Portfolio Committee on Public Enterprises

Update on Addressing Governance and Financial Challenges of State-owned Companies

(Including *Recent Explosion at Medupi, Corporatisation of Transnet National Ports Authority, Status of Denel, Liquidation of SAX, Implementation of SAA Business Rescue Plan)*

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10:00 – 13:00

public enterprises

Department:
Public Enterprises
REPUBLIC OF SOUTH AFRICA

Contents

Instruments to improve Governance

- Board Performance Evaluation Framework has been developed and submitted to Boards for Implementation
- The review of the Remuneration Guide is underway
- The Risk and Integrity Framework has been developed
- The review of the Memorandum of Incorporation is underway

What the Management Shareholder Bill Aims to Achieve

The Shareholder Management Bill Seeks to strengthen the framework governing SOEs, including:

- The need for the introduction of an overarching act governing SOEs;
- Determining an appropriate Shareholder Ownership Model and institutional arrangements for overseeing SOEs, including the future role of the PSEC;
- Appropriately categorising the SOEs;
- Integrating lessons from the Commission of Inquiry into Allegations of State Capture, Commission of Inquiry into Allegations of Impropriety regarding the Public Investment Corporation (PIC) and other public inquiries;
- Ensuring the appointment of competent individuals with unquestionable integrity through a transparent and robust process to SOE Boards and Senior Management positions;
- Clarifying the respective roles and responsibilities of the Executive Authority, Boards and Executives;
- Regularly reviewing and updating the guidelines such as the remuneration of Boards and Executives and the Board Performance Reports; and
- Reforming procurement by SOEs to reduce the likelihood of corruption

Financial Challenges - Alexkor

- Alexkor risks liquidation due to depleting cash resources and PSJV's inability to settle obligations when they fall due.
- Lack of independence between management and board occupation of both positions by the same person.
- Community structures remain in administration.
- Long-term future of entity should be produced soon.

Financial Challenges - Eskom

- Declining sales volumes
- Liquidity constraints
- Access of funding to capital markets in the absence of government guarantee
- Lack of cost reflective tariff
- Debt levels
- Illegal connections
- Cable theft
- Aging power plants
- Low energy availability factor leading to load shedding
- Municipal arrear debt

Financial Challenges - SAFCOL

- Emerging liquidity risk due to stagnant revenue and slow progress of strategic projects.
- Prolonged implementation period of the Timbadola projects due to delays caused by international lockdowns.
- Weak control environment is negatively impacting SAFCOL sustainability due to increasing financial reporting risk and systems to support better decision making such as an appropriate ERP system.

Financial Challenges - Transnet

- The severe impact on markets both locally and globally have affected overall performance in Transnet. The severe inactivity during the initial stages of lockdown have continuing effects on the economy and demand for transport of freight. However, volumes and revenues are gradually improving.

- Financial ratios have started to compromise Transnet's funding but Transnet is managing the situation through interaction with lenders. There is a risk of further credit rating downgrades in the near future.

- Even before the lockdown, the corporatisation of Transnet National Ports Authority was highly contentious as the effect on Transnet loans could seriously compromise the group's financial sustainability.
- Strict regulatory action may further compromise the financial sustainability.
- Transnet's liquidity has risen significantly.

Financial Challenges - Denel

- The SOC is financially distressed and a solution is being formulated.
- Timeous decision on the future and support for Denel is critical.
- Risk of the new operating model being implemented due to loss of critical skills.
- Risk of Denel's collapse on the SANDF's ability to fulfil its constitutional obligations.

The Current State of Denel

- The SOC continues to experience liquidity challenges. The SOC is unable to raise the required bank guarantees to fund operations.
- The threat of liquidation is real with a number of suppliers including individual employees approaching or threatening to approach the courts for relief.
- The SOC has lost critical skills putting at risk the viability of certain capabilities that are critical to the Department of Defence.

New Business Model – to Reposition the SOC for Sustainability

DENEL SERVICES
Overberg Test Range (OTR) for T&E
Properties

Denel SOC
Holding Company Concept
(R&D, Innovation, IP Development & Integration)

Denel Associates & Subsidiaries
Rheinmetall Denel Munitions (Large)
Barij Dynamics (UAE) (PGM's)
Hensoldt Optronics (SA)

DENEL 5.Y STRATEGY – NEW OPERATING MODEL IMPLEMENTATION

Engineering
(R&D, Innovation, Design & Integration)

Land Systems
- Infantry Systems
- Artillery Systems

Vehicle Systems
- Armoured Vehicles
- Mechatronics

Dynamics
- Missiles
- Precision Guided Munitions (PGM's)

