W1

WITNESS STATEMENT
&
ANNEXURE

FOR

KGATHATSO TLHAKUDI

JUDICIAL COMMISSION OF INQUIRY INTO ALLEGATIONS OF STATE CAPTURE, CORRUPTION AND FRAUD IN THE PUBLIC SECTOR INCLUDING ORGANS OF STATE

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GLOSSARY OF ABBREVIATIONS

ABBREVIATION	DESCRIPTION
AFS	ANNUAL FINANCIAL STATEMENTS
AGM	ANNUAL GENERAL MEETING
AR	AUDIT REPORT
ARM	SCOR ARMAMENTS CORPORATION OF SOUTH AFRICA
BAE	MARCONI ELECTRONIC SYSTEMS (MES) AND BRITISH AEROSPACE (BAE) MERGED TO
FORM	BAE SYSTEMS (30 NOVEMBER 1999)
BER	BOARD EVALUATION REVIEW
CEO	CHIEF EXECUTIVE OFFICER
CP	CORPORATE PLAN
CV	CIRRICULUM VITAE
DOG	DEPUTY DIRECTOR-GENERAL
DG	DIRECTOR-GENERAL
OPE	DEPARTMENT OF PUBLIC ENTERPRISES
GCEO	CROUP CHIEF EXECUTIVE OFFICER
GCFO	GROUP CHIEF FINANCIAL OFFICER
KPI	KEY PERFORMANCE INDICATOR
KPA	KEY PERFORMANCE AREA
LSSA	LAND SYSTEMS SOUTH AFRICA
PFMA	PUBLIC FINANCE MANAGEMENT ACT
SAAB	SVENSKA AEROPLAN AKTIEBOLAGET (SWEDISH AEROPLANE CORPORATION -
AUTO/AIRCRAFT	MANUFACTURER)
SAFCOL	SOUTH AFRICAN FORESTRY COMPANY LIMITED
ShC	SHAREHOLDERS COMPACT
SIS	STRATEGIC INTENT STATEMENT
SOC	STATE OWNED COMPANY
SOE	STATE OWNED ENTERPRISE
AFS	ANNUAL FINANCIAL STATEMENTS
AGM	ANNUAL GENERAL MEETING

IN THE JUDICIAL COMMISSION OF INQUIRY INTO ALLEGATIONS OF STATE CAPTURE, CORRUPTION AND FRAUD IN THE PUBLIC SECTOR INCLUDING

ORGANS OF STATE

"THE ZONDO COMMISSION"

I, the undersigned,

KGATHATSO TLHAKUDI

states as follows:

INTRODUCTION

1 I was appointed as a Deputy Director-General (DDG) at DPE on 01 November 2012 and have remained in this position since then.

2 I hold a Bachelor of Science in Engineering from the University of Witwatersrand (1995) and a Master of Business Administration from the University of Cape Town (2003). I have had the privilege of being a Sainsbury Scholar at the University of Cambridge (2004). I further hold postgraduate diplomas in Air Transportation Management from the Royal Aerospace Society, United Kingdom (1998), Programme Management and Systems Engineering from the University of North West (2008).

3 I have 24 years working experience starting as an engineer at Denel, where I spent 9 years rising to the position of an Aircraft Conversion and Maintenance Centre Manager by the time I left in 2004. I joined Volkswagen South Africa where I was the Field Operations Manager for a period of 4 years responsible for the after sales business in the RSA Northern Provinces (Free State, Northern Cape, Gauteng, Northern Cape, Mpumalanga, and Limpopo), Botswana and

Namibia. In 2008 I returned to the defence sector as the Senior Manager Aircraft Systems Acquisition at Armscor, the acquisition agency of the Department of Defence.

4 At Armscor I was responsible for overseeing the acquisition of new aircraft systems and the upgrade of existing systems for the Department of Defence (South African Air Force) and some of the South African Police helicopter systems. The delivery of the South African Air Force Strategic Defence Package component (SAAB Gripens, BAE Systems Hawks, Agusta-Westland Super Lynx, and Agusta A109s) were delivered during my tenure. The result was that I worked closely with Denel, as some of the programmes were executed at Denel.

5 I can safely say that through my working experience and academic experience I have had the privilege of a good understanding of the workings of the defence and aerospace sector.

6 I believe that my recruitment to join the Department of Public Enterprises in late 2012 was driven by this track record. I therefore, found myself coming full circle, entrusted with the responsibilities, as a DDG, of exercising oversight over the following State Owned Entities (SOE): Denel, Alexkor, and Safcol

7 I performed the function for the last 6 years. I have from 1 January 2019 been assigned the responsibility for the Business Enhancement Services portfolio in the Department of Public Enterprises.

8 As can be seen from the portfolio, I had oversight over the mining and forestry SOE's as well. In this regard, I had access to a team of engineers, foresters, financial analysts who assist in providing the technical expertise in areas where I may be found wanting. With my team, we provided strategic support and sector team leadership to the three entities. I also had access to Legal, Governance,

Environmental, Economic and Socio-Economic specialists located in other units in the Department to assist with setting objectives for the SOE's and in their monitoring.

9 In the oversight role I ensure that the following are performed throughout the financial year:

9.1 The Minister, in his role as a Shareholder Representative of Government, provides the SOE Board with Government's expectations of the SOE: confirmation of mandate, strategic objectives, and policy imperatives that should inform SOE planning. This is done through the Strategic Intent Statement (SIS), which should be issued a year ahead of the financial year, for which it is applicable.

9.2 The SOE's are performance contracted. In the 3rd Quarter of the preceding financial year a Shareholder Compact (ShC) is concluded between the Minister and the SOE Board. This normally coincides with the Annual General Meeting (AGM). The ShC would detail the Key Performance Areas (KPA) and Key Performance Indicators (KPI) that the SOE should deliver on and these would be aligned to the SIS.

9.3 The SOE would further be expected to produce and submit a Corporate Plan (CP), by the end of February of a preceding financial year, to the Department and National Treasury which details how it intends to utilise the resources within its control to realise the strategic objectives contained in the ShC and SIS.

9.4 The Department throughout the financial year would receive monthly and quarterly performance reports from the SOE, which are analysed to assess whether the SOE are delivering on the ShC performance

expectations, further, whether the SOE is meeting the agreed CP. The analysis is elevated to the Minister to advise on areas of concerns and whether any intervention is necessary. The intervention would be in the form of a letter to the SOE Board, and/or a meeting with the SOE Board depending on the degree of deviation from agreed performance targets.

9.5 The pinnacle of a financial year would be the AGM, which is held normally during the 3rd Quarter of the subsequent Financial Year, where the Annual Report (inclusive of the Annual Financial Statements (AFS) and the External Auditors Report (AR)) is tabled for consideration by the Minister of Public Enterprises. It is at the AGM, where the SOE Board Evaluation Report (BER) would also be considered, and depending on the term(s) of the SOE Board member(s), the Minister would consider retention or rotation of the SOE Board member(s).

9.6 The Department receives various correspondence from stakeholders within the economic sector, government, organised labour, communities, and Parliament requiring the Director General or Minister to intervene with the SOE. These are evaluated and the correspondents engaged to determine an appropriate course of action, and the Director General or Minister would then be advised accordingly.

9.7 There are also forums within and outside government that the Department has to be represented by virtue of the SOE operations potential impact – negative or positive.

THE PURPOSE OF THIS STATEMENT

10 The purpose of this statement is to give an outline of events and circumstances that transpired around the year 2015 pertaining to the appointment of the new board by former Minister Lynne Brown (the Minister) and also the circumstances pertaining to Denel PFMA application for approval of the Denel Asia Joint Venture.

11 This statement will be structured as follows:

11.1 Firstly, I will give an account of the sequence of events and processes followed in the DPE leading to the 2015 board appointments for Denel by the Minister.

11.2 Secondly, a sequence of events in relation to Denel's application for approval to for a joint venture entity in terms of Section 51(1)(g) and section 54 (2) of the Public Finance Management Act No. 1 of 1999.

2015 DENEL BOARD APPOINTMENT

HISTORICAL BACKGROUND - BOARD APPOINTMENTS

12 The circumstances that transpired in relation to the Denel board appointment were mirrored with the rest of the of the other SOE board appointments, as they pertain to the SOE's I have oversight over (at least under my oversight: Alexkor and Safcol). Hence, I will only deal with the Denel board member appointments in this statement.

13 As I indicated earlier, generally the SOE Boards were reviewed at the AGM (Denel 2015 AGM pack is included as Annexure **KT1**) of each SOE where a

general review of the board would be conducted, which included, amongst other things:

13.1 to assess the SOE performance against the ShC, AFS, and AR and whether the Board has steered the SOE effectively during the year under review and during the rest of its tenure.

13.2 the SOE Board dynamics and effectiveness would be evaluated guided by the BER, which in some cases would include a peer review, to identify member(s) that could be negatively affecting the functioning of the Board or not pulling their weight as per the SOE Board and Committees attendance record, for rotation.

13.3 evaluation of the SOE Board skill mix to identify whether the board still had the capacity to ensure that the SOE can attain the objectives set out by the Minister in the SIS and ShC.

13.4 There could also be member(s) of the board that had reached the end of their term (as per the SOE Memorandum of Incorporation (MOI)) or who may have expressed a desire to be relieved of their responsibilities and are therefore up for rotation.

13.5 The board review was done in consideration of the above factors holistically with other factors that would be relevant at the time.

14 A critical consideration in the composition of the Board, would generally be: sector knowledge and experience, critical skills representation (inter alia, at least one chartered accountant, technical expertise (engineer or scientist with industry experience, a commercial lawyer, a human resources specialist, etc.): and probity of the individual as per the integrity report. This would be informed by the need to ensure that there are skills to populate the Board Committees.

15 On joining the Department, which was during the tenure of Minister Malusi Gigaba, I became aware of the database of potential board members, which is maintained by the DPE Governance unit. The database would be used to source board members for whenever vacancies arise and when the time for SOE Board rotation came up. The database was updated regularly including through requests to the public for submission of applications for consideration.

16 Its existence did not however mean that other potential board members could not be sourced from the network outside that database. If a suitably qualified person was not listed in the database, they could still be appointed. It was merely meant to be a pool of readily available qualifying people.

17 The process of filling SOE Boards would normally unfold as follows:

17.1 The Department prompted by Ministry would initiate the process. The process would be overseen by the Governance unit with strong input from the Sector Units (in the case of Denel, Alexkor and Safcol it would be my unit).

17.2 As indicated earlier: the SOE Board BER, the SOE ShC performance, SOE Board members tenure, and SOE Board members attendance record would be considered in deciding whether any of the current SOE Board member(s) should be rotated. Further, the Government expectations of the SOE as contained in the SIS and ShC would inform skills that should be brought in to strengthen the Board.

17.3 The above process would result in a draft (or long) list of Board members for consideration by the Minister. The Governance Unit would be entrusted to vet the list to ensure that the proposed members are fit and proper. The process is iterative with continuous

engagements with Department and Ministry aided by the Governance Unit.

17.4 The list would be presented to the Minister for consideration and as it is convention before it can be presented to Cabinet for consideration, the Minister would consult with political counterparts to ensure its acceptance. The process would result in some changes to the names proposed.

17.5 The Department would then compile a Decision Memorandum to the Minister incorporating a Cabinet Memorandum with the proposed final list for submission to Cabinet.

18 In relation to the review of the Denel Board in anticipation of the 2015 AGM, there was a significant departure from the above process by Minister Lynne Brown, who had replaced Minister Malusi Gigaba after the 2014 National Elections.

19 The Governance and Defence Sector Units had initiated the process of Board review leading up to the 2015 AGM and the files with the profiles of the potential board members had been delivered to my office by the Chief Director Governance, Ms Orcilla Ruthnam. These were collected before my team and I could commence the process by Ms Ruthnam citing an instruction from the Minister.

20 The next time I saw the list of board members it was a final list that had to be submitted to Cabinet. I was concerned with the list but I kept my views to myself, except to highlight to the Ministry that the proposed chairperson had been struck off the attorneys roll at some point. I pointed out that this could raise questions and that the Ministry should have a response to the inevitable questions that will be raised.

THE DENEL PRE 2015 AGM BOARD

21 On arriving at the Department on 1 November 2012, I found a Board that was chaired by Mr Zoli Kunene, whom I had known of from quite early in my career was one of the leading industry defence executives and entrepreneurs. Mr Kunene retired from the Board at the 2014 AGM and was replaced by an equally impressive Ms Martie van Rensburg.

22 The outgoing Board at the 2015 AGM, headed by Ms van Rensburg were:

COMMISSION OF INQUIRY INTO STATE CAPTURE

	Name	Qualifications	Role	Duration
22.1	Martie JV Rensburg	BCom, Bcompt (Hon), CTA, CA (SA), Executive leadership programme	Interim Board Chairperson Member of the Audit and Risk Committee	August 2014 – July 2015 August 2010 – July 2015
22.2	Riaz Salojee	Executive National Security Programme, BGen (retired), Senior Command and Staff Course (SAAF), Junior Command and Staff Course (SA Army), Certificate (Strategic Management) (UP)	Group CEO	January 2012 – September 2015
22.3	Fikile Mhlontlo	BCompt, BCompt (Hons), CA (SA)	Group CFO	November 2008 – September 2015
22.4	Adv Gandhi Badela	MSc Eng (Electromechanical), MSc Eng (Packaging Technology), MSc (Engineering Management), MBA, LLB	Member of Personnel Remuneration and Transformation Committee	July 2011 – July 2015
22.5	Dr Gert Cruywagen	MBSc, PhD, PMD, FIRM (SA), Risk Management Diploma, Certificate Advanced Security	Chairman of the Audit and Risk Committee	September 2008 – July 2015

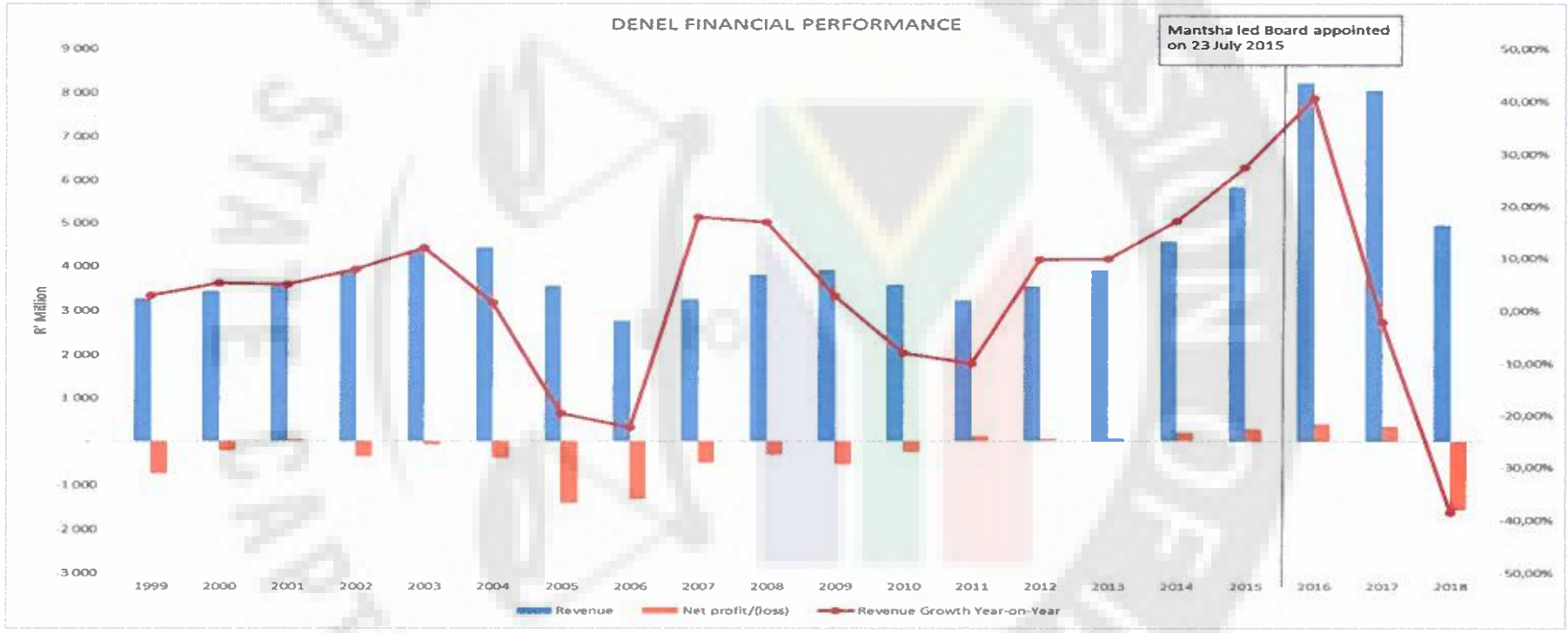
	Name	Qualifications	Role	Duration
		Management	Member of the Social and Ethics Committee	
22.6	Ziphozethu Mathenjwa	BSc, Certificate in Financial Management and Investments, Post-graduate Diploma in Business Management, Strategic Management and Corporate Governance, MBA, MSc (International Business)	Member of Audit and Risk Committee	July 2011 – July 2015
22.7	Nkopane Motseki	Certificate in Forensic Investigations and Crime Intelligence	Member of the Board	July 2011 – July 2015
22.8	Mavuso Msimang	BSc, MBA	Member of the Social and Ethics Committee	July 2011 – July 2015
22.9	Bafana Ngwenya	Certificate in Defence Management, Certificate in Practical Project Management, Certificate in Strategic Management	Member of the Board	July 2011 – July 2015

