was incorporated on 24 February 1995 with Mr Shabir Shaik owning 100% of the issued share capital. In 1996 he transferred 69% of his shares as follows:

- |                                |     |
|--------------------------------|-----|
| • Floryn Investments (Pty) Ltd | 20% |
| • Workers College              | 10% |
| • Chartley Investments         | 39% |

On 20 August 1996, all the said shareholders transferred their shares to Nkobi Holdings (Pty) Ltd. This company was incorporated on 27 February 1995, with Mr Shabir Shaik holding 100% of the issued shares. Various share transfers occurred subsequently, but essentially Mr Shabir Shaik indirectly held the majority shares in Nkobi Holdings (Pty) Ltd.

- (b) Since 1996, Nkobi Holdings had been holding 10% of the shares in Thomson-CSF Holdings (SA) (Pty) and 30% of the shares in Thomson–CSF (Pty) Ltd. In September 1999, certain share transactions were concluded that resulted in Nkobi Holdings acquiring 25% of the shares of Thomson–CSF (Pty) Ltd. The purchase price was R7 464 000. The background to these transactions can briefly be stated as follows:
- Thomson-CSF Holdings (SA) (Pty) Ltd had been incorporated on 21 May 1996, to *promote development in SA by entering into joint ventures*.
  - On 26 May 1996, Nkobi Investments acquired 10% of Thomson-CSF Holdings (SA) (Pty) Ltd from Thomson-CSF France for R10 000. Thomson-CSF France held 85%, Nkobi Investments 10% and Gestilic 5% (Nkobi Investments, however, sold back its shares on 30 September 1999 for R500 000).
  - On 1 August 1996 Nkobi Investment obtained 30% of the shares of Thomson–CSF (Pty) Ltd from Thomson-CSF Holdings (SA) (Pty).
- (c) Thomson-CSF of France acquired 50% of the shares in ADS on 24 April 1998. The negotiations that led to this purchase apparently commenced a year earlier. On 25 August 1998, ADS changed its name from Altech Defence Systems to African Defence Systems and retained the abbreviated name ADS. Thomson-CSF France acquired the remaining 50% of the shares on 19 February 1999.
- (d) The shares in ADS were all transferred to Thomson-CSF France, a company incorporated in France. However, on 9 June 1999, Thomson-CSF France transferred the shares to Thomson-CSF International. Later,

on 15 September 1999, Thomson International transferred 80% of the ADS shares to Thomson-CSF (SA) (Pty) Ltd for R29,8 million and the remaining 20% to FBS for R7,4 million. On 30 September 1999, Nkobi Holdings acquired 25% of the shares in Thomson-CSF (SA) (Pty) Ltd for R7,4 million.

- (e) The negotiations pertaining to these transactions had apparently commenced early in 1999, which is evident from the fact that on 22 June 1999, Thomson-CSF International had signed an agreement with FBS for the sale of 20% of its shares in ADS. Pursuant to this agreement the shares were transferred in September 1999, as discussed above.

#### 10.4.3 Directorship

Mr Shabir Shaik was a Director of Thomson-CSF Holdings (SA) (Pty) Ltd from 21 May 1996 until 30 September 1999. He was also a Director of Thomson-CSF (Pty) Ltd from 16 July 1996, a position which he still holds. His interests in these companies were held *via* Nkobi Holdings and Nkobi Investments and he had been a Director of both these latter two companies since incorporation in February 1995. Mr Shabir Shaik was appointed as an alternate director of ADS in September 1999.

#### 10.4.4 Involvement of the Thomson Group and ADS in the SDP

- 10.4.4.1 Altech was a company that conducted business in the defence industry for many years and had been working with Armscor in its retention of technology programmes. Hence, it featured strongly in the SDP. In the proposal submitted in 1998 by the GFC for the supply of the Corvettes, ADS was nominated to undertake the development, design and production of the Combat

Suite. GSC also proposed it as a subcontractor for the Submarines and Agusta in the LUH programme.

- 10.4.4.2 Thomson-CSF France also became a partner in the GFC for the supply of the Corvettes. Minutes of the PCB meeting held on 6 June 1999, revealed that Thomson (SA) (Pty) Ltd was a strong contender in the Corvettes programme as one of the subcontractors for certain elements of the Combat Suite.