Integrated Systems Solutions (ISS)
- GBADS, as well as other complex Integrated ICT Systems and Cyber Solutions

New business and diversification

Commercial
- New business development
- IP (registry & management)
- Offset
- Legal & Compliance
- Risk

EXITS / DISPOSALS
(under evaluation)
- Spaceteq (Exit / Transfer)
- Mechem (Exit)
- DGR (Exit)
- Property consolidation

Maintenance & Manufacturing

Aeronautics
- Military Aircraft & Engine – MRO
- Systems Integration and Upgrades
- Rooivalk Helicopter
- Unmanned Aerial Vehicles (UAVs)

Pretoria Metal Pressing (PMP)
- Small & Medium Calibre Munitions
- Infantry Weapons

Vehicle Systems Maintenance

Dynamics production

Strengthen core business

New model built on a **foundation of standardised Governance, Policies, Practices, Standards and Business Management Systems**

Supported by **centralised services for Human Resource Management, Supply Chain Management, Financial Management and ICT**

Industry involvement and development through supply chain with PPPs for lower level production, manufacturing and support

Critical Objective:
Retain & develop the knowledge base,
Reduce the cost base
Restructured for Efficiency, Agility, Competency, Career, Development, Diversification and Growth

Key Notes:
- Reduction in overheads & redundancies in the cost base (target 35%)
- IP protection & retention of strategic capabilities
- Commercial exploitation of IP & strategic capabilities
- Industry leader in R&D, innovation and technology development
- Streamlined Business Processes
- Development of new non-military business and technologies
- Smart Partnering to access to new technologies and markets
- Evolution of commercially driven culture

Funding Requirement and Options

- The Department has made a submission for funding for Denel through the MTEF process.
- The Department and National Treasury are finalisng the options related to the guaranteed debt.
- The DPE is engaging the Department of Defence on the sale of non-core assets and businesses.

Airlines: Resumption of Operations

- SAA plans to resume with operations are underway – date for the resumption will be communicated to the market in due course;
- SAA has leased aircraft for the domestic and regional operations
- SAA received its AOC (Air Operators Certificate)
- Both cabin crew and pilots will undergo the necessary training in preparation for resumption of operations

Strategic Equity Partner

- The due diligence is at an advanced stage and should be completed in the next week or so;
- After this, the process will then enter the Sale and Purchase Agreement (SPA) stage;
- After the successful completion of the SPA stage, we will be able to announce the completed deal to the public pending regulatory approval.

Status Of Subsidiaries

Mango

- The company is experiencing severe liquidity issues, cannot pay its debts and meet the obligations when they fall due.

- Government has allocated funding to Mango to meet its Recapitalisation requirements. However, the funding available will not be enough to meet the current obligations.

- Board of SAA commissioned a Sustainability Assessment of Mango. The Sustainability Assessment Report recommended that Mango be placed under business rescue.

- The unions approached the Court to place Mango under business rescue.

- Board had already taken a resolution to place Mango under business rescue. The Court placed Mango under voluntary business rescue.

Status Of Subsidiaries

SAAT

- SAAT is implementing a Section 189 process to reduce the headcount;

- A portion of the appropriated funds transferred for:
  - Purchase of spares
  - Payment of outstanding salaries

Air Chefs

- Air Chefs will also be implementing a Section 189 process to reduce headcount

- A portion of the appropriated funds transferred for:
  - Payment of outstanding salaries

South African Express Airways Update

- The court on 28 July 2021 granted an extension for the provisional liquidation process;
- The potential buyer has submitted a revised offer, currently awaiting a bank guarantee to formalise the purchase process;
- National Union of Metal Workers of South Africa (NUMSA) and South African Cabin Crew Association (SACCA) have gone to the Constitutional Court to challenge the liquidation of SA Express without the involvement of Parliament in the process;
- DPE will prepare answering affidavit for the NUMSA application above

Medupi Unit 4 Generator Explosion

- Medupi Power Station experienced an explosion on the Unit 4 generator at approximately 22h50 on 08 August 2021
- At the time of the incident, Medupi Unit 4 was on a short-term outage (since 06 August 2021) for repairs on some of the milling plant components
- The explosion has resulted in extensive damage to the generator and other components within close proximity. The full extent of the damage is still to be determined
- There was additional scope requested for Eskom Rotek Industries (ERI) to identify and repair an external Generator Hydrogen leak.
- The Operating Department was tasked with the purging of Hydrogen (H2) from the Generator prior to the leak search.