	Name	Qualifications	Role	Duration
22.10	Prof Stella Nkomo	BA (Business Education), MBA, PhD	Member of Personnel Remuneration and Transformation Committee Member of the Social and Ethics Committee	July 2011 – July 2015
22.11	Adv Melissa Ntshikila	BA, LLB	Member of Personnel Remuneration and Transformation Committee	July 2011 – July 2015
22.12	Matodzi Ratshimbilani	BProc, Certificate in Business Management, Mining Executive Preparatory Programme and Certificate Prospective and Mining Law	Member of Personnel Remuneration and Transformation Committee	July 2011 – July 2015

CONFIDENTIAL

Initial: KG

23 The result was a Denel whose performance was trending in the right direction. The business was recovering from years of record losses and meeting its Corporate Plans. In order to illustrate the situation at Denel and the recovery trend:



CONFIDENTIAL

Initial: KT

KT-013

DENEL TURNAROUND

24 The turnaround of Denel had been built on:

24.1 Partnership with leading international defence equipment suppliers to leverage their established international value chains and markets and attract capital and intellectual capital investment. This saw the following entities taking strategic equity partnership in Denel divisions:

24.1.1 Rheinmettal AG (Germany) in February 2008 acquired 51% of Denel Munitions to form Rheinmettal-Denel Munitions.

24.1.2 Turbomeca (France) in May 2002 acquired 51% of Denel Airmotive to form Turbomeca Africa. Turbomeca (now called Safran Helicopter Engines) in September 2017 disinvested due to a downturn in its engines business worldwide, and it is consolidating in the home market.

24.1.3 SAAB AB (Sweden) in September 2006 acquired 70% of Denel Military Aircraft to form SAAB-Denel Aerostructures. The partnership was not successful and SAAB in 2010 disinvested and sold back its stake to Denel.

24.1.4 Carl Zeiss Optronics AG (Germany) in 2007 acquired 70% of Denel Optronics to form Carl Zeiss Optronics (Property) Limited. The Carl Zeiss stake has since evolved through Airbus Optronics to a business that is now owned by Hensoldt domiciled in Germany.

24.2 Appointment of credible and competent executives supported by an experienced Board of Directors. The step was critical in ensuring support from key stakeholders: the Department of Defence and Financial Institutions amongst others.

24.3 The financial institutions were critical as Denel was heavily dependent on the banks for its working and investment capital. The cases in point are:

24.3.1 On conclusion of an order, Denel normally requires 30% advance payment to enable project commencement. Denel is then required by a customer to provide a bank guarantee as security for the advance payment.

24.3.2 The R850 million acquisition of BAE Land Systems South Africa (LSSA) in April 2015 had to be funded through the banks as Denel did not have adequate cash reserves to fund the transaction.

25 Therefore, the dismissal of the Denel Board in July 2015 interrupted the recovery trajectory that Denel had been on. It sent discomforting signals to the key stakeholders, especially the financial institutions.

26 The change at the Board was followed a year later (September 2015) by the suspension and dismissal of the Executive Directors: Riaz Saloojee (Group Chief Executive Officer), and Fikile Mhontlo (Group Chief Financial Officer).

PROCESS FOR APPOINTMENT OF NEW BOARD (2015)

27 Prior to the 2015 Denel AGM, the Department started preparations for the AGM and we were of the view that the existing board under Martie Janse van Rensburg had done well considering Denel history of financial problems.

28 In light of the above considerations, the DPE (at least in my unit) approach was leaning towards the retention of the majority of the board members. It is also good practice to ensure a certain level of continuity when considering Board changes.

29 As I indicated earlier, in reviewing the Board for possible rotations, files with CVs sourced from the database were brought to my office by Orcilla Ruthnam (Ruthnam) from the DPE Governance unit.

30 However, before we could commence with the task, hardly a day two at the most, the files were collected from my office by Ruthnam indicating that the Ministry will manage the process from that point onwards, as appointment of Boards is the Minister's prerogative.

31 This was the last time I heard of the Denel board appointment process, until a Decision Memorandum with a Cabinet Memorandum attached, and the proposed Denel board members was brought to my office for my signature.

32 The proposed Board was composed of the following individuals, whom with all due respect to them when I compared their collective qualifications and experience to the outgoing Board, there was a big expertise gulf :

	Name	Qualifications	Role	Duration
32.1	Daniel Mantsha	BJuris, LLB	Board Chairperson	July 2015 – April 2018
32.2	Riaz Saloojee	Executive National Security Programme, BGen (retired), Senior Command and Staff Course (SAAF), Junior Command and Staff Course (SA Army), Certificate (Strategic Management) (UP)	Group CEO	January 2012 – September 2015
32.3	Fikile Mhlontlo	BCompt, BCompt (Hons), CA (SA)	Group CFO	November 2008 – September 2015
32.4	Mpho Kgomongoe	BCom	Interim Chairperson of the Audit and Risk Committee	July 2015 – April 2018
32.5	Pinkie Mahlangu	BProc, Certificate (Business Rescue Proceedings)	Member of Personnel Remuneration and Transformation Committee	July 2015 – April 2018
32.6	Nonyameko Mandindi	BSc (Quantity surveying), Diploma (Project	Member of Personnel Remuneration	July 2015 – April

	Name	Qualifications	Role	Duration
		Management), Certificate (Housing Finance)	and Transformation Committee	2018
32.7	Refiloe Mokoena	BJuris, LLB	Member of Social Ethics Committee	July 2015 – April 2018
32.8	Nkopane Motseki	Certificate (Forensic Investigations and Crime Intelligence)	Member of Social Ethics Committee	July 2011 – April 2018
32.9	Thamsanqa Msomi	BA Law	Member of Audit and Risk Committee	July 2015 – April 2018
32.10	Themba Nkabinde	MBA, BMil, Project Management Programme	Chairman of the Personnel Remuneration and Transformation Committee	July 2015 – April 2018
32.11	Khumbudzo Ntshaveni	MBA, BA (Hons) (Labour Relations), BA (Hons) (Development studies), BA (Political science)	Chairperson of Social Ethics Committee Member of Audit and Risk Committee	July 2015 – April 2018

33 The decision memorandum (Annexure **KT2**) with names of candidates that I had never seen before and not discussed with my team was presented to me for signature. Besides myself the following other people in the Department were required to sign the memo in that regard:

33.1 the Acting Director-General, Matsietsi Mokholo; and

33.2 the Head of Governance Unit, Ruthnam.

34 Upon inspection and scrutinising, amongst other things, the following struck myself as red flags in regards to the list:

34.1 A number of lawyers in it.

34.2 There was no chartered accountant in the list whilst there was an audit committee that requires a CA.

34.3 The board chairperson was a man who had a questionable past in relation to his profession (previously struck-off the roll of attorneys for trust account related infidelity).

34.4 Most of the persons in the list had no or little experience as board members.

34.5 A retention of only one previous board member, Mr Johannes "Sparks" Motseki (Motseki). I found it odd that Mr Motseki had been the one person that would have been retained. I did not get to know the reasons for the decision.

34.6 The only person with the relevant experience of the industry (defence) was Ms Refiloe Mokoena due to her board experience at ARMSCOR where she had served as a Deputy Chairperson.

34.7 Former adviser to former Minister Gigaba, Mr Thami Msomi was part of the list.

35 I reluctantly signed the memo because I knew that matters were no longer under my control and the political atmosphere alive at the time meant that if I did not sign the internal memo I would be victimised.

36 I decided to not stand in the way of the Ministry, but to sign the memo for the reason, amongst others, that:

36.1 Firstly, my previous experience for standing up against higher authority almost cost me my job. Highly publicised legal battles cost me dearly.

36.2 Secondly, the political atmosphere at the time meant that if you did right you were the enemy.

37 However, the process being followed by Ministry in the appointment of the Boards was raised with the Acting Director General, Ms Matsietsi Mokholo by the Sector DDG's, including the discomfort in having to sign off on Board lists they did not participate in putting together.

38 Ms Mokholo raised the matter with Minister Brown, who expressed to Ms Mokholo that Board Appointments were her prerogative and that Sector DDGs should be removed from the process going forward with the Governance unit providing secretarial support.

39 The result was that the decision memorandum in Paragraph 35 was not, eventually processed, as the Minister, had opted to put together a new memorandum appointing three Boards: SA Express, Denel and Eskom with the assistance of the Legal Governance and Risk unit. The latter memorandum without my signature is attached as **Annexure KT3**.

40 On 24 July 2015 Minister Brown announced the appointment of Denel new board members after approval by Cabinet.

DENEL DECLINE

41 In my own assessment, Denel had shown good progress towards sustainability, though the profit margins were still thin as per graph on Paragraph 23.

42 The appointment of an ill-equipped board, which proceeded to make poor decisions set off a race to the bottom, including:

42.1 The unilateral setting up of Denel Asia and the Board decision to institute a court challenge to the Minister of Finance to force a PFMA Section 51 approval and PFMA Section 54 concurrent approval sent negative signal to stakeholders, especially the financial institutions.

42.2 The abrupt abandonment of ongoing partnership arrangements in the land vehicles development business and the acquisition of electronic capability. Plans which had been formulated by the Executive and outgoing Board.

42.3 The dismissal of an executive team (Riaz Saloojee and Fikile Mhontlo) that had performed a stellar job in turning around the business.

42.4 The importance of maintaining good governance practices seemed to have been lost on the Mantsha Board leading to loss of confidence in Denel amongst critical stakeholders.

43 Denel was forced to settle R455 million bridging facilities with Nedbank and R400 million with ABSA secured during the acquisition of BAE Land Systems South Africa (now known as Denel Vehicle Systems). In essence Denel had to find R855 million to settle the facilities.

44 Denel saw its general banking facilities not being renewed when they became due. The execution of the order pipeline slowed down due to an inability to secure bank guarantees for new equipment orders, and the early banking facilities settlement drained cash that should have paid suppliers, who in turn reduced deliveries and tightened delivery terms.

45 Denel operations ground to a halt as the business did not have enough internal funds and could not secure external financial support to generate the cash it requires to meet its obligations.

46 The result was that the defence industry, which is dependent on Denel with 6 jobs for every job at Denel, saw some of the businesses retrenching to reduce their operations footprint and some severe instances going into liquidation due to Denel not being able to pay for delivered components or new deliveries.

DENEL ASIA

DPE PFMA SECTION 54 APPLICATION PROCESS

47 DPE PFMA Section 54 application process:

47.1 The Department instituted a PFMA Pre-Notification Phase to enable the SOC to give the Minister a heads up on the transaction being conceived.

47.1.1 The Minister, advised by the Department, would be able to express his/her views on the transaction before resources are expended in putting together the transaction.

47.1.2 The Department would seek understanding from the SOC executives on the rationale for the transaction.

47.1.3 Advised by the Department, the Minister can either decline or approve that the SOC proceed to the PFMA Application stage. The approval would accompanied by guidance to the SOC Board on the information that should accompany the PFMA Application.

47.1.4 The process is not legislated and does not have specified timelines though the Department would seek to respond, through Minister, to the SOC within 30 days.

47.2 The SOC on receiving the Pre-Notification approval can proceed with the submission of the PFMA Section 54 application:

47.2.1 The timing of the submission of the application is the prerogative of the SOC. The Department, through the Minister, as per legislation has 30 days to respond to the SOC. The norm due to the effort required to process the application within 30 days is wholly inadequate and the Department would write to the SOC to seek an extension.

47.2.2 The processing of the application is preceded by engagement with SOC Executives and subject matter experts (within DPE, at SOC, and independent) to test the business case submitted by the SOC and other information submitted.

47.2.3 The National Treasury and the Policy Departments would also be engaged to ensure alignment with wider Government objectives, policies and regulations.

47.2.4 Informed by the engagements, the Department would proceed to put together a submission to Minister to either approve or decline the transaction.

47.2.5 Further, where Minister of Finance concurrence or approval (Section 51(1)) is required, the Minister would notify the SOC to ensure this approval before concluding the transaction.

DENEL ASIA PFMA APPLICATION

48 A pre-notification letter dated 29 October 2015 from Denel to DPE in terms of section 54 (2) of the PFMA was received on 30 October 2015. I attach hereto a copy of the said notification as Annexure **KT4**.

49 After careful consideration of the notification by my team, we drafted a decision memorandum to the DPE Minister. The memo set out to advise of the notification and our recommendations regarding the application. I attach hereto a copy of the memorandum as Annexure **KT5**.

50 On 23 November 2015, the Minister granted Denel an in principle approval to continue discussions with VR Laser subject to a condition that it complied with, amongst others, the following conditions:

50.1 the PFMA applications had to be accompanied by:

50.1.1 A comprehensive business case to enable the Executive Authority and the Minister of Finance to optimally apply their minds regarding this transaction;

50.1.2 A comprehensive due diligence report on the financial regulatory requirements of the Hong Kong jurisdiction as it relates to foreign owned entities;

50.1.3 A comprehensive due diligence of VR Laser, which includes its financial standing, ownership, capabilities (including its product and service range) as well its client base.

50.2 Denel was further instructed to ensure that:

50.2.1 There was adequate governance oversight regarding the transaction, and that issues of conflict of interest, real or perceived, are adequately dealt with.

50.2.2 Risk exposure to Denel and the Shareholder is minimised.

51 I attach hereto a copy of the letter from the DPE Minister to Denel's Daniel Mantsha, dated 23 November 2015, as Annexure **KT6**.

52 The letter by the Minister highlighted the concerns that the department had raised in its evaluations and set out in certain terms a list of requirements that had to be complied with before the application could be approved.

53 On 10 December 2015, Denel made a formal application to the DPE Minister seeking approval to establish Denel Asia SOC Limited, in terms of Section 54 (1) and 54 (2) of the PFMA. I attach hereto a copy of the application as Annexure **KT7**.

54 I am aware that Denel also applied to the Minister of Finance in terms of section 51 (1) (g) of the PFMA for a similar approval. I attach hereto a copy of the letter to the Minister of Finance as Annexure **KT8**.

55 Denel submitted both PFMA Section 51(1) (g) and 54(1) and 54(2) applications on 11 December 2015 with all the required documents. Section 51(1) (g) is the reserved responsibility for the Minister of Finance.

56 Section 54 (2) approval, specifically for Denel, is the concurrent function of the Executive Authority with the Minister of Finance in line with R1.85 billion Government Guarantee given to Denel in 2012.

DPE DECISION MEMORANDUM

57 On 24 December 2015, my team responsible for Denel in the DPE drafted a Decision Memorandum as well as a Cabinet Memorandum advising the Minister that it had reviewed the PFMA application and that it was not in a position to advise her on the position she should take in regards to the transaction as:

57.1 The detailed information expected in the application as per requirements in the previous decision memorandum had not been provided by Denel.

57.2 A further engagement with the Denel executives was required as the information provided was either not comprehensive or raised further questions.

58 In line with paragraph 3.10 of the memo to Denel, (dated 16 November 2015), at paragraph 3 of that memo we highlighted areas of discussion with Denel, such as:

58.1 The outstanding Finance Minister approval;

58.2 Funding plans were not included in the application;

58.3 A business plan with a lack of detail and depth;

58.4 The suitability of VR Laser based on due diligence reports;

58.5 The due diligence of the shareholders of VR Laser and political implications; and

58.6 The lack of detail in the funding plan for the establishment of Denel Asia.

59 As part of the review of the Denel Asia PFMA application, we also considered what caused an about turn from going at it alone or with its existing partners in the Pacific Asia market. Another question was how they ended up with VR Laser, a company that was essentially South African.