#### 10.4.5 Declaration of interest

- 10.4.5.1 V Adm Simpson-Anderson dealt with the conflict of interest relating to Mr Shaik's position in a letter dated 17 October 2000 addressed to Mr Gavin Woods of SCOPA. He stated the following:

*"To my knowledge no members of the SA Navy involved in the selection process to determine equipment, whether at Project Team, Naval Board or Project Control Board level had then or has now any interest or connection with any of the tendering suppliers or sub-suppliers"*

*The chief of acquisition disclosed his perceived interest that his brother had an interest in ADS which was tendering for the submarines, on the grounds that a perception of bias might exist. It was agreed that whenever the corvette and submarine combat suites were discussed I would take over as chairperson, Mr Shaik would not take part in any discussions, consultations or decisions. This was at the level of the Project Control Board."*

- 10.4.5.2 The minutes of the PCB meeting held on 4 December 1998, indicate that Mr Shaik declared an interest in the following terms: *"The Chairperson informed the meeting that, due to a conflict of interest, he is to recuse himself from the combat suite element of the corvette and submarine requirement."*

### 10.4.5.3 Minister Erwin testified during the public phase of the investigation that:

*"We were appraised of this matter very, very early on in the process. Before the final decisions were taken.*

*Mr Shaik himself informed me of the position. I happen to know his brother well. So I was aware of it from that source as well, and we discussed the matter once again when Jarenda Naidoo was appointed as the chief negotiator.*

*The was no sense in him recusing himself from all the areas at all because this was a certain part of the equipment, not the total contract as a whole."*

On the issue whether Mr Shaik had to recuse himself, Mr Erwin testified that:  
*"From my point it was an instruction taken with the minister of defence. The president knew about it, we issued an instruction that he must recuse himself".*

10.4.5.4 A letter from the former Minister of Defence, Mr J Modise, addressed to the chairperson of SCOPA, indicated that Mr Shaik had informed the former Minister of his possible conflict of interest due to the fact that Thomson-CSF France was in the process of acquiring ADS. The letter stated that Mr Shaik's conflict of interest could materialise in the event of Thomson-CSF France transferring its shares to Thomson South Africa as his brother, Mr Shabir Shaik, was a shareholder in Thomson South Africa. He had advised Mr Shaik to follow the Armscor procedures in this regard.

10.4.5.5 The PCB minutes of subsequent meetings showed that, despite his declaration of conflict of interest in December 1998, and contrary to the instruction referred to by Mr Erwin, Mr Shaik had actively participated in discussions relating to the evaluation, selection and appointment of the main contractors and subcontractors in respect of which ADS and Thomson had been contenders. It also appeared that, outside the PCB, he was also involved in matters that

directly or indirectly concerned ADS and Thomson, despite having previously declared a possible conflict of interest based on his brother's interest in these companies (Refer chapter 11).

#### 10.4.5.6 In this regard the following serve as examples:

- (a) At a meeting of the PC held on 8 March 1999, the following was recorded:
- "The chairperson re-iterated that, due to a possible conflict of interest, he will recuse himself from any decisions taken on the combat suite but will not recuse himself from the meeting."* Mr Shaik merely handed over the chairmanship but remained in the meeting when the Combat Suite negotiations were presented. He was also present when a briefing was given on the submarines, which included an element of the Combat Suite in respect of which Thomson was a contender against STN Atlas.

- (b) Mr Shaik chaired the PCB meeting of 27 May 1999. He did not declare any conflict nor did he recuse himself. He actively participated in the discussions relating directly to the issues in respect of which he had previously declared a conflict of interest. The following was recorded:

*"the best and final offer was received on 24 May from GFC/ADS incorporating the price reductions arising from the functional and scope reductions of both the platform and combat suite.....The Chairperson then explained the contractors concern wrt their negotiations with the Department of Trade and Industry and the Department of Finance. POP Sitron said he believes that the combat suite price be reduced to less than RM2600. PMP then stated that the project team would not be able to reduce the price any further unless a different suite configuration and contracting model is used. The chairperson indicated that a total of RM 6694,61 was set aside by the DOF in the affordability study documents presented to Cabinet subcommittee. A combat price of RRM2600 was indicated in the affordability documents."*

*The Chairperson instructed the POP Sitron to complete the price negotiations first. Once this is done POP SITRON is to return to the PCB with a further presentation."*