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Immediate Actions Taken/in Progress

- Preliminary investigations indicates that the procedure for the purging of the generator may not have been followed. Therefor eight individuals have been suspended pending the investigation:
  - Operating Manager
  - Outage Manager
  - 2 Shift Managers
  - 4 Senior Plant Operators
- Inspector of Machinery has been on site – site inspection completed
- Insurance Assessor to be at Medupi today (12 August 2021)
- Will be appointing a Recovery Manager soon to coordinate all recovery activities
- ERI will strip the plant so that full damage can be assessed
- The Original Equipment Manufacture will likely be contracted for the reconstruction Kusile unit 6 generator will be used for the Medupi 4 recovery

Critical Next Steps to be Taken by Eskom

- Detail Major Event Investigation to be completed
- Extent of plant damage to be established, including opening and inspections of the 4 main turbine cylinders, structural integrity of adjacent plant, etc.
- Detail scope of work to be compiled for the recovery of the Unit
- Full-time recovery manager and multi-disciplinary team to be appointed
- Schedule which will inform Unit 4 return to service date to be compiled
- Opportunity maintenance to be conducted on all other plant area
- Preservation procedure to be activated where necessary

Corporatisation of Transnet National Ports Authority

Commercial Ports Policy

- The National Commercial Ports Policy (Ports Policy) provided guidelines of the White Paper on National Transport Policy (1996), proclaiming that four fundamental port policy guidelines as follows:
  1. the establishment of the National Ports Authority;
  2. the establishment of the Ports Regulator of South Africa (Ports Regulator);
  3. the separation of the port authority and port operations functions; and
  4. the promotion of low cost, high level of service, and shipper choice in the port operations by creating a competitive environment in the commercial ports system.

- The key guiding principles underlying the new port dispensation are:
  1. The current National Ports Authority within Transnet will be positioned outside Transnet in accordance with the restructuring programme of Transnet, as approved by the Minister of Public Enterprises;
  2. The National Ports Authority post Transnet end-state will then be established as a new State-owned corporate entity;
  3. The 'National Ports Authority' will be the landlord of the South African ports and will own all the land and the port infrastructures within the port estates;
  4. Greater private sector involvement in operations will be sought through leases and concessions;
  5. The allocation of leases or concessions will be open to competitive bidding; and
  6. The bidding process will be transparent and based on a set of clearly stated objectives/targets, criteria and measurable deliverables.

Commercial Ports Policy - Corporatisation

1. The Ports Policy proclaims that Transnet National Pots Authority (TNPA) will be positioned outside Transnet in accordance with the restructuring programme of Transnet, as approved by the Shareholding Minister; and it will, post the Transnet end-state be established as a new State-owned corporate entity. These policy provisions form the basis of the following sections of the National Ports Act, No 12 of 2015 (Ports Act) with regard to the corporatization and conversion of TNPA into a separate public entity:

   a) “(2) As soon as this Act takes effect the Shareholding Minister must ensure that the necessary steps are taken for the incorporation *of the National Ports Authority of South Africa as a company contemplated in subsection (3).”*

   b) “(*3) The Registrar of Companies must- (a) register the memorandum and articles of association and incorporate National 30 Ports Authority of South Africa under the name “National Ports Authority (Pty) Ltd” with Transnet as the sole member and shareholder; (b) issue to that entity the necessary documents to enable it to conduct business as a corporate entity*.”

   c) *“4 (1) Notwithstanding sections 32, 66, 190 and 344(d) of the Companies Act, on a date after the incorporation of National Ports Authority (Pty) Ltd, and with the concurrence of the Minister, the Shareholding Minister may take the necessary steps to convert the company into a public company, styled “National Ports Authority Limited”, vested with the authority to own, manage, control and administer ports within the Republic.”*

How Corporatisation Will Unfold

1. JUNE 2021: The interim Board of the TNPA subsidiary has been appointed for a period of three months as a transition Board(June 2021).
2. The Nomination process for a full Subsidiary Board will be done through a public process as stipulated in the Port Act Section 14 and 15 accordingly. The department has to implement the process within the three months, whilst the interim board is operating in transit.
3. Transnet has submitted the Gazette statement to DPE for approval – 29 July 2021
4. Transnet is preparing the Memorandum of Incorporation (MOI) for the incorporation of TNPA as a subsidiary of Transnet.
5. A PFMA section 54 application will be submitted to the Department for approval, and the National Treasury will be notified.
6. A project plan detailing the transition of the TNPA to a full subsidiary Section 80(e)) including all Statutory, Financial and Employee matters has been submitted to the Minister of Public Enterprises for consideration and approval. This project plan stipulates all the financial activity plans including the engagement with lenders and other stakeholders for the TNPA.
7. The TNPA financials will be incorporated into Transnet SOC Ltd, the holding company as per the Companies Act to fulfil the subsidiary and holding company status. This will avoid any financial disruptions to the Transnet Balance Sheet.