60 Due to lack of information in the Denel response and the due diligence, report attached to the application, red flags were raised on VR Laser Asia. Based on that and other factors mentioned above, we recommended to the Minister that she request further compliance with the list of requirements, which we again listed in the Minister's letter to Denel.

61 Effectively, the Minister's letter would have meant that the engagement with Denel on the PFMA application would have continued, thus thwarting Denel's assumption of a "deemed approval" in terms of PFMA Section 54(3).

62 I attach hereto a copy of the said letter, dated 24 December 2015, as Annexure **KT9**.

63 The decision memorandum and letter for Minister to sign and send to Denel were delivered by email to both the Director-General, Mogokare Richard Seleke and the Ministry (Ministers' Advisors Annelize Van Wyk and Daniel Plaatjies and Deputy Minister Head of Office, Mr Phillip Mbanyana) on 24 December 2015 (Annexure **KT10**). An original of the memo was delivered by the office professional assistance who would have registered the document in the register on the same day.

64 I received no further communication from neither the DG nor the Minister following the submission of my memorandum, except for the memorandum being returned from the DG office (Annexure **KT11**) on 11 January 2016 without instruction on what the team should do with the memorandum.

TIMING OF THE APPLICATION

65 In my own analysis, I did consider the timing of the formal PFMA application to be curious in that:

65.1 The turnaround period from the PFMA Prenotification response by Minister, 23 November 2015, to receiving the PFMA Application, 11 December 2015, was rather short considering the requirements we had placed on Denel for the application submission.

65.2 The submission came through to the department a few days before the start of the festive season, and the Department was instructed by the Ministry to process it before closure.

65.3 The pressure that the team and I were placed under was quite disconcerting, as we knew that Denel would be closing on 15 December 2015, therefore not much would be done to conclude the transaction during the month of December 2015.

DENEL'S ANNOUNCEMENT OF THE ASSUMED APPROVAL

66 On 5 February 2016, Denel informed the Executive Authority that it had proceeded to implement the transaction as it assumed that approval was granted in terms of Section 54(3) of the PFMA, which states that if no response was received from the Executive Authority within thirty days, the application will be deemed to have been granted.

67 The announcement by Denel caught some of us in the Department by surprise and seemed ill-informed, as besides PFMA Section 54, PFMA Section 51, which refers to Minister of Finance approval for establishment of a new state entity, was

also applicable and did not have time limits by which the Executive Authority should have responded.

68 Further, it made no sense why Denel Board did not, in the period leading to the expiry of the 30 days (10 January 2016), formally inform the Ministers of Public Enterprises and Finance of their intention to invoke PFMA Section 54(3), deemed approval provision. Common courtesy and recognition of Ministers' authority would have required such response from Denel. In the time that I had been with the Department, there had not been an SOC that had behaved in this manner and checking with colleagues that had been longer in the Department, they also did not recall such a development.

69 However, from subsequent engagements between the Minister and the Denel Board, it was clear that Minister had come to terms with Denel Board decision and jointly they were looking for ways to get the Minister of Finance and National Treasury to come around to the DPE and Denel position.

THE RELATIONSHIP WITH THE DIRECTOR-GENERL, MOGOKARE RICHARD SELEKE

70 The attitude of the Department towards the Denel Asia transaction started to change during 2016, post the announcement by Denel of its partnership with VR Laser Asia to form Denel Asia.

71 Prior to the announcement of the partnership, the Department had been adamant that the choice of partners for the Denel Asia transaction was unfortunate and that Denel had been delinquent in invoking PFMA Section 54(3). The Minister had been strangely rather quiet and removed from the matter during this period – at least I was not aware of her position.

72 It is my considered view that I and my unit had been deliberately targeted to ensure a change in position:

72.1 DG Seleke had been appointed as Director General of the Department on 01 December 2015. It became clear on starting that he was intent on getting rid of some of the officials in the Department, as he eloquently put it at the strategic session with the senior managers on 20 January 2016 that he will be "thinning" the Department and that some of the officials should expect to exit the Department. The statement left some of the officials uneasy and in the coming months there was a significant turnover of senior managers, with people opting to jump before being pushed. I was also unsettled.

72.2 On 4 February 2016, the Mail and Guardian newspaper had sent enquiries to DG Seleke regarding the Denel Asia transaction and the involvement of the Gupta associates (as relayed to my team by DG Seleke).

72.2.1 The Mail and Guardian newspaper, as per its edition of 5 February 2016, had found that Salim Essa, a known associate of the Gupta family was the majority shareholder in VR Laser South Africa and VR Laser Asia. The report also cited that Mr Duduzane Zuma was the shareholder through JIC Mining Services in VR Laser South Africa. (Denel on 29 January 2016 had announced the tie up with VR Laser but had not indicated the personalities behind the transaction in its tie up with VR Laser Asia.)

72.2.2 On 4 February 2016, the Minister and DG Seleke were at a Cabinet Lekgotla, but DG Seleke felt it necessary to leave the session and come through to my team planning session, which was at Protea Hotel Manor in Hatfield.

72.2.3 DG Seleke indicated that he had been up from early morning fielding enquiries from the newspaper. He accused my team and me of leaking the story to the Mail and Guardian and indicated that further action against whomever is found to have been the source will be forthcoming.

72.3 The encounter had left me anxious for my future in the Department. The manner and the tone in which he addressed my team and I was rattling to such an extent that I believed that I was soon to be suspended or fired.

72.4 2016 was the last year of my contract, which was expiring on 30 November 2016. DG Seleke on commencing his duties had raised the subject of paying out my contract, which he said was on the instruction of the Minister. The Minister, according to DG Seleke, had been unhappy with my appointment of a Director Human Resources without consulting with her. I had indicated to DG Seleke that I would prefer to leave under amicable terms and paying out the remainder of my contract was acceptable to me. We had a number of discussions but a formal offer was not made. I concluded that DG Seleke had opted to let my contract run out.

72.5 It was therefore not a surprise when my contract on expiring at the end of November 2016 was renewed for a month to the end of December

2016 instead of the norm of 3 to 5 years. The message was clear: my time at DPE had come to an end. I then proceeded to pack my personal items and take them home. I was aware that

72.6 Deputy Minister Martins had also intervened with the Minister. On 22 December 2016, which would have been my last day at DPE I received a letter that my contract had been extended by an additional 1 year. This was of course a relief as I did not have another job.

73 The result of these episodes was I made a decision, and I advised my team accordingly, that we should be circumspect on matters that could be at odds with our principals views or positions, and that with regard to Denel Asia we should act on instruction. The result was that when Minister and DG advised that they accept the "deemed approval status" of Denel Asia, as indicated in their respective letters of 15 July 2016 and 20 September 2016 (Annexures **KT12** and **KT13**). I drafted the letters as directed by the principals and submitted for signature and transmission to National Treasury.

74 I was in a self-preservation mode and so were most of the colleagues in the Department.

MEETING IN CAPE TOWN

75 On 16 or 18 February 2018 I joined DG Seleke in a meeting with Chairperson of Denel Board, Mr Daniel Mantsha. The meeting was in Cape Town and I happened to be in the Cape Town office at the time. The meeting was to discuss Denel Asia, and DG Seleke and Chairperson Mantsha were preparing for a meeting that the two were to have with the Minister.

76 In the meeting it became clear that DG Seleke was intent on ratifying the Denel decision to announce the Denel Asia venture. I pointed out to DG Seleke and Chairperson Mantsha that the meeting was irregular in that it has not happened that an SOC is party to a decision that affects it. This led to a long and acrimonious debate, however it was made clear to me that the decision is made and memorandum should be amended accordingly.

77 The memorandum was amended to reflect that the Department and Minister had on 24 December 2015 granted a conditional approval of the transaction (Annexure **KT14**).

78 The conditions in the revised memorandum were:

78.1 Denel secures an irrevocable commitment by VR Laser to make all the required funding to establish and run the affairs of Denel Asia;

78.2 Denel should implement a comprehensive risk mitigation plan to address the risks raised in the due diligence reports and report progress on the effectiveness of the mitigation actions in the agreed performance reports; and

78.3 For the transaction, Denel has to receive the following approval from the Minister of Finance: Sections 51(1) (g) and 54(2)(a) as required by R1.85 billion government guarantee conditions;

79 DG Seleke and Chairperson Mantsha left our meeting to their meeting with Minister Brown. I did not hear further on the outcome of their discussion. However, it became apparent over time that the Minister did not sign off on the revised memorandum as it was never heard of again.

DENEL AND VR LASER

80 The Denel Asia matter was not the first time that Denel had had a business relationship with VR Laser Services. The business had made inroads into Denel through Denel Land Systems. At the time Stephen Burger, was a CEO of Denel Land Systems.

81 VR Laser Services had been a supplier of cut and weld armoured steel for the production of armoured vehicle: armoured personnel carriers, artillery systems, armoured combat vehicles, armoured support vehicles including ambulances, etc.

82 Forensic investigations at Denel by Ngidi Forensic Services dated March 2018 had showed that Denel Land Systems "irregularly" awarded VR Laser Services a contract for provision of metalwork services for a period of 10 years, which contract had conservatively been estimated at R10 billion (Annexure **KT15**).

CONCLUSION

83 I have reflected in this short statement on what appears to me to be relevant facts. However, I am prepared to provide further detail should it be required and also reserve the right to amplify and supplement this statement.

SIGNED AT **ARCADIA** ON THIS DAY **25 FEBRUARY 2019**.

WITTNESS 1

MR KGATHATSO TLHAKUDI

WITTNESS 2

ANNEXURE "KT1"

public enterprises
Department:
Public Enterprises
REPUBLIC OF SOUTH AFRICA

DECISION MEMORANDUM

DEPARTMENT OF PUBLIC ENTERPRISES
PRIVATE BAG/PRIVAAT SAK X15
2015 -08- 13 11:30
HATFIELD 0028
DEPARTEMENT VAN OPENBARE ONDERNEMINGS

TO : **MS LYNNE BROWN, MP**
MINISTER

FROM : **MR MELANCHTON MAKOBE**
ACTING DEPUTY DIRECTOR-GENERAL: LGR

FILE REF : **10/2/5**

IDMS REF : **182874**

SUBJECT : **DENEL SOC LTD 2015 ANNUAL GENERAL MEETING DOCUMENTATION AND ANNUAL FINANCIAL STATEMENTS**

DATE : **29 JULY 2015**

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1. PURPOSE

1.1. To brief the Minister on the agenda items, proposed motions and resolutions taken at the Denel SOC Ltd (Denel) 2015 Annual General Meeting ("the AGM") that took place on 23 July 2015 at the Denel offices, at Denel Dynamics Auditorium, Nellmapius Drive, Irene.

1.2. To request the Minister to note, for the record, resolutions taken at the Denel 2015 AGM; and

1.3. To advise the Minister on the overall performance of Denel for the financial year ended 31 March 2015.

2. SUMMARY

2.1. Section 61 (7) (b) of the Companies Act 71 of 2008 ("the Companies Act") requires a public company to hold an AGM once in every calendar year, but not more than 15 months after the date of the previous AGM. Denel has complied with the requirements of the Companies Act in that its previous AGM was on 15 August 2015, 13 calendar months following the previous AGM.

- Confidential -

2.2. Section 62 (1) of the Act provides that a Company must deliver a notice of the shareholder's meeting fifteen (15) business days before the meeting, unless the Memorandum of Incorporation ("MOI") provides for a shorter or longer period.

2.3. Denel's MOI provides that a notice of the AGM must be delivered to the Shareholder not less than 15 business days before the AGM. Denel submitted its official AGM notice and pack on 02 July 2014, hence this provision has been complied with.

2.4. In brief, the motions proposed by Denel for adoption by the Shareholder includes the following:

2.4.1. To approve the Minutes of the Twenty First Annual General Meeting held on 15 August 2014;

2.4.2. To note the audited Annual Financial Statements for the year ended 31 March 2015, the Integrated Report including the Directors' Report, Audit Committee, Remuneration, Social and Ethics Committee report and the External Auditors report;

2.4.3. Retirement, Appointment and Re-appointment of Non–Executive Directors;

2.4.4. Appointment of External Auditors for the year 2015/16;

2.4.5. Dividends for the financial year ended 31 March 2015;

2.4.6. To Note the remuneration of Prescribed Officers for the financial year ended 31 March 2015;

2.4.7. Approval of the Directors' fees for the year ending 31 March 2016;

2.4.8. To approve the Group Executive Committee Remuneration for the year ending 31 March 2015 and proposed increase effective 1 April 2015;

2.4.9. To approve that the company may provide financial assistance to its subsidiaries, section 45 of the Company's Act 2008,and section 14.1.1.3 of the Memorandum of Incorporation;

2.4.10. To note the Board Evaluation Report for the year ended 31 March 2015.

2.4.11. To Note the schedule of Directors' attendance of Board and Committee meetings for the year ended 31 March 2015;

2.4.12. Noting of the disclosure of Director's interest for the year ended 31 March 2015.

3. ANALYSIS AND FINDINGS

3.1. The essence of this memorandum is to communicate to the Minister a record of the documents received from Denel, omissions and/or areas of non-compliance regarding the Denel AGM held on 23 July 2015.

3.2. Section 61 (8) of the Companies Act provides that the AGM must, at a minimum, provide for the presentation of the Directors' Report, audited Annual Financial Statements (AFS), the Audit Committee Report and as any matters raised by the Shareholder, with or without advance

notice to the Company. The table of recommendations on each resolution taken is attached as **Annexure "1"**.

3.3. Section 55 (1) (d) of the Public Finance Management Act, 1 of 1999 (the PFMA) provides that the Accounting Authority (Board) of a public entity must submit within five months of the end of a financial year to the relevant Treasury and to the Executive Authority (Minister) responsible for that public entity an annual report on the activities of that public entity during that financial year, the financial statements for that financial year after the statements have been audited and the report of the auditors on those statements. A copy of the Denel AGM Agenda is attached herewith and marked as **Annexure "2"**.

4. PROPOSED AGENDA ITEMS

4.1. Agenda Item No. 1: Opening and Welcome

4.1.1. Although the Annual General Meetings are Shareholder meetings, in terms of Denel's MOI the Chairperson should preside as the Chairperson at the AGM. In light of the impact of the Act to the South African Company law and legal landscape, the Department is of the view that the Chairperson of the Denel Board should preside as the Chairperson at the AGM. This does not present a material legal impediment to the Department but instead avoids a situation where the Minister (as Shareholder Representative) presides over a meeting where she is expected to approve or decline (as the case may be) the resolution put before her.

It was recommended that the Minister:

a) Note that the Chairperson of the Denel Board is the Chairperson of Denel's AGM; and

b) Note that the quorum necessary for the AGM is the Minister as the sole member of the company (or a duly-appointed proxy) and that the AGM is thus duly constituted.

4.2. Agenda Item No. 2: Safety Briefing and Evacuation

4.2.1. This is a standard requirement in terms of Denel's Health and Safety Policy and it normally addresses evacuation procedures in the event of fire or similar type emergencies.

It was recommended that the Minister note this agenda item.

4.3. Agenda Item No. 3: Notice of the Meeting

4.3.1. In terms of Section 62 (1) of the Companies Act, the company must deliver a notice of the Shareholders' meeting to all shareholders, at least 15 business days before the meeting. Section 12.1.1 provides that the Board shall convene an Annual General

Meeting at least once a year but no later than 15 (fifteen) months after the date of the previous Annual General Meeting.

4.3.2. Denel has complied with this legislative requirement in that the notice for the Denel AGM, together with a full pack of relevant documents, were received by the Department on 02 July 2015, 15 business days before the AGM scheduled for 23 July 2015 and complied with its MOI and the Companies Act. A copy of the Denel AGM notice is attached herewith and marked as **Annexure "3"**.

It was recommended that the Minister note compliance of Denel's AGM Notice with the provisions of the Companies Act.

4.4. **Agenda Item No. 4: Address by the Minister**

4.4.1. This is an address by the Minister on strategic issues that affect Denel regarding the business, operational and governance issues. This item serves as a communiqué by the Minister, highlighting issues of concern regarding the overall performance of Denel as well as compliance issues. A copy of the address is attached herewith as **Annexure "4"**.

It was recommended therefore that the Minister notes that this was used to reflect on Denel's business and acknowledged the role played by the Board to steer the company towards profitability.