- (c) During the same meeting, the JPT presented a detailed list of the Combat Suite elements, the supplier and the estimated prices for discussion.
- (d) There was also a presentation of the submarine Combat Suite and a comparison of the ADS and STN Combat Suites offers. In this regard the following was noted: *"The project officer presented the impact of the parallel combat suite offer (statutory cost excluded) and gave an overview of how the increase in the ADS price is determined. The Chairperson then raised his concern regarding the visibility of how the GSC determined the price difference and indicated that the GSC had undertaken to give him and CEO Armscor the required visibility."*
- (e) On 8 June 1999, a *"decision-making PCB"* was convened and chaired by Mr Shaik. He informed the meeting that its aim was to confirm decisions already taken by the PCB with regard to certain projects. This in itself seemed strange. A list of contenders for the various elements of the ship platform and the Combat Suite was presented to the board for ratification. The list was entitled *"Project SITRON: summary of supplier decisions by PCB where alternatives were evaluated or considered."* Thomson featured prominently on this list. The PCB proceeded to ratify the decisions to select the suppliers. There is no indication that Mr Shaik recused himself from this *"decision-making PCB"* meeting. Mr Shaik signed the minutes. He participated in the discussions as per the following recordings:
  - *"The Chairperson tasked POP S to provide CEO Armscor and C Acq with a list of the single source equipment for the Corvette."*

- *"In reply to a query by SM DIP, the Chairperson confirmed that as from this meeting GFC could be approached to firm-up on proposals connected with decisions ratified by the board".*

(f) Mr Shaik chaired the PCB meeting that was held on 24 August 1999. The following was recorded in minutes of that meeting:

### *"ITEM 5: CORVETTES*

*Contracting Model Categories of Risks. The acting project officer briefed the board on the combat suite risk and the risk management pertaining to project-contracting model contained in Appendix A. He emphasised that, although the SAN accepts some risk wrt Category C products the Prime Contractor retains full responsibility for the delivery and performance of a fully integrated vessel, which includes the full integration of the combat suite ashore and abroad.*

### *Combat Suite Data Bus*

*The project team categorise the C<sup>2</sup>I<sup>2</sup> Bus as a Category B risk, i.e. the Prime Contractor retains full responsibility for the delivery and performance of a fully integrated vessel, which includes sub-systems that have a critical effect on the overall vessel delivery. Further, acting POP S informed the board that if C<sup>2</sup>I<sup>2</sup> Data bus option is selected over the ADS Detexis Data bus the project team would have to find the extra funds required to bring both options on par wrt risk coverage. This would result in lifting the ceiling price of the Corvettes*

*C.Acq informed the board that the CEO of Armscor had presented this matter to the AAC and that the Minister supported the issue of the main contractor carrying the overall risk and the responsibility for the sub-contractors. If the principle of the Main contractor carrying the risk for the sub-suppliers is changed, then the added difference in costs will have to be borne by the DoD. The principle of the*

*contractor carrying the risk must be adhered to. The AAC decided that the ceiling price per equipment should not be raised.*

*Mr Swan and R Adm Howell will meet with Mr Richard Young of C<sup>2</sup>I<sup>2</sup> to discuss the matter with him”*

- (g) The presentation was annexed to the minutes and contains details of the contracting model for the Combat Suite. The background problem relating to the Combat Suite was discussed. Of significance is the list with Category B equipment which contained the following information:

*"Combat Management System: Thomson/ADS*

- *Includes Databus and interface units*
- *Merging of Thomson Tavitec and ADS diamond*
- *Considerable software development*
- *Risk: medium to high*
- *Surveillance Radar: Thomson NCS*
- *Navigation segment: ADS*
- *System Management System: ADS*
- *IFF: Thomson /Tellumet*
- *Underwater Telephone ADS*
- *Bathy Thermograph ADS*
- *Combat Team Trainer ADS*
- *Integration Test Bed: ADS”*

- (h) Later in the same meeting the following appears:

*"Ratification by Board.*

*The following proposals by the project team, details of which are contained at Appendix F were ratified by the board*

*(Note: refer to C.Acq's possible conflict of interest as indicated in par 13 of the minutes of the PCB held on 28 April 1999):*

- (i) Combat Suite software only to be frozen by delivery of the third vessel.*
- (ii) Delivery of Cat C sub-systems to Main contractor be extended by six months.*
- (iii) SAN takes delivery of platforms in Germany.*
- (iv) Navy accepts risk for CS equipment while in Dockyard awaiting installation."*

Mr Shaik signed the abovementioned minutes on 30 September 1999.