4.5. **Agenda Item No. 5: Approval of the Previous Minutes**

4.5.1. At the AGM held on 15 August 2014, the Minister was accompanied by the Deputy Minister (Mr BG Magwanishe), former Director-General (Mr T Matona), DDG: Legal, Governance and Risk (Ms M Mokholo), former Minister's Special Advisor (Mr B Roberts) , DDG: Manufacturing Enterprises (Mr Kgathatso Tlhakudi), CD: Financial Analyst (Ms Vuyo Tlale), CD: Governance (Ms Orcilla Ruthnam), D:Governance (Ms Shelley Pather), former Director: Defence (Mr E Jele), Mr T Matheza, Mr. L McPatle. The Minutes are a true reflection of what transpired at the meeting. A copy of the previous AGM Minutes is attached herewith as **Annexure "5"**.

It was recommended that the Minister accept the Minutes of the previous AGM held on 15 August 2014 as a true reflection of the proceedings at the meeting.

4.6. **Agenda Item No.6. Matters arising from the previous Minutes of the AGM held on 15 August 2014.**

4.6.1. A report on the status of matter arising from the Minutes of the previous AGM. There was only one matter arising from the minutes of the AGM held on 15 August 2014. It

has been resolved and the report was submitted to the Minister on 20 November 2014. A copy of the report is attached herewith as **Annexure "6"**.

4.7. **Agenda Item No. 7: Board Social and Ethics Committee ("SEC")**

4.7.1. The purpose of the SEC is to advise the Board in regard to responsible citizenship, and the ethical relationship between the company and society. It manages the company's legal and moral obligations for its economic, social and natural environment, including the objectives and standards of the company's conduct and activities.

4.7.2. The SEC was mandated to oversee the five (5) main areas of focus for the 2014/15 financial year and are the following:

4.7.2.1. Fraud and corruption;

4.7.2.2. Corporate Social Investment;

4.7.2.3. Stakeholder Management; Transformation including BBBEE status; and

4.7.2.4. Occupational Health and Safety.

4.7.3. The Committee was apprised of the Company's fraud prevention measures and is satisfied that these measures were effective.

4.7.4. The mandate of the SEC is reviewed annually for relevance and the annual work plan for the following financial year is developed and agreed to in advance, in terms of the priorities and areas that need special attention, for example, employment equity, BBBEE status, fraud and prevention measures. A copy of the SEC report is attached herewith as **Annexure "7"**.

It was recommended that the Minister notes Denel's Social and Ethics Committee report.

4.8. **Agenda Item No. 8: Presentation of the Annual Financial Statements for the period ended 31 March 2014.**

4.8.1. **Responsibility and Accountability**

4.8.1.1. The Board provides strategic leadership and oversight, and oversees the control environment in order to achieve and sustain value to the company's shareholder and stakeholders. The Board ensures adherence to principles of good governance and accountability as espoused in King III and its Board Charter. All the members of the Board are individually and collectively aware of the responsibilities to the group's stakeholders, and each director brings experience, independence of character and judgment. The Board ensures regular reviews of its performance and core governance.

4.8.1.2. The Board is responsible for the preparation and fair presentation of the financial statements in accordance with International Financial Reporting Standards (IFRS) and the requirements of the PFMA, the Companies Act and for such internal controls as the Directors determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

4.8.1.3. During the year under review, the Directors retained full effective control over the group and monitored management in implementing the approved plans, risk management and strategies. The Board is satisfied that the risk management processes are effective. The integrated Report for 2014/2015 is attached herewith as **Annexure "8"**.

4.8.2. **Director's Opinion**

4.8.2.1. The Board of Directors is of the opinion that the consolidated Annual Financial statements present fairly the financial position of Denel and its subsidiaries and the results of their operations and cash flows for the year ended 31 March 2015.

4.8.2.2. The Denel Board is satisfied that the group has in all material respects complied with the provisions of the PFMA, the Companies Act and other applicable legislation.

4.8.3. **Independent Auditors' Report**

4.8.3.1. The responsibility of the Auditors is to express an opinion on the financial statements based on their audit. They conduct this in accordance with the Public Audit Act, 25 of 2004, the General Notice issued in terms thereof and International Standards on Auditing. Those standards require the Auditors to comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatements.

4.8.3.2. The Denel auditors are of the opinion that the consolidated and separate financial statements present fairly, in all material respects, the financial position of Denel and its subsidiaries and their financial performance and cash flows for the year then ended 31 March 2015 in accordance with IFRS and the requirements of the PFMA and Companies Act.

4.8.3.3. The auditors considered Denel's internal control environment relevant to the audit of the financial statements, performance report and compliance with laws and regulations.

4.8.4. Report of the Audit and Risk Committee

4.8.4.1. The Audit and Risk Committee ("Committee") reports that it has adopted appropriate formal Terms of Reference ("ToR") as approved by the Board and is satisfied that it has discharged its responsibilities as per the Companies Act and PFMA, and further responsibilities assigned to it by the Board as contained in the ToR.

4.8.4.2. The Committee reports that it has adopted appropriate formal ToR as approved by the Board and is satisfied that it has discharged its responsibilities as per the Companies Act and PFMA, and further responsibilities assigned to it by the Board as contained in the ToR.

4.8.4.3. The Committee has satisfied itself that the Group Finance Director (GFD) has appropriate expertise and experience. It has also satisfied itself with the appropriateness of the expertise and the adequacy of resources of the finance function and experience of the senior members of management responsible for the financial function.

4.8.5. Analysis of the Annual Financial Statements for the year ended 31 March 2015.

4.8.5.1. Statement of Comprehensive Income

Statement of Comprehensive Income	2015 Rm	2014 Rm	Variance Rm	Variance %
Turnover	5 852	4 588	1 264	28%
Cost of Sales	(4 715)	(3 689)	(1 026)	28%
Gross Profit	1 137	899	238	26%
Other Income	137	204	(67)	-33%
Other operating expenses	(939)	(879)	(60)	7%
Operating profit/(Loss)	335	224	111	50%
Finance costs	(176)	(140)	(36)	26%
Finance income	53	48	5	10%
Share of profit/(loss) of associates	64	58	6	10%
Profit/(Loss) before tax	276	190	86	45%
Income tax expense	(6)	4	(10)	-250%
Profit/(Loss) for the year	270	194	76	39%

Table 1: Abridged Income Statement

4.8.5.1.1. Denel recorded 28% revenue growth when compared against the same period in the prior year. The key entities that contributed to revenue performance include DLS, DD, DAv and PMP. Export revenue constitutes 52% of total revenue and the remainder being local revenue.

4.8.5.1.2. DLS generated good sales from the contracts on Hoefyster, AV-8 and SAPS Maintenance Repair and Overhaul (MRO) of R5 rifles. DD generated sales from the A-Darter and Seeker 400 contracts mainly from export orders. DAv generated revenue mainly from additional MRO required as a result of Department of Defence's (DoD) participation in peacekeeping missions. The introduction of brokering services, which are once off in nature at PMP boosted revenue performance.

4.8.5.1.3. Operating expenses increased conservatively when taking into account revenue growth. The main components of the operating expenses are staff costs and Research and Development (R&D).

4.8.5.1.4. The net profit for the period ending 31 March 2015 is R270 million and it has increased by 39% when compared against the profit of R194 million which was achieved in the prior year. This is mainly due to higher revenue performance, increase in finance income as well as share of profits in associates.

4.8.5.2. **Statement of Financial Position**

Statement of Financial Position	2015 Rm	2014 Rm	Variance Rm	Variance %
Assets				
Property, Plant and Equipment (PPE)	915	861	54	6%
Investment Properties	590	534	56	10%
Inventories	1 511	1 020	491	48%
Trade receivables and other receivables	3 520	2 930	590	20%
Cash and short-term deposits	1 909	1 513	396	26%
Total Assets	9 687	8 089	1 598	20%
Total equity	1 927	1 664	263	16%
Liabilities				
Loans and borrowings	888	1 616	(728)	-45%
Advance payments received (Long term)	2526	2066	462	22%
Trade and other payables	1 306	1 100	206	19%
Loans and borrowings	1 270	259	1 011	390%
Advance payments received (Short term)	940	628	312	50%
Total liabilities	7 760	6 425	1 335	21%
Total borrowings	2 158	1 875	283	15%
Total prepayments	3 466	2 694	774	29%
Total equity and liabilities	9 687	8 089	1 598	20%

Table 2: Abridged Statement of Financial Position

4.8.5.2.1. The current state of Denel's financial position is concerning. The high level of prepayments, anticipated funding requirements for the two PFMA acquisitions, the redemption and re-issue of commercial paper are adversely impacting the financial position of the entity.

4.8.5.2.2. Even though the Department is cognisant that the defence industry requires high working capital management which then places defence companies in a challenging position from a cash management point of view, Denel's working capital management is concerning. This is demonstrated by the increase in inventory, trade receivables and trade and other payables.

4.8.5.2.3. The continued use of prepayments to execute customer orders is another area of concern for the Department. Prepayments constitute 44% of total liabilities. Currently the total prepayments are approximately R3.5 billion In the event that customer's withdraw funds invested in programmes, Denel will be exposed to liquidity risk.

4.8.5.2.4. The increase in loans and borrowings is as a result of R1 billion of the DMTN programme moving to short-term liabilities. Meaning it will be due in the new financial year. Commercial Paper redemption will

be due in the current financial year. The amount linked to this is R1 billion. In addition, Denel utilised R7.6 billion from a total of R10.4 billion in bank facilities as at 31 March 2015. The facilities available amount to R2.8 billion.

4.8.5.2.5. Denel has a cash balance of R1.9 billion which translates into an increase of 26% when compared against the prior year. However, R1.3 billion of the cash balance is ring-fenced for the Hoefyster project, meaning the actual balance available is R600 million. When taking into account the required funding for the C2 PFMA applications and debt obligations mentioned in paragraph 4.8.5.2.4, the liquidity of the entity is at risk.

4.8.5.3. **Statement of Cash Flows**

Statement of Cash Flows	2015 Rm	2014 Rm	Variance Rm	Variance %
Net cash flows from operating activities	212	474	(262)	-55%
Receipts from customers	5 256	4 086	1 170	29%
Payments to suppliers and employees	(5 657)	(4 674)	(983)	21%
Cash utilised in operations	(401)	(588)	187	-32%
Net cash flows used in investing activities	(177)	(206)	29	-14%
Net cash flows from financing activities	361	(52)	413	794%
Net increase in cash and cash equivalents				
Cash and cash equivalents at the beginning of the	1 513	1 297	216	17%
Cash and cash equivalents at the end of the year	1 909	1 513	396	26%

Table 3: Abridged Statement of Cash Flows

4.8.5.3.1. Denel is not generating sufficient cash from operations. This is demonstrated by the negative cash utilised in operations.

4.8.5.3.2. The decrease in cash used in investing activities is primarily due to a decline in the cash utilised to acquire Property, Plant and Equipment (PPE), repayments of loan advance to associated companies and acquisition of additional shares in an associate company.

4.8.5.3.3. The significant improvement in cash flows from financing activities is mainly due to an increase in interest bearing borrowings by R1.1 billion.

4.8.5.3.4. Despite an improvement in the cash balance by 26% compared to the prior year, the Department has concerns as indicated above in 4.8.5.2.5

4.8.5.4. Shareholder's Compact

Key Performance Area	Key Performance Indicator	2014/15	
		Long Term Target	Actual
Security of supply and retention of capabilities in areas required by the DoD and MV	Retained strategic capabilities in support of the DoD and MV's requirements	100%	100%
Programme delivery	Milestone achieved per contract deliverables	85%	>97%
Investment in R&D	Self-funded R&D as a % of revenue	3%	2%
Revenue	Increase in revenue year on year	12%	28%
Profitability management	EBIT margin	5%	7%
Order cover	% of orders concluded in respect of the coming year as a % of revenue budget for that year	60%	77%
Cash flows from operating activities	Cash-flow from operating activities before working capital changes as a % of revenue	2%	8%
Operating expenses	Operating costs as a % of revenue	23%	17%
Maximise the appointments from designated groups in order to address employment equity requirements	ACI as % of total appointments	75%	87%
	Women as % of total appointments	20%	30%
Local content	Local procurement as % of total procurement	70%	67%
Preferential procurement and enterprise development (current baseline for women owned = 1.3%)	Procurement from black owned suppliers as defined in the B-BBEE codes, as % of local spend	20%	22%
	B-BBEE (recognised spend as % of local spend)	70%	96%
	Black women owned as defined in the B-BBEE codes (% of local spend)	3%	8%
	Black youth owned as defined in Annexure B, (% of local spend)	3%	1%
	Small and emerging enterprises suppliers developed (number of beneficiaries)	20	114
B-BBEE level	B-BBEE contributor level	Level 3	Level 2
Training spend	% of employee cost	3%	4%
Skills development - scarce and critical skills	Total number of engineering trainees (bursaries and internship)	90	92
	Total number of artisan trainees	100	157
	Total number of technician trainees	-	9
	Total number of DTA artisan and technical skills trainees (enrolments during the year)	300	355
Employment - scarce and critical skills	Increase number of jobs	100	275
Corporate social investment	Spend on CSI as specified in the B-BBEE codes	1%	2%

Table 4: Shareholder's Compact

4.8.5.4.1. Denel achieved 88% of the Shareholder Compact (SHC) targets. The Department acknowledges the improvement in the KPI on

BBBEE contributor level. Denel improved to a level 2. With regards to the non-achievement of KPIs that fall under Socio-Economic

objectives, the Department will raise this matter with the executives and in the Minister's address for the Annual General Meeting (AGM).

4.8.5.5. Directors' Remuneration

4.8.5.5.1. Executive Directors' Remuneration

EXECUTIVE DIRECTORS	2015 R'000	2014 R'000
Mr R Saloojee	4 180	3 972
Mr F Mhlontlo	3 489	3 318
Sub Total	7 669	7 290
PRESCRIBED OFFICERS		
Ms N Davies[1]	1 659	1 384
Mr JV Morris[2]		2 892
Mr VM Ngidi[3]		140
Mr ZN Ntshepe	2 204	2 094
Maj gen (Ret.) OA Schür[4]		180
Mr JM Wessels[5]	2 115	1 921
Sub total	5 978	8 611
Total	13 647	15 901

1 Appointed 1 July 2013
2 Resigned 30 September 2013
3 Passed away 27 April 2013
4 Resigned 30 April 2013
5 Appointed as Group COO 1 May 2013

Table 5: Executive Director's Remuneration

4.8.5.5.1.1. The executive director's remuneration decreased by 14%. This is mainly due to the non-filling of the position vacated by Mr. JV Morris.

4.8.5.5.2. Non-Executive Director's Remuneration

NON-EXECUTIVE DIRECTORS	2015 R'000	2014 R'000
Ms MJ Janse van Rensburg (Interim chairman)[1]	647	283
Mr NR Kunene (Chairman)[2]	294	773
Adv G Badela	176	200
Dr GC Cruywagen	342	310
Prof T Marwala[3]	49	76
Ms Z Mathenjwa	193	203
Mr NJ Motseki	111	136
Mr M Msimang	155	222
Mr BF Ngwenya	140	230
Prof SM Nkomo	293	354
Adv MS Ntshikila	103	226
Ms B Paledi[3]	35	167
Mr MV Ratshimbilani	109	209
Total	2 647	3 389

1 Interim chairman from 15 August 2014
2 Chairman resigned 15 August 2014
3 Resigned 15 August 2014

Table 6: Non-Executive Director's Remuneration

4.8.5.5.2.1. The non-executive director's remuneration decreased by 22%. This is mainly due to the interim chairperson not earning the full term chairpersonship remuneration. Furthermore, there was a resignation during the financial year and the position was not filled.

4.8.5.5.3. **Auditors Opinion**

4.8.5.5.3.1. The auditors expressed an unqualified audit opinion with no emphasis of matter for Denel's 2014/15 financial statements. Auditors also did not identify any material findings on the usefulness and reliability of the reported performance information on predetermined objectives i.e. SHC targets.

4.8.5.5.3.2. In the past years, Denel received unqualified audit opinions with emphasis of matter and in the current year the company managed to achieve an unqualified audit opinion without an emphasis of matter.

It was recommended that the Minister addresses the Board on financial performance of the Company and:

a) Note the Annual Financial Statements for the year ended 31 March 2015;

b) Notes the report of the Independent Auditors for the year ended 31 March 2015 in accordance with the provisions of the Act;

c) Note the Directors' Report, as incorporated in the audited Annual Financial Statements for the year ended 31 March 2015; and

d) Note the Audit Committee Report, as incorporated in the audited Annual Financial Statements for the year ended 31 March 2015 in accordance with the provisions of the Act;

4.9. **Agenda Item No. 9: Rotation/retirement and Appointment/re-appointment of Non-Executive Directors**

4.9.1. In terms of the Denel MOI the Board shall consist of a minimum of three (3) Directors and a maximum of 16 (sixteen) Directors, with no less than 2 (two) Executive Directors, being the CEO and CFO. The Non-Executive Directors shall be appointed for a period of 3 (three) years at a time which appointment is reviewable annually, provided that no reason is appointed as a Director for longer than 3 (three) consecutive terms. Directors are normally appointed for a specific period and may be re-elected, if they make themselves available for this purpose.

4.9.2. At the 2014 AGM the Minister requested that the expiring Denel Directors terms of office be extended to the 2015 AGM to enable the Minister to undertake a review of the Board and a proper rotation scheduled implemented.

4.9.3. In a letter dated 25 May 2015 to the Acting Chairperson, the Minister confirmed the completion of the review and the retirement by rotation of the following Board members, with the Exception of Mr Motseki who has been re-elected, as per section 13.11.1 of the MOI. A copy of the rotation of directors is attached herewith as **Annexure "9"**.

The following Board members to retire by rotation are as follows:

- ***Ms. MJ Janse van Rensburg (Acting Chairperson),***
- ***Dr. Gert Cruywagen as Non-Executive Director of Denel SOC Limited,***
- ***Mr. G Badela as Non-Executive Director of Denel SOC Limited,***
- ***Ms. ZB Mathenjwa as Non-Executive Director of Denel SOC Limited,***
- ***Prof. S Nkomo as Non-Executive Director of Denel SOC Limited,***
- ***Mr. NJ Motseki as Non-Executive Director of Denel SOC Limited,***
- ***Mr. M Msimang as Non-Executive Director of Denel SOC Limited,***
- ***Mr. BF Ngwenya as Non-Executive Director of Denel SOC Limited,***
- ***Ms. MS Ntshikila as Non-Executive Director of Denel SOC Limited,***
- ***Mr. MV Ratshimbilani as Non-Executive Director of Denel SOC Limited,***

It was recommended that the Minister accept the resignation/retirement of the following Non-Executive Directors and note the Board members will have to by default resign from the Audit and Risk Committee, Personnel, Remuneration and Transformation Committee and the Social and Ethics Committee:

4.10. **Agenda Item No. 10: Appointment of External Auditors for 2014/15**

4.10.1.1. In terms of section 58 of the PFMA, SOC Annual Financial Statements must be audited by the Auditor-General or an external auditor duly registered and practising as such. Where an SOC elects to appoint an external auditor, the appointment must be done in consultation with the Auditor-General. It should be noted that an auditor may not be discharged by a SOC, prior to the expiry of the auditor's term of appointment. Only the Executive Authority of a SOC can attend to this function, subject to various conditions having been complied with.

4.10.1.2. The PFMA requirement should be read with the provisions of the Public Audit Act as well as the Companies Act (Part C) dealing with appointment, resignation, vacancies, rights and restricted function and rotation of auditors. Denel's auditors are SizweNtsalubaGobodo ("SNG") and will be serving a fourth year of the five year contract. It is important to note that the Companies Act (section 92) limits the

auditor's term to at least a period of five (5) years after which the Auditor must be rotated.

4.10.1.3. SNG develops a smaller audit firm, namely Kwinana Inc. However it should be noted that proper procedures were not followed in requesting Minister to approve the arrangement. The said arrangement was only mentioned in the Integrated Report, the department only got to know about it during the preparations of the Denel AGM. Minister was very concerned about the arrangement and raised her concerns during the AGM, Minister wanted to know; how the arrangement came about without Shareholder's approval? Denel was thereafter requested to provide details on the arrangement between the two firms to her by 29 July 2015. A copy of the appointment of external auditors is attached herewith as **Annexure "10"**.

It was recommended that the Minister:

a) Approve the appointment of SNG as Denel's External Auditors for the 2015/16 financial year; and

b) Notes the audit fee of R10.8m for the year ended 31 March 2015.

4.11. **Agenda Item No. 11: Dividend for the year ended 31 March 2015**

4.11.1. By law, dividends are declared to the Shareholder in circumstances where cash cannot be effectively utilised in the business and provided that appropriate gearing ratios are maintained by the company.

4.11.2. The Denel Board is requesting Minister to approve that no dividend be declared after taking into account the going concern, capital structure and dividend policy. The Department supports the resolution proposed by Denel that no dividend be paid.

It was recommended that the Minister approve the non-payment of a dividend by Denel subject to surplus being used to address strategic priorities in the Company's Corporate Plan.

4.12. **Agenda Item No. 12: Performance of Directors: Board Evaluation Report**

4.12.1. Good governance requires that Board members regularly undergo evaluation in order to assess Board effectiveness and individual contribution by directors. A systematic evaluation process is a necessary tool in (i) enhancing Board professionalism since it highlights the duties and responsibilities of the Board members; (ii) identifying necessary competencies and directors' profiles; and (iii) it is a useful incentive for individual members to devote sufficient time and effort to their duties as Board members.

4.12.2. An annual Board evaluation was conducted to assess the effectiveness of the Board and the individual contributions of the directors. The process was managed by Deloitte. The scope of the Board effectiveness done by Deloitte included the following:

4.12.2.1. An overall effectiveness assessment of the Denel Board itself, collectively;
4.12.2.2. An effectiveness assessment of each of the Board committees;
4.12.2.3. 360 degrees peer reviews of individual directors' performance and contributions; and
4.12.2.4. 360 degrees review of the Chairman's leadership and contribution.

4.12.3. The Report provides a positive outcome on the effectiveness and functioning of the Board. However, the Board did not receive much on-going development during the period under review, in addition meeting attendance has been good over the past year, except for one instances where the Director was absent for four consecutive meetings. There are areas of improvement in the report of Board Committees, progress on implementation of Strategic Plan and strengthening of the Board with engineering, Chartered Accounting skills. A copy of the Board Evaluation Report is attached herewith as **Annexure "11"**.

It was recommended that the Minister note the Denel Board Evaluation Report for the year ending 31 March 2015 and:

a) Remind the Directors that attendance to meetings signals the availability of each Director to dedicate sufficient time and expertise to the business of the Company.

4.12.4. **Attendance of Directors**

4.12.4.1. The Minister is requested to note the Directors' attendance of Board meetings as satisfactory and commends the Board for the commitment shown in exercising their duty of care and skill to the Company. A copy of the Directors attendance is attached as **Annexure "12"**.

It was recommended that the Minister note the attendance of Directors as submitted by the Directors.

4.12.5. **Disclosure of Interests**

4.12.5.1. In compliance with section 75 of the Companies Act, all the Directors of Denel have declared their interests. A copy of the declaration of interests is attached herewith as **Annexure "13"**. This disclosure obligation applies to all contracts and not only those that come before the Board. It is the Director's duty to determine whether they will have sufficient time to devote to Denel on accepting an appointment and in so doing discharge their duty of care towards Denel.

4.12.5.2. The disclosure of interests includes directorships, shareholding and partnerships. In terms of the Companies Act, Denel needs to include disclosures of related persons' interest in compliance with Section 75 of the Companies Act. All conflicts including related persons' interest to be dealt with in terms of the Companies Act on-going disclosure and recusal

4.12.5.3. According to the report provided by the Board, there are no material interests in contracts or conflict of interest that may negatively affect the Directors position on the Board and it was noted that none of the Non-Executive Directors hold more than 10 Directorships.

It was recommended that the Minister:

a) Notes the Disclosure of Interests of Directors on the Denel Board for the year ended 31 March 2015; and

b) Impress upon the Directors that it is the duty of each Director to continuously determine whether they will have sufficient time to devote to Denel and in so doing, discharge their duty of care to Denel.

4.13. **Agenda Item No. 13: Directors' Remuneration**

4.13.1. **Special Resolution: Approval of Remuneration of Non-Executive Directors**

4.13.1.1. The Directors' fees for Non-Executive Directors vary based on their appointment to the various committees of the Board. The Non-Executive Directors are paid an annual retainer as well as an additional retainer fee for committee membership. Denel is requesting the Minister to approve the resolution of a 6% increase for the Non-Executive Directors. The table below depicts the actual remuneration of Denel Non-Executive Directors for the 2014/15 financial period.

NON-EXECUTIVE DIRECTORS	2015 R'000	2014 R'000
Ms MJ Janse van Rensburg (Interim chairman)[1]	647	283
Mr NR Kunene (Chairman)[2]	294	773
Adv G Badela	176	200
Dr GC Cruywagen	342	310
Prof T Marwala[3]	49	76
Ms Z Mathenjwa	193	203
Mr NJ Motseki	111	136
Mr M Msimang	155	222
Mr BF Ngwenya	140	230
Prof SM Nkomo	293	354
Adv MS Ntshikila	103	226
Ms B Paledi[3]	35	167
Mr MV Ratshimbilani	109	209
Total	2 647	3 389

1 Interim chairman from 15 August 2014
2 Chairman resigned 15 August 2014
3 Resigned 15 August 2014

Table 7: Non-Executive Director's Remuneration

4.13.1.2. In terms of section 66 (8) and 66 (9) of the Companies Act, remuneration of directors may only be paid in accordance with a special resolution approved by the shareholders within the previous two (2) years.

4.13.1.3. In line with the directive from the Shareholder Representative, the Department can confirm that there are no deviations of the Board fees for the previous financial year. In light of the review of the Remuneration Standards, the Department proposes that the Minister declines the 7% salary increase for NED for the year ending 31 March 2016 and approves the increase of 5.3% for NED fees for the year ending 31 March 2016. A copy of Directors remuneration is attached herewith as **Annexure "14"**.

It was recommended that the Minister:

a) Decline the resolution of a proposed 7% fee increase for Non-Executive Directors; and

b) Approve an increase of 5.3% increase on the remuneration of Non-Executive Directors for the 2014/15 financial year.

5. FINANCIAL IMPLICATIONS

None for the Department.

6. CONSULTATION/PROJECT TEAM

Legal, Governance and Risk unit, Manufacturing Enterprises unit and Denel SOC (Pty) Ltd.

7. RECOMMENDATION

It is recommended that the Minister note, for the record, the resolutions taken at the Denel AGM held on 23 July 2015.

COMMISSION OF INQUIRY INTO STATE CAPTURE

Memorandum prepared by:

SIBONGILE MHLONGO
GOVERNANCE SUPPORT
DATE: 31 July 2015

XOLILE MAHLANGU
ASD: FINANCIAL ANALYST
DATE: 31/07/2015

REVIEWED AND SUPPORTED:

ORCILLA RUTHNAM
CD: GOVERNANCE
DATE: 01/08/2015

WEEKEND BANGANE
CD: DEFENCE
DATE: 04/08/2015

ADV MELANCHTON MAKOBE
ADDG: LGR
DATE: 12/08/2015

KGATHATSO TLHAKUDI
DDG: MANUFACTURING
DATE: 07/08/2015.

M.A. Mokholo
MS.MATSIETSI MOKHOLO
ACTING DIRECTOR-GENERAL
DATE: 12/08/2015

RECOMMENDED / NOT RECOMMENDED / COMMENTS

WHY ARE THE DDGs NOT DATING THE MEMO??
- Apologies ADG, they DDGs this will never happen again
12/08/15

MS. LYNNE BROWN, MP
MINISTER
DATE: 14/08/2015

APPROVED / NOT APPROVED / COMMENTS

MR. BULELANI GRATITUDE MAGWANISHE, MP
DEPUTY MINISTER
DATE: 31/08/2015

NOTED / COMMENTS

DENEL SOC LTD 2015 AGM
TABLE OF RESOLUTIONS AND AGENDA ITEMS
THURSDAY, 23 JULY 2015 AT 09:00
DENEL DYNAMICS AUDITORIUM, NELLMAPIUS DRIVE, IRENE

	AGENDA ITEM	DISCUSSION ITEM	RECOMMENDATION	NOTES
01.	Opening and Welcome	**It is recommended that Minister:** • Notes that the Chairperson of the Board is the Chairperson of the AGM; and • Notes that the quorum necessary for the AGM is the Minister as the sole member of the company (or a duly-appointed proxy) and that the AGM is thus duly constituted.	***Motion to be noted***	
02.	Safety Briefing	**It is recommended that Minister:** • Notes this agenda item	***Motion to be noted***	
03.	Attendance Register and Apologies	**It is recommended that Minister:** • Notes this agenda item	***Motion to be noted***	
04.	**Ordinary Resolution Number 1** Notice of the meeting	**It is recommended that Minister:** • Approves the agenda as proposed by Denel, and • Notes that Denel submitted the official AGM	***Motion to be adopted***	**Memo 1** as the Notice of the AGM The Notice of the AGM of Denel was given in accordance with the

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DENEL SOC LTD 2015 AGM
TABLE OF RESOLUTIONS AND AGENDA ITEMS
THURSDAY, 23 JULY 2015 AT 09:00
DENEL DYNAMICS AUDITORIUM, NELLMAPIUS DRIVE, IRENE

	AGENDA ITEM	DISCUSSION ITEM	RECOMMENDATION	NOTES
		notice and pack on 02 July 2015.		provisions of Denel's MOI and the Companies Act
05.	Address by the Representative of the Sole Shareholder of the Company.	**It is recommended that Minister:** • Uses this opportunity to reflect on the performance, strategic issues and challenges of the company for the year under review	***Motion to be adopted***	**Memo 2** as draft address by Minister highlighting the strategic, operational and financial highlights of the year under review as well as critical areas of focus for the year ahead.
06.	**Ordinary Resolution Number 2** Approval of the Minutes of the Annual General Meeting held on 15 August 2014.	**It is recommended that Minister:** • Adopts the minutes of the previous AGM held on 15 August 2014 as a true reflection of the proceedings at the said meeting	***Motion to be adopted***	**Memo 3** as Minutes of the 2014 AGM. **Memo 3A** as amendments by the Department (attached) have been incorporated into the minutes.
07.	Matters arising from the minutes of the Annual General Meeting held on 15 August 2015.	**It is recommended that Minister:** • Notes the feedback on and close-out of the matter arising from the minutes of the AGM held 15 August 2015.	***Motion to be noted***	**Memo 4** Progress report on matter arising from the minutes of the previous meeting

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DENEL SOC LTD 2015 AGM
TABLE OF RESOLUTIONS AND AGENDA ITEMS
THURSDAY, 23 JULY 2015 AT 09:00
DENEL DYNAMICS AUDITORIUM, NELLMAPIUS DRIVE, IRENE

	AGENDA ITEM	DISCUSSION ITEM	RECOMMENDATION	NOTES
				Refer to Memo 4 Appendix A, There was one matter arising from the minutes of the AGM held on 15 August 2015. Denel submitted a transformation strategy to the Minister on 20 November 2014. It should be noted that the Department will undertake an independent assessment of Denel's progress on transformation.
08. 8.1. 8.2. 8.3.	**Ordinary Resolution Number 3** Presentation of the Annual Financial Statements and Integrated Report for 2014/2015 Directors Report Report by External Auditors Report by Audit and Risk Committee	**It is recommended that Minister:** • Notes the Annual Financial Statements, • Notes the Directors' Report; • Notes the External Auditors report ; • Notes the Report by Audit and Risk Committee;	***Motion to be noted***	**Memo 5 (a)** as the **2015** Integrated Report.

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DENEL SOC LTD 2015 AGM
TABLE OF RESOLUTIONS AND AGENDA ITEMS
THURSDAY, 23 JULY 2015 AT 09:00
DENEL DYNAMICS AUDITORIUM, NELLMAPIUS DRIVE, IRENE

	AGENDA ITEM	DISCUSSION ITEM	RECOMMENDATION	NOTES
8.4	Subsidiary List	• Notes the list of subsidiaries as indicated in the Integrated Report; and		
8.5.	**Ordinary Resolution Number 4** Board Social and Ethics Committee Report	**It is recommended that Minister:** • Notes the matters in the Social and Ethics Committee Report.	***Motion to be noted***	**Memo 6** as Report of the Board Social and Ethics Committee
9.	**Ordinary Resolution Number 5** Retirement, Appointment and re-appointment of Non-Executive Directors	**It is recommended that Minister:** Notes that the following members are being rotated by means of separate resolutions. ➢ Ms MJ Janse van Rensburg (Acting Chairperson) ➢ Dr GC Cruywagen ➢ Adv G Badela ➢ Ms ZB Mathenjwa ➢ Mr NJ Motseki ➢ Mr M Msimang ➢ Mr BF Ngwenya ➢ Prof SM Nkomo ➢ Adv MS Ntshikila ➢ Mr MV Ratshimbilani • Accepts the resignation/retirement of the above Non-Executive Directors and note that Board members will have to by default resign from the Audit and Risk Committee, Personnel,Remuneration and Transformation Committee and the Social and Ethics	***Motion to be adopted***	**Memo 7** as the list of Board Members to be rotated the said members terms of office expired at the 2014 AGM, and were subsequently re-elected to hold office until the conclusion of the 2015 AGM. Minimum: 3 Maximum: 16 Current:12 Vacancies: 4 The new Denel Board was approved by Cabinet on the 13 May 2015 with the appointment being effective 24 July.