- (i) At the PCB meeting held on 3 February 2000, the project team reported that C<sup>2</sup>I<sup>2</sup> Databus was a Category B risk and that Mr Swan and Adm Howell met Dr R Young who apparently agreed to withdraw legal action. This report was received under the chairmanship of Mr Shaik. In respect of the Hull Mounted Sonar for the submarine programme, Mr Shaik had recused himself from the discussion surrounding the evaluation of the equipment.
- (j) The PCB convened three times thereafter i.e. on 4 August 2000, 28 August 2000 and 6 October 2000. The minutes of the meeting held on 4 August 2000 stated that the minutes of the previous meeting were accepted after the word "reclused" in the Note under item 5 on page 5 was corrected to read "recuse". This referred to a statement in the minutes of the meeting held on 3 February. However, the minutes of the meeting held on 28 August stated that the minutes of the previous meeting were accepted with the following amendments:

*"The note on page 5 is to be amended to read; "C Acq stated that due to a possible conflict of interest he recuses himself from any decision that may arise in discussions surrounding the combat suite elements, including the hull mounted sonar"*

- (k) However, this appears not to be relevant to the minutes of the previous meeting, but was in fact relevant to the minutes of the meeting held on 3 February 2000 which had already been amended once. The 3 February 2000 minutes had therefore been corrected twice; the word 'reclused' was corrected to read "recuse", and the entire paragraph was subsequently amended to include the declaration of conflict of interest and recusal.

10.4.5.7 It is noteworthy that certain important share agreements were being negotiated during the same months when the contracts, that were ultimately awarded to ADS and Thomson, were discussed in the PCB minutes. The negotiations that ultimately resulted in Thomson purchasing the remaining shares in Altech, the name being changed to ADS and the acquisitions in September 1999.

10.4.5.8 Certain allegations in connection with the involvement of the former Minister of Defence, in a company that was to benefit from the SDP procurement, came to the attention of the investigation teams. This matter was not investigated during the public and forensic phases of the investigation.

## 10.5 FINDINGS

10.5.1 The acquisition policies and guidelines of DoD and Armscor, as well as the Defence Review, stipulate that the prime responsibility for the selection of subcontractors rests with the main supplier. However, Armscor was not precluded from contracting subcontractors directly if this proved to be more cost effective. Armscor did in fact nominate and select subcontractors for the supply of the engines for the LUH and the gearboxes for the Corvettes.

- 10.5.2 Fair and competitive procurement procedures for the selection of sub-contractors were not followed in all cases where strategic considerations played a significant role.
- 10.5.3 DoD and Armscor nominated certain subcontractors for equipment that had been locally developed in order to ensure compliance with technical standards. This did not, however, preclude the main contractor from suggesting and selecting a different subcontractor.
- 10.5.4 There was a conflict of interest with regard to the position held and role played by the Chief of Acquisitions of DoD, Mr S Shaik, by virtue of his brother's interests in the Thomson Group and ADS, which he held through Nkobi Holdings. Mr Shaik, in his capacity as Chief of Acquisitions, declared this conflict of interest in December 1998 to the PCB, but continued to take part in the process that led to the ultimate awarding of contracts to the said companies. He did not recuse himself properly.
- 10.5.5 During the course of the investigation it was established that the Chief of Acquisitions, Mr S Shaik, has not applied for and did not receive the military security clearances required by law.

## 10.6 RECOMMENDATIONS

- 10.6.1 The guidelines contained in the Defence Review that relate to the selection and appointment of subcontractors must be followed and steps taken to ensure that a open and fair process is adhered to for the selection of subcontractors.
- 10.6.2 DoD and Armscor should develop specific rules and guidelines to address conflict of interest issues and to ensure that personnel are properly informed in

this regard. Steps should also be taken to ensure that a particular individual, irrespective of his/her position is not tasked with incompatible functions in multifaceted procurements in order to prevent a conflict or perceived conflict of interest, which would have a detrimental effect on the overall acquisition process.

- 10.6.3 DoD undertakes an urgent personnel audit to ensure that all its staff comply with the prescribed security clearance requirements.