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DENEL SOC LTD 2015 AGM
TABLE OF RESOLUTIONS AND AGENDA ITEMS
THURSDAY, 23 JULY 2015 AT 09:00
DENEL DYNAMICS AUDITORIUM, NELLMAPIUS DRIVE, IRENE

	AGENDA ITEM	DISCUSSION ITEM	RECOMMENDATION	NOTES
		Committee.		Minister is requested to note that the Board still requires a CA (to chair the Audit and Risk Committee) and an engineer.
10.	**Ordinary Resolution Number 6** Appointment of External Auditors for 2014/15	**It is recommended that Minister:** • Approves the resolution to re-appoint SizweNtsalubaGobodo (SNG) as external auditors for the 2015/16 financial year, subject to annual review. • Notes that there is an arrangement whereby SNG develops a smaller audit firm, namely Kwinana Inc. • Proper procedure was not followed in requesting me to approve the arrangement. However the arrangement is mentioned in the Integrated Report. My question is; how did the arrangement came about without Shareholder approval? • Denel must provide details on the arrangement between the 2 firms to me by 29 July 2015. • Note that the audit fees for the year ended 31 March 2015 was R10.8m.	***Motion to be adopted***	**Memo 8** as the proposed resolution for re-appointment of Denel's External Auditors, appointed during the 2011/12 financial year for a maximum period of 5 years. 2015/16 will be the 4th year of the appointment.
11	**Ordinary Resolution Number 7**	**It is recommended that Minister:**		**Annexure 9** As the proposed resolution. The Board approved that no

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DENEL SOC LTD 2015 AGM
TABLE OF RESOLUTIONS AND AGENDA ITEMS
THURSDAY, 23 JULY 2015 AT 09:00
DENEL DYNAMICS AUDITORIUM, NELLMAPIUS DRIVE, IRENE

	AGENDA ITEM	DISCUSSION ITEM	RECOMMENDATION	NOTES
	Distribution to the Shareholder	• Notes that the Board approved that no dividends be paid for year ended 31 March 2015.	***Motion to be noted***	dividend be declared, taking into account the following issues ,namely, that the organization is not in a financial position, the current capital structure, and the dividend policy approved that no distribution be declared.
12.	Directors Remuneration	**It is recommended that Minister**		
12.1	Year ending 31 March 2015-Non-Executive Directors	• Notes the fees paid to Non-Executive Directors;	***Motion to be noted***	**Memo 10 annexure A** As Non-Executive Remuneration.
12.2	**Special Resolution 1** Non-Executive Directors Remuneration for the year ending 31 March 2016.	• Declines the Special Resolution for 7% increase for NED fees for the year ending 31 March 2016;	***Motion to be declined***	
		• The increase for the portfolio of SOCs will be set at 5.3% for the 2015/16 financial year; and		
		• Approves an increase of 5.3% per scale in remuneration of Non-Executive Directors for the year ending 31 March 2016.	***Motion to be adopted***	
		• Notes that NED's fees across the portfolio		

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	AGENDA ITEM	DISCUSSION ITEM	RECOMMENDATION	NOTES
		tend to be more conservative in comparison to the market and also in the current economic climate. • Directs the Company to engage the Department on phasing in the new Standards • Informs the Company that consultations on the Remuneration and Incentive Standards are at an advanced stage. Hence, Denel, through the new Board must make submissions on its revised Remuneration Policy within the next 3 months.		
12.3	Group Executive Committee Remuneration year ending 31 March 2015. **Ordinary Resolution No. 8** Proposed increase for Executive Directors and Prescribed Officers effective 1 April 2015	**It is recommended that Minister:** • Notes the remuneration of the Group EXCO for the year ended 31 March 2015; and • Declines the Special Resolution of 7% salary remuneration increases for the Prescribed Officers, including the Group CEO and the Group Financial Director as from 1 April 2015 (refer **Annexure B**). • Approves an increase of 5.3% per scale in remuneration of Executive for the year ending 31 March 2016.	***Motion to be noted*** ***Motion to be declined*** ***Motion to be adopted***	**Memo 11 annexure A** As Group Executive Committee remuneration **Memo 11 annexure (B)** as proposed Group Executive Committee increase **Memo 11 Ordinary Resolution Number (C)** NB: Request copy of the employment contract of the

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DENEL SOC LTD 2015 AGM
TABLE OF RESOLUTIONS AND AGENDA ITEMS
THURSDAY, 23 JULY 2015 AT 09:00
DENEL DYNAMICS AUDITORIUM, NELLMAPIUS DRIVE, IRENE

	AGENDA ITEM	DISCUSSION ITEM	RECOMMENDATION	NOTES
				CFO – appointed in 2008.
13.	**Special Resolution 2** Financial Assistance to subsidiaries I.T.O section 45 Companies act 2008	**It is recommended that Minister ;** • Approves the resolution allowing Denel to provide financial assistance to the following subsidiaries in order to meet the requirements of the Companies Act. -Denel Aerostructures -LMT -Densecure -LSSA	***Motion to be adopted***	**Memo 12 Annexure A** as the Special Resolution for Minister's Signature **Memo 12 B** Approved memo
14 14.1 14.2	**Ordinary Resolution Number 13** **Ordinary Resolution Number 14** Performance of Directors Board Evaluation Meeting Attendance	It is recommended that Minister: • Notes the Board Evaluation Report for 2015; • Notes the attendance of Board and Committee meetings for the year under review.	***Motion to the noted*** ***Motion to the noted***	**Memo 13** as the Board Evaluation Report Acknowledges the positive report on the effectiveness of the Board; Notes the actions that have already been taken in respect of the findings of the Report; **Memo 14** as the attendance to Board and Committee meetings for the year. Majority attendance is noted as very good.

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DENEL SOC LTD 2015 AGM
TABLE OF RESOLUTIONS AND AGENDA ITEMS
THURSDAY, 23 JULY 2015 AT 09:00
DENEL DYNAMICS AUDITORIUM, NELLMAPIUS DRIVE, IRENE

	AGENDA ITEM	DISCUSSION ITEM	RECOMMENDATION	NOTES
14.3	Declaration of Interests Disclosure of Non-Executive Director's Interest for the year ended 31 March 2015.	• Notes Prescribed Officers' disclosure of interests of the financial year ended 31 March 2015; • Notes Director's disclosure of interests for the financial year ended 31 March 2015 • Request the Company to amend the disclosure of interest template to include nature of business, contracts with Denel, signature of member, Chairperson and CFO.	***Motion to the noted*** ***Motion to the noted***	**Memo 15** as the list of interests of Directors It should be noted that none of the Non-Executive Directors hold more than 10 Directorships.
15 15.1 15.2	**Ordinary Resolution Number 16** **Resolutions** Ordinary Resolutions Special Resolutions	It is recommended that Minister: • Notes and signs the Ordinary Resolutions as reflected on decision taken; • Notes and signs the Special Resolutions as reflected on decision taken.	***Motion to be noted*** ***Motion to be noted***	**Memo 16** as the Ordinary Resolutions; **Memo 17** as the as the Special Resolution
16.	**Closure**			

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TWENTY THIRD ANNUAL GENERAL MEETING OF DENEL SOC LTD TO BE HELD ON THURSDAY, 23 JULY 2015 AT 09:00 IN THE DENEL DYNAMICS AUDITORIUM NELLMAPIUS DRIVE, IRENE

AGENDA

ITEM NO	SUBJECT	MEMO NO	ACTION
1.	OPENING AND QUORUM		
2.	SAFETY BRIEFING		
3.	ATTENDANCE REGISTER		
4.	NOTICE OF MEETING	1	Noting
5.	ADDRESS BY MINISTER	2	Noting
6.	APPROVAL OF THE MINUTES OF THE ANNUAL GENERAL MEETING HELD ON 15 AUGUST 2014	3	Approval
7.	PROGRESS REPORT ON MATTERS ARISING FROM PREVIOUS AGM MEETING	4	Noting
8.	PRESENTATION OF ANNUAL FINANCIAL STATEMENTS	5	
8.1	Directors Report		Noting
8.2	Report by External Auditors		Noting
8.3	Report by Audit and Risk Committee		Noting
8.4	Subsidiary list		Noting
8.5	Board Social and Ethics Report	6	Noting
9.	ROTATION OF THE NON-EXECUTIVE DIRECTORS	7	Approval
10.	APPOINTMENT OF EXTERNAL AUDITORS FOR 2015/16	8	Approval

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ITEM NO	SUBJECT	MEMO NO	ACTION
11.	DISTRIBUTION TO THE SHAREHOLDER	9	Noting
12.	DIRECTORS REMUNERATION:	10	
12.1	Year ending 31 March 2015 – Non-executive		Noting
12.2	Year ending 31 March 2016		Approval
12.3	Group Executive Committee Remuneration year ending 31 March 2015 and proposed increase effective 1 April 2015	11	Approval
13.	FINANCIAL ASSISTANCE TO SUBSIDARIES I.T.O. SECTION 45 COMPANY'S ACT 2008	12	Approval
14.	PERFORMANCE OF DIRECTORS		
14.1	Board Evaluation	13	Noting
14.2	Meeting Attendance	14	Noting
14.3	Declaration of Interest	15	Noting
15.	RESOLUTIONS		
15.1	Ordinary resolutions	16	Approval
15.2	Special resolutions	17	Approval
16.	CLOSURE		

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DENEL SOC LIMITED

(Registration No: 1992/001337/30)

NOTICE TO MEMBERS

Notice is hereby given that the twenty first Annual General Meeting of members of Denel SOC Ltd will be held in the Denel Dynamics Auditorium, Nellmapius Drive, Irene, on Thursday, 23 July 2015 at 09:00.

NOW THEREFORE IT IS:

1. ORDINARY BUSINESS

To consider and, if deemed fit, to pass, with or without modification, the following ordinary resolutions:

1.1 Ordinary Resolution 1

To receive and consider the annual financial statements for the years ending 2014/15, including the Director's report and the report of the Auditors therein.

1.2 Ordinary Resolution 2

In accordance with the Memorandum of Incorporation of the Company section 13.11.1, the following Directors term of office expires at the AGM and will retire by rotation with the exception of Mr NJ Motseki, who being eligible offer himself for re-election:

Ms MJ Janse van Rensburg (Acting Chairperson)
Dr GC Cruywagen
Adv G Badela
Ms ZB Mathenjwa
Prof SM Nkomo
Mr M Msimang
Mr BF Ngwenya
Adv MS Ntshikila
Mr MV Ratshimbilani

1.3 Ordinary Resolution 3

To appoint SizweNtsalubaGobodo, as external auditors of the company, to hold office until the conclusion of the next Annual General Meeting i.t.o. section 17.5 of the Memorandum of Incorporation.

1.4 Ordinary Resolution 4

To note the proposed remuneration for the Executive Directors and Prescribed Officers.

1.5 Ordinary Resolution 5

To note that no distribution has been declared for the year ended 31 March 2015.

2. SPECIAL BUSINESS

To consider and, if deemed fit, to pass, with or without modification, the following special resolutions:

2.1 Special Resolution 1

To determine the remuneration of the Non- Executive Directors i.t.o. section 12.1.1.4 of the Memorandum of Incorporation.

2.2 Special Resolution 2

To approve that the company may provide financial assistance to its subsidiaries i.t.o. Section 45 of the Company's Act 2008, and section 14.1.1.3 of the Memorandum of Incorporation.

3. To transact such other business as may be transacted at an Annual General Meeting.

4. VOTING

A member entitled to attend and vote at the meeting is entitled to appoint a proxy or proxies to attend, speak and vote in his/her stead. A proxy need not be a member of the Company. Proxy forms should be forwarded to reach the Business Office of the Company at least 24 hours, before the time appointed for the holding of the Annual General Meeting.

5. PROXIES

A form of proxy which sets out the relevant instructions for its completion is attached for use by Shareholders of the Company who wish to appoint a proxy. The instrument in appointing a proxy and the authority, if any, under which it is signed, must be received by the Company at the fax number given below by not later than 09:00 on Wednesday, 22 July 2015.

By order of the Board

DENEL SOC LTD

.....

EM Africa (Ms)
GROUP COMPANY SECRETARY

26 June 2015

Business address
Nellmapius Drive
Irene
(P O Box 8322, Centurion, 0046)
(Fax No 012 671 2860)

Registered office
Nellmapius Drive
Irene
0046

DENEL 2015 AGM
Minister Lynne Brown: Shareholder address
23 July 2015
Denel Auditorium, Irene

Introduction

I first wish to note the role and contributions of all employees of Denel, management and Board of Directors towards another successful financial year. I am cognisant that my address to the 2015 AGM also marks the end of term of the current Board. It has indeed been a pleasure working with you. Your professionalism, the spirit in which you have served the Company, has not only ensured a smooth transition, but more especially set the Company on a long term path of sustainable performance. Hence, my remarks, on the overall performance of the Company, must also be shared with the incoming Board who must give attention to the matters raised herein.

Financial Overview

I note the following positive development in relation to finances:

- order cover in excess of R35 billion;
- 28% improvement in revenue (from R4.6 billion to R5.8 billion);

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- the fifth consecutive year in a row that Denel is posting a profit, which is now standing at R270 million;
- the continued improvement in total equity position(it has tripled to R1.9 billion in 3 years); and
- the improvement in interest cover is noted.

I wish to highlight the following areas of concern on the financials:

- commercial paper redemption will be due in the current financial year and the Denel Board and the Department need to ensure that the SOC is in a position to fulfil this obligation;
- current liabilities are at the highest in the last ten years – the correct balance with the assets side of the balance sheet needs to be maintained at all times;
- the level of prepayments and their utilisation needs close attention. In this regard a benchmarking study in this current financial year will be conducted to assess the SOC practice in relation to industry and best practice;

Shareholders' Compact Performance

I note the following areas of performance:

- the SOC has achieved 88% of the Shareholders' Compact targets for the year under review;

KT-071

- pleasing strides in increasing black people and women representation at all levels of the organisation – 53% HDI representation is a movement in the right direction;
- The SOC maintenance of strategic and sovereign capabilities and alignment of capabilities with the 2014 Defence Review including cultivating a good working relationship with the SANDF and DOD; and
- Excellent execution of strategic acquisition projects.

Denel must increase the level of effort in the following areas:

- **Research and Development:** Denel is a high technology enterprise and it is accepted truth with these enterprises that investment in research and development is a key driver for business sustainability. Denel must seek to invest more in next-generation technologies and products to ensure continued competitiveness.

  Denel has to find innovative ways of increasing investment in research and development. Collaboration in research and development is a growing trend, especially for defence and aerospace industry. Denel has taken steps in this direction in some of its product development initiatives: A-Darter and Airbus A-400M. Denel must seek to do more in this area.

  The Department has made me aware of Denel Executive discomfort with the research and development KPA and KPI target of 5% of revenues. I urge the two parties to find each other to develop appropriate performance metrics.

  This should be done without negatively affecting the level of effort in technology development.

KT-072

- **Transformation**: We must always remind ourselves that SOCs are operating within a complex socio-economic environment given our past. Your excellence will not only be judged in terms of how big your revenue and profits are but on whether our people are benefiting from these revenues.

  I therefore expect Denel to pay special attention to enterprise and supplier development.

  The defence industry is one of the least transformed in the country. What concerns me is that some players are so arrogant about their lack of appetite to embark on meaningful transformation. For instance, during my visit of individual South African exhibition stands at 2016 Abu Dhabi International Air Show, a South African Executive from a private sector company had the audacity to criticise the country's BBBEE policy. Denel has the necessary weight and muscles to correct such unhelpful attitudes by ensuring that you transact mainly with entities and individuals who propagate transformation and inclusivity.

- **Skills development**: The defence industry, like all the productive sectors of the economy, has become increasingly vocal about how fewer students are focused on STEM (science, technology, engineering and mathematics), and how that may eventually harm sustainable continuity. Please continue with your efforts in this area and I especially note the good work being done in Gauteng and North-West in improving matric pass rates. I would like to hear from Denel on how we can expand this effort to the other provinces.

  I also wish to note the good work being done with post matriculants and graduates through The Denel Technical Academy and the Denel Dynamics Engineering academies. These are examples of what can be achieved when our hearts are in it.

KT-073

The Department has assisted Denel to receive R58 million from the National Skills Fund to train 197 artisan trainees. The SOC needs to be more ambitious with the number of young people taken on for artisan and engineering programmes – and not be guided solely by Denel's own requirements.

Reporting Structure

Denel is a multifaceted organisation with 6 divisions, 3 subsidiaries and 4 associate companies. And I am made to understand that the number is likely to increase with the acquisitions planned. The Board needs to ensure that the SOC is adequately structured to oversee these varied governance arrangements. I am concerned that in the aggregation of numbers, there are nuances of the business that are lost, denying the Shareholder the opportunity to fully appreciate this complex business.

I have directed the Department to evaluate the reporting structure to ensure that it adequately surfaces areas that require attention. Denel's collaboration will be appreciated.

Message to the Outgoing Board of Directors

The SOC and the Department developed a Turnaround Plan in 2012, which was approved by Cabinet. This was a condition of a R1.8 billion guarantee to restructure the SOC debt. The quality of the plan and its implementation was a critical role played by the Board. I commend you on a job well done.

KT-074

You are handing over the company that is truly on a path to sustainability. I thank you for the handover report. The Department will ensure it is incorporated into the induction of the new Board of Directors.

I wish you well in your future endeavours.

Conclusion

To the Executive Management, continue to do your best to ensure that the SOC fulfils its primary mandate. You are an important constant in the transition between the incoming and outgoing Board. We are counting on you to ensure this process is managed properly.

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MINUTES OF THE TWENTY SECOND ANNUAL GENERAL MEETING HELD ON 15 AUGUST 2014 AT 09:00 IN THE DENEL DYNAMICS AUDITORIUM, NELMAPIUS DRIVE, IRENE

NO	ITEM	DISCUSSION/DELIBERATION	ACTION/RESOLUTION	TIME FRAME	RESPONSIBILITY
1.	WELCOME	The Chairperson welcomed all to the Twenty Second Annual General Meeting (AGM) of Denel SOC Ltd, and extended a special word of welcome to the honourable Minister Lynne Brown of Public Enterprises and Deputy Minister BG Magwanishe. The attendance register was circulated for signature.			
2.	APOLOGIES	Adv M Ntshikila	Noted.		
3.	PRESENT	The Honourable Minister Lynne Brown, Minister of Public Enterprises Deputy Minister BG Magwanishe Mr NR Kunene - Chairperson Mr R Saloojee - Group Chief Executive Officer Adv G Badela Dr GC Cruywagen Ms MJ Janse van Rensburg Prof T Marwala Mr NJ Motseki Mr F Mhlontlo Ms ZB Mathenjwa Mr M Msimang Mr BF Ngwenya Prof SM Nkomo			

NO	ITEM	DISCUSSION/DELIBERATION	ACTION/RESOLUTION	TIME FRAME	RESPONSIBILITY
		Ms B Paledi Mr MV Ratshimbilani Mr T Matona - Director General Mr B Roberts - Special Advisor Ms M Mokholo - DDG: Legal and Governance Ms V Tlale - CD: Financial Analyst Ms S Pather - Dir: Legal and Governance Mr K Tlhakudi Mr E Jele Mr T Matheza Mr L McPatie Ms N Davies Mr I Dockrat Mr A Carim Mr T Kleynhans Mr M Kgobe Ms F Legoabe Mr D Mlambo Mr T Monaheng Mr P Petje Ms V Qinga Mr J Wessels Mr Z Ntshepe Mr T Zwelibanzi Ms V Ravjee Ms N Gobodo - SizweNtsalubaGobodo Mr D Simpson - SizweNtsalubaGobodo Ms P Nhantsi - SizweNtsalubaGobodo Ms I Gray - Deloitte &Touche Mr P Bhana - Deloitte &Touche Ms G Sibiya - Xabiso Ms EM Africa - Group Company Secretary			

NO	ITEM	DISCUSSION/DELIBERATION	ACTION/RESOLUTION	TIME FRAME	RESPONSIBILITY
4.	**CONSTITUTION OF MEETING**	The required quorum being present the Chairperson declared the meeting duly constituted in terms of the MoI of the Company.	**Noted.**		
5.	**NOTICE OF MEETING Memorandum 1**	The Chairperson stated that the notice convening the meeting should be read by the Secretary; however, as it has already been circulated to the shareholder he requested the consent of the meeting to take the notice as read.	**AGREED.**		
6.	**SHAREHOLDER COMMUNIQUÉ**	Shareholder Address by the Minister of Public Enterprises, Ms Lynne Brown, on the occasion of the Denel Annual General Meeting held in Irene on 15 August 2014, noted as follows: **Introduction** Deputy Minister, Director-General, Chairperson, CEO and members of the Board, ladies and gentlemen, let me begin by sharing a little secret. A few years ago I numbered among my prize possessions a cap and a lapel badge which proudly promoted the Rooivalk. I had accompanied a delegation to a show in which the Rooivalk was being showcased and had been given these as part of Team Rooivalk. For quite a while after that I continued to wear them. I must say that I doubt very much if sales actually increased as a result of my efforts. Nevertheless, I hope it gives credence to my claim that I have been a supporter of Denel and its mission for longer than just the past few months. Looking at the headlines in your Integrated Report, I know that you must be tempted at this moment to pat yourselves on the back with four consecutive years of			

NO	ITEM	DISCUSSION/DELIBERATION	ACTION/RESOLUTION	TIME FRAME	RESPONSIBILITY
		net profit behind you, revenue heading rapidly towards R5 billion and an impressive-looking order book. And so you should. However, while you celebrate your success, I urge you not to lose sight of the fact that only part of the job is done. Denel and other State-Owned Companies are not like conventional companies. Besides delivering well on your core mandate, you also have an important role to play in a drama which goes way beyond your basic business. That drama is about our fight against poverty, unemployment and inequality. The Fifth Democratic Administration, which I represent here today, has declared that if we are to make real strides towards winning that battle, we need: • Sustainable and inclusive economic growth of better than 5 percent, • Much higher levels of employment creation, and • More rapid reduction of inequality, including de-racialization of the economy. The Medium-Term Strategic Framework – our detailed plan – sets out to achieve this through a range of mutually reinforcing initiatives, with Government departments, State-Owned Companies and Public Entities working together and in an aligned manner. Denel must be quite central to this. Let me suggest a few ways in which you can contribute to these urgent developmental goals as I reflect on your performance.			

NO	ITEM	DISCUSSION/DELIBERATION	ACTION/RESOLUTION	TIME FRAME	RESPONSIBILITY
		Performance First, through the growth of your output in both volumes and value, this is why I am thrilled to see an order pipeline of over R30 billion. Second, through growing exports which earn the country valuable foreign currency and contribute towards the achievement of a positive balance of payments. So, naturally, I am delighted to see exports growing in 2013/14 to 50% of revenues. Third, we must make global competitiveness the new normal. It is good to observe that the Denel team has achieved success in a global defence market dominated by fifteen countries which tend to favour their domestic manufacturers. Fourth, best price, best quality, must be delivered on time. In order for Denel to maintain or improve on current performance, it will need to ensure that the concluded orders are delivered as per customer requirements. A few years ago, the Japanese joked that they had invented the Just In Time system and we had invented the Just Too Late system. Humour aside, Denel has in the past not covered itself in glory in this area. This operational risk will be significant as you enter into serial production of a number of major orders. I urge you to prepare adequately. Fifth, in the light of the overwhelming competing demands on the fiscus for basic social services, reduce current government guaranteed debt.			

NO	ITEM	DISCUSSION/DELIBERATION	ACTION/RESOLUTION	TIME FRAME	RESPONSIBILITY
		Finally, given its technological capabilities, Denel has to up-scale its role as an instrument of industrial strategy. In this light, I am pleased to inform you that the Departments of Public Enterprises and Defence have developed a cooperation agreement, which articulates the strategic importance of Denel to both departments. I am expecting Denel and the Department to ensure that we leverage this agreement to promote advanced manufacturing and industrialization. **Acquisitions** I would like to express a few thoughts on the long-term growth strategy and its relationship to the sustained profitability of the business. In realizing the strategy and developing identified capability gaps, I expect the Board to be judicious and diligent in authorizing acquisitions. Organic growth should be the preferred option in order to manage the exposure of the company. The acquisitions must take into account the recommendations of the Defence Review Report. I note the establishment of Denel Spaceteq. The business offers a platform for development and maintenance of satellite applications technologies, which we have identified as having great potential for advancing our development agenda. In 2012/13 Denel concluded the acquisition of LMT. The consolidation of the business with Denel Landward Systems should be explored.			

NO	ITEM	DISCUSSION/DELIBERATION	ACTION/RESOLUTION	TIME FRAME	RESPONSIBILITY
		A National Maintenance Repair and Overhaul Entity Let me turn to a matter close to my heart: cooperation between State-Owned Companies. At the last AGM, my predecessor raised the matter of consolidation of the Aviation Maintenance, Repairs, and Overhaul businesses within this portfolio: Denel Aviation, SAA Technical and SA Express Technical. The Department has developed the DPE Aerospace Strategy to enable alignment between all parties. The terms of reference and the memorandum of agreement for the three parties have been finalized and are awaiting approval. **Transformation** Now, for the vexed issue of transformation, or the lack thereof. The current significant lack of representivity of black people and women is baffling. Since we last met, I have been asking myself why this situation still prevails in the 21st year of democracy. It has been difficult to avoid the conclusion that, even bearing in mind that you would have had to begin by growing your own timber from scratch, you should have had a significant cohort of qualified and suitably experienced black and women employees at all levels by now. If I add to that the fact that the business is at risk in the face of impending retirements and natural attrition due to its skewed demographic profile, I feel that I need to say bluntly that it appears as if somebody has			

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NO	ITEM	DISCUSSION/DELIBERATION	ACTION/RESOLUTION	TIME FRAME	RESPONSIBILITY
		been asleep at the wheel. I would have expected there to be some extraordinary initiative under way to address this very high risk to the sustainability of the business. I am also concerned that Denel is unable to produce the number of trainees contracted with the Department. Having said this, the Department has briefed me on the strides being made to transform Denel Training Academy (DTA) into a modern training facility, by leveraging synthetic training technologies. In the light of the above, within three months, I want the Board to present a plan to me which will mitigate the immediate risks presented by the impending retirements and which accelerates the achievement of representivity within this term of Government. I want to propose that the Board considers withholding bonuses from all of those who fail to meet their targets in such a plan. Let me also express my concern about enterprise development. Important as they are, it should not just be about further training opportunities for black people, youth, women and people-living-with-disabilities. These entrepreneurs also want to be given an opportunity to do business with Denel. Unfortunately for them, the latest quarterly performance report demonstrates the difficulty the company is still experiencing in reaching its target for Black-owned, and women-owned companies.	Present risks mitigated i.t.o. the impending retirements and measures to accelerate the achievement of representivity within this term of Government.	Within 3 months	Board

NO	ITEM	DISCUSSION/DELIBERATION	ACTION/RESOLUTION	TIME FRAME	RESPONSIBILITY
		Conclusion In closing, I would like to avail my assistance in any strategic marketing activities. Let me know well in advance. I do not need any special kit; I still have my Rooivalk cap and lapel pin. Chairperson, Board Members and CEO, can you please extend my heartfelt appreciation to every single employee for their contributions to the success of the company over the reporting period. Thank you for your attention. The Chairperson then thanked the Minister and informed her that her concerns as detailed above were noted.			
7.	**APPROVAL OF THE MINUTES OF THE TWENTIETH ANNUAL GENERAL MEETING HELD ON 22 JULY 2013** **Memorandum 2**	The minutes of the Twentieth Annual General Meeting held on 22 July 2013 were tabled for consideration.	It was **resolved** that the minutes of the AGM held on 22 July 2013 be taken as read and that the Chairperson be authorised to sign these as a true reflection of the proceedings.		
8.	**MATTERS ARISING FROM THE PREVIOUS MEETING** **Memorandum 3**	A progress report on matters arising from the previous meetings was tabled for noting.	**Noted.**		
9.	**BOARD SOCIAL AND ETHICS COMMITTEE** **Memorandum 4**	The Chairperson stated that in terms of Section 43 (c) of the Companies Regulations unless the meeting unanimously agrees to the contrary, the report of the Committee should be read out at this meeting.			

NO	ITEM	DISCUSSION/DELIBERATION	ACTION/RESOLUTION	TIME FRAME	RESPONSIBILITY
		At the Chairperson's request the Minister consented to take the Social and Ethics Committees report as read and noted.	**Noted.**		
10.	**ADOPTION OF ANNUAL FINANCIAL STATEMENTS; DIRECTORS AND AUDITORS REPORT FOR 2013/14 Memorandum 5**	The Chairperson tabled the Annual Financial Statements for the financial year ended 31 March 2014 and noted that they had been circulated to the shareholder. He stated that unless there are particular questions on the Financial Statements, he would put a motion for the acceptance and adoption of the Company's Financial Statements for the year ended 31 March 2014. The Minister noted the following with regards to the Financial Statements: • The expression of an unqualified audit opinion by the auditors; • The improvement in Denel's financial performance, which has had a positive impact on the equity position. • A sustained growth in revenue of above 10% in the last three years. The continuous increase in export revenue, which is now 50% of all revenue collected during the year under review. • That this is the fourth consecutive year that Denel is reporting a profit after a decade of accumulating losses. It was stated in the previous AGM address that Denel's profitability needs to be improved to reflect more of operational profit than accounting gains. Denel must continue working on improving its operational profitability so as to enable it to have surplus funds to reduce its guaranteed debt.	It was **resolved** that the annual financial statements including the directors' and auditors' reports for the financial year ended 31 March 2014 be and are hereby **noted.**		

NO	ITEM	DISCUSSION/DELIBERATION	ACTION/RESOLUTION	TIME FRAME	RESPONSIBILITY
		• The improvements on the cash and equity position of the company. Denel must note that: The fiscal budget is under strain with the current deficit in the trillion rand mark. Therefore the state will be limited in terms of any financial support or otherwise that can be provided to the SOC. It is therefore critical that Denel works towards reducing its reliance on state support and must focus on sustainability on a standalone basis. The Minister then noted the Annual Financial Statements.			
11.	**ROTATION/ RETIREMENT/ APPOINTMENT AND RE-ELECTION OF NON-EXECUTIVE DIRECTORS** **Memorandum 6**	In terms of Clause 13.11.1 of the Memorandum of Incorporation, the re-appointment of the eligible Non-executive Directors retiring in accordance with the provisions of the Company's Memorandum of Incorporation, was tabled for approval and confirmation by way of separate resolutions. The following ordinary resolution was tabled: That the re-appointment of the Non-Executive Directors who retire in accordance with the provision of the Company's Memorandum of Incorporation, being eligible for re-appointment in terms of Clause 13.11.1 of the Memorandum of Incorporation, be approved by way of a separate resolution in respect of each appointment, subject to a review within the next five months to afford the Minister (Representative of the Sole Shareholder) an opportunity to consider Board composition in light of skills, experience, tenure and demographic profiling.	**Noted.** **Approved** per separate resolution, subject to a review within the next five months to afford the Minister (Representative of the Sole Shareholder) an opportunity to consider Board composition in light of skills, experience, tenure, and demographic profiling.		

NO	ITEM	DISCUSSION/DELIBERATION	ACTION/RESOLUTION	TIME FRAME	RESPONSIBILITY
		The following Non-Executive Directors were reappointed as detailed above, and on such terms and conditions on which Directors shall rotate and/or retire from Office as determined by the Representative of the Sole Shareholder of the Company: 1. That Dr GC Cruywagen be re-appointed as a Director of the Company. 2. That Adv G Badela be re-appointed as a Director of the Company. 3. That Ms MJ Janse van Rensburg be re-appointed as a Director of the Company. 4. That Ms ZB Mathenjwa be re-appointed as a Director of the Company. 5. That Mr NJ Motseki be re-appointed as a Director of the Company. 6. That Mr M Msimang be re-appointed as a Director of the Company. 7. That Mr BF Ngwenya be re-appointed as a Director of the Company. 8. That Prof SM Nkomo be re-appointed as a Director of the Company. 9. That Adv MS Ntshikila be re-appointed as a Director of the Company. 10. That Mr MV Ratshimbilani be re-appointed as a Director of the Company.			
11.1	**Resignation of Directors in terms of clause 13.11.3.2.1 of the Company's Memorandum of Incorporation**	The resignation of the following Directors whose term of office expired at this AGM and did not offer themselves for re-election was accepted and noted: 1. Prof T Marwala; and 2. Ms B Paledi.	**Noted.**		

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NO	ITEM	DISCUSSION/DELIBERATION	ACTION/RESOLUTION	TIME FRAME	RESPONSIBILITY
12.	**RETIREMENT OF THE CHAIRPERSON OF THE BOARD AND AS NON-EXECUTIVE DIRECTOR AND APPOINTMENT OF A NEW/OR ACTING CHAIRPERSON** **Memorandum 7**	The Chairperson requested the Minister to confirm retirement of the Chairperson of the Board whose term of office expires in accordance with the provision of the Company's Memorandum of Incorporation. He then tabled a motion for the confirmation and retirement of the current Chairperson of the Board Mr Zoli Kunene and the appointment of a new Chairperson of the Board or an acting Chairperson from any of the other Non-executive Directors. The Minister in confirming the retirement of the current Chairperson of the Board, approved the appointment of Ms MJ Janse van Rensburg as acting Chairperson of the Board.	**Adopted.** **Resolved** to **approve** Ms MJ Janse van Rensburg as acting Chairperson of the Board, until the next AGM.		
13.	**CONFIRMATION OF AUDITORS TO PERFORM THE AUDIT FOR THE YEAR ENDING 31 MARCH 2014** **Memorandum 8**	The proposal that the re-appointment of SizweNtsalubaGobodo as external auditors of the Company until next AGM of the Company be confirmed was tabled for consideration.	**Adopted.**		
13.1	**Report of the Audit Committee on the fixing and approval of the Auditors' fees for the year ended 31 March 2014**	The report of the Audit and Risk Committee of the Company on the fixing and approval of the auditors' remuneration at R10 million for the year ended 31 March 2014, as detailed in the Annual Financial Statements, was tabled for noting.	**Noted.**		
14.	**DIVIDEND** **Memorandum 9**	It was noted that in light of the company's financial position, no dividends would be declared.	**Noted.**		

NO	ITEM	DISCUSSION/DELIBERATION	ACTION/RESOLUTION	TIME FRAME	RESPONSIBILITY
15.	**SHAREHOLDER'S COMPACT THE YEAR ENDING 31 MARCH 2016, INCLUDING MATERIALITY AND SIGNIFICANCE FRAMEWORK 2014/15 - 2017** **Memorandum 10**	The 2016 Shareholders' Compact including the Significance and Materiality Framework for the following three financial years, namely 2014/15, 2015/16 and 2016/17 that had been discussed and negotiated with DPE officials and is included in the AGM pack was tabled for approval.	**Approved.**		
16.	**APPOINTMENT OF AUDIT AND RISK COMMITTEE FOR 2014/15** **Memorandum 11**	A proposal that the following Non-executive Directors of the Company be appointed, by way of separate resolution, as the members of the Audit and Risk Committee until the conclusion of the 2015 AGM of the Company, on such terms and conditions to be determined by the Company, was tabled for consideration and approval.			
		• That Ms MJ Janse van Rensburg step down as the Chairperson of the Audit and Risk Committee of the Company and be appointed as a member of the Audit and Risk Committee of the Company.	**Approved.**		
		• That Dr GC Cruywagen be appointed as the Chairperson and a member of the Audit and Risk Committee of the Company.	**Approved.**		
		• That Ms ZB Mathenjwa be appointed as a member of the Audit and Risk Committee of the Company.	**Approved.**		
		The resignation of Mr B Paledi who resigned as Non-Executive Director of the Board and thus by default resigns as a member of the Audit and Risk Committee was noted.	**Noted.**		

NO	ITEM	DISCUSSION/DELIBERATION	ACTION/RESOLUTION	TIME FRAME	RESPONSIBILITY
17.	**CONFIRMATION OF THE MEMBERS OF THE SOCIAL AND ETHICS COMMITTEE TO SERVE UNTIL THE 2015 ANNUAL GENERAL MEETING** **Memorandum 12**	A proposal was tabled that the following Non-executive Directors of the Company be confirmed by way of separate resolutions, as the members of the Social and Ethics Committee until the conclusion of the 2015 AGM of the Company, on such terms and conditions to be determined by the Company: • That Prof SM Nkomo be confirmed as a member and the Chairperson of the Social and Ethics Committee of the Company. • That Dr GC Cruywagen be confirmed as a member of the Social and Ethics Committee of the Company. • That Mr M Msimang be confirmed as a member of the Social and Ethics Committee of the Company.	**Confirmed.** **Confirmed.** **Confirmed.**		
18.	**PERFORMANCE OF DIRECTORS** **Memorandum 13**	The Board Evaluation Report for the year ended 31 March 2014, was tabled for noting.	**Noted.**		
19. 19.1	**NON-EXECUTIVE DIRECTORS' REMUNERATION** **Confirmation of Non-executive Directors' fees for the year ended 31 March 2014** **Memorandum 14**	A proposal was tabled that the Non-executive Directors' emolument in the amount of R3.3 million for the year ended 31 March 2014 be confirmed. Prior to discussing the proposal for the increases for the Non-Executive and Executive Directors including the Prescribed Officers, the Executive Directors and Prescribed Officers were excused.	**Confirmed.**		

NO	ITEM	DISCUSSION/DELIBERATION	ACTION/RESOLUTION	TIME FRAME	RESPONSIBILITY
19.2	**Proposed increase for Non-Executive Directors for the year ending 31 March 2015**	A proposal to increase the Non-Executive Directors fees by 6% was tabled for consideration. In considering the proposal the Minister approved a 5% increase, based on the following: 1. The Department has developed the Remuneration and Incentive Standards for State Owned Companies (SOC) for Executive Directors, Prescribed Officers and Non-Executive Directors ("the Remuneration Standards"). 2. The Standards have been approved by my predecessor and SOCs within the portfolio have begun testing its application. Thus far the feedback to the Department has been useful to ensure continuous improvement and strengthening of the Standards. 3. While Cabinet was generally supportive of the Standards, the matter was deferred to afford the new Administration an opportunity to engage on its contents. It is critical that Cabinet is fully informed about the impact the Standards will have on existing remuneration levels. In other words, the Department will need to show exactly how the guiding principles of the Standards translate into the monetary value of remuneration and incentives. 4. Denel is therefore required to continue engaging the Department on aligning its Remuneration Policy to the new Remuneration Standards. 5. With regard to the remuneration and incentives of Executive Directors and Prescribed Officers:	**Approved** 5% increase, for Non-Executive and Executive Directors, including the Prescribed Officers.		

NO	ITEM	DISCUSSION/DELIBERATION	ACTION/RESOLUTION	TIME FRAME	RESPONSIBILITY
		In terms of the request for increases for the 2014/15 financial year, I approve a 5% increase for Executive Directors and Prescribed Officers with effect from 1 April 2014. 6. I prefer to take a conservative approach to percentage increases granted this year, based on the fact that there still needs to be engagement with Cabinet on the new Standards and SOCs still need to provide me with the Company's new Remuneration Policy based on these Standards. 7. Accordingly, issues raised in the pre-meeting such as long-term incentives cannot be implemented prior to my approval of the whole of the Company's new Remuneration Policy. 8. I am encouraged by the Company's diligence in adapting to the Shareholder model for remuneration and note the declaration that there are no hidden benefits in your current Remuneration Policy. 9. However, there is much work still to be done which requires further consultation between me and the Board. In submitting the revised Remuneration Policy, the Board must also provide me with copies of the Performance Agreements of the Executive Directors and Prescribed Officers highlighting the alignment to the Strategic Intent Statement and the Shareholder's Compact. I thank you			

NO	ITEM	DISCUSSION/DELIBERATION	ACTION/RESOLUTION	TIME FRAME	RESPONSIBILITY
		Conclusion I trust that the issues raised above sufficiently signal my faith and confidence in the Board and Management and provides the motivation and stability required to meet and overcome challenges towards achieving the long-term growth strategy for the company. The Minister then thanked everyone.			
20.	**CLOSURE**	There being no further business to discuss the Chairperson thanked everyone and declared the meeting closed.			
21.	**DATE OF NEXT MEETING**	TBA			
		APPROVED	**DATE**		


COMMISSION OF INQUIRY
INTO STATE CAPTURE

public enterprises
Department:
Public Enterprises
REPUBLIC OF SOUTH AFRICA

Suite 301, Infotech Building1090 Acadia Street Hatfield, 0083 Private Bag X15 Hatfield 0028
Tel: (012) 431 1000 Fax: 086 501 2624 / 086 501 0629

Address by Minister Lynne Brown, Shareholder Representative
Denel Special General Meeting and Board Induction

24 July 2015

Deputy Minister Magwanishe;
Chairperson the Board,
Members of the Board of Directors,
Acting Director General,
Chief Executive Officer, and
Officials and Executives;

Good morning,

It gives me great pleasure as the Representative of the sole Shareholder to address you as the new Board of Denel SOC Ltd at this Special Annual General Meeting.

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I wish to thank each one of you for accepting the appointment to serve on the Denel Board. I also express my appreciation that you have made yourself available at such short notice for this special meeting and induction.

THE PURPOSE OF INDUCTION

Directors, individually and collectively as a Board, are accountable for the affairs, performance and well-being of the State Owned Company (SOC). They act in a role of stewardship on behalf of the Shareholder and the people of South Africa. Therefore, the role and effectiveness of SOC Boards is a matter of great importance to the effective running of the enterprise.

I place great emphasis on the importance of induction and orientation of Board because the public sector is a unique and complex environment. It is a space where you will be dealing with a multiplicity of essential stakeholders who may feel to have legitimate reasons to influence the work of the SOC. The induction is meant to equip you to be able to navigate in this space and to allow for agility in performing your duties in providing strategic direction to the SOC. It is not an easy balancing act.

Director induction, orientation and on-going development are vital to the effectiveness of Boards and individual Directors. It should not be approached as a "tick-box" exercise but must equip Directors with the knowledge, skills and understanding to contribute with substance to an effective Board.

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In presenting this induction and orientation session, the DPE's aim is to promote and enable a consistent and comprehensive approach across SOCs under DPE's portfolio. This session is an opportunity for the Board to hear first-hand from the Shareholder Representative on expectations, the strategic intent and protocols for the Board.

You have been chosen to serve as Directors of Denel after a rigorous selection process which involved wider consultation including Cabinet. I am therefore confident that this induction and other forms of ongoing training will adequately equipped you as Board members to discharge your accountability to the SOC and the developmental programme of Government.

DENEL's MANDATE

The Department of Public Enterprises is tasked to look after six (6) State Owned Companies. Unlike the other SOCs, Denel does not have an enabling legislation. At the main Denel is governed by the Companies Act and the Public Finance Management Act (PFMA).

Let me share with you a brief history of Denel

Denel was established when the manufacturing subsidiaries of Armscor were split off in order for Armscor to become the procurement agency for the Department of Defence, and the manufacturing divisions were grouped together under Denel as divisions. Denel was established in terms of the Companies Act as a state-owned industrial company under the Ministry of Public Enterprises in April 1992. It inherited most of Armscor's

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production and research facilities, and over 15 000 employees. The company has undergone a number of restructuring processes necessitated by a changing international and regional political landscape as well as domestic government priorities. The company had to dispose of a significant portfolio of non-core assets and to invite strategic equity partners into those business units which were bleeding. Now, the employment levels at Denel is 4500 people.

In the absence of an enabling legislation, the Minister of Public Enterprises as the Executive Authority sets the mandate for Denel after having consulted with Cabinet. Denel is a strategic national asset. Denel primary purpose for Denel existence is to provide, grow and maintain strategic and sovereign defence capabilities to the country's armed forces and other security services.

Therefore, Denel is one of the key strategic components essential in maintaining the sovereign integrity of our country. Chapter 15 of the Defence Review 2014, the country's blue-print defence document, clearly outlines the role that Denel is expected to play with regard to its primary role. I will urge the Board members to familiarise themselves with the Defence Review and to share with me and the Department your view on how you see the Defence Review influencing your role of overseeing Denel.

Over and above its primary role, Denel has a critical role to play in the economy particularly in the area of advance manufacturing. Growing the economy and, in particular, reviving the local manufacturing sector is at the heart of Government's drive to reduce unemployment, poverty and inequalities. Denel has advanced

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industrial manufacturing capabilities which include highly specialised engineering skills which are critical in this effort.

STRATEGIC INTENT WITHIN GOVERNMENT'S STRATEGIC OBJECTIVES

The work of Government is directed by the National Development Plan (NDP) through the five year Medium Term Strategic Framework MTSF. The SOC are an integral part in achieving the aims of the MTSF. These are:

1. Sustainable and inclusive economic growth of greater than 5%;
2. Increasing the investment rate to 25% of GDP;
3. Increasing public sector investment to 10% of GDP;
4. Far higher levels of employment creation; and
5. More rapid reduction of inequality, including de-racialisation of the economy.

It is my expectation that the Denel and SOCs in deriving their strategies and business plans, they will ensure that these are aligned to the programme of economic, socio-economic, and political objectives of government. Denel has been exemplary in this regard, and I urge the Board to ensure that this track record is maintained.

I therefore present the Shareholder's strategic intent statement for Denel

The expectations of the Shareholder (which are aligned to both the NDP and MTSF) with regard to Denel are defined in terms of the following objectives:

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1. Supporting, growing and maintaining the DOD's sovereign and strategic industrial defence capabilities
2. Denel acting as a catalyst for advanced manufacturing
3. Increasing sales, product and service offerings
4. On-time and on-cost programme delivery on major programmes
5. Transformation of the work force at all levels
6. Skills development
7. Ongoing compliance with policy and regulation
8. Research and Development
9. Corporate social investment and environmental responsibility
10. Reduce reliance on State support. Government Guarantee (R1.85 billion) may not be renewed when it expires in September 2017. I would urge the Board to ensure that the order book is converted into quality revenues and profits that will eventually see Denel surviving on the strength of its own balance sheet

KEY STAKEHOLDERS OF DENEL

As I pointed out earlier in my introduction that Denel is operating in multi-stakeholder environment. It is important to understand the dynamics of each and every stakeholder. The following are one of key strategic stakeholders:

1. The DOD. The primary existence of Denel is to ensure security of supply of key capabilities to the DOD and the South African National Defence Force. The Department has negotiated a Memorandum of Cooperation with the DOD to formalise a common approach with regard to the role and the support that should be given to Denel.

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2. Armscor as procurement agency of the DOD. Maintaining sound relations with Armscor is vital considering that over 40% of Denel's revenue is sourced through Armscor. Armscor is also key in the funding most of Denel's research and development work.
3. The Department of Trade and Industry particularly in the areas of industry development. The Industrial Policy Action Plan (IPAP) is a critical policy that locates defence and aerospace industry at core of advance manufacturing.
4. Department of Science and Technology and the CSIR in the area of technology development.
5. Local industry which is key component of Denel's supply chain
6. Denel's own employees

LEVERAGING RELATIONSHIPS

South Africa has number of bi-lateral and multi-lateral relationships with many countries. I wish to request the Board to look to leverage on this to increase Denel's global presence. There are opportunities to be exploited for example within the BRICS and IBSA multi-lateral arrangements. Of all the SOCs, Denel is being viewed as an ideal one to benefit from these kinds of relationships.

Denel is ideally placed to play a leading role as a major supplier of defence solutions in the growing African market. Concerted efforts are required for Denel to have a sizeable foothold in the continent. The Department is available to assist Denel in this regard.

One area which is important but somehow battling to takeoff is the issue of SOC to SOC collaboration. Denel's engineering capabilities are so advanced. With proper discussions, some of these capabilities could be used to address some of the challenges that other SOCs are facing. Denel is primed to play a significant role in the

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localisation and indigenisation of certain critical components that are needed by other SOCs. The conversations in this area of collaboration must begin in earnest.

DENEL'S PERFORMANCE 2014/15 AT GLANCE

I have felt it necessary to repeat the statement I made to the outgoing Board at the AGM yesterday on the performance of Denel in the last financial year.

1. The SOC achieved 88% of the Shareholders' Compact targets in the last financial year. I am happy with the performance, as it is amongst the best in the SOCs in our portfolio. I however wish to challenge the Board and management to achieve 100% of set targets. Excellence must not be compromised;

2. I am pleased with the strides in increasing black people and women representation at all levels of the organisation – 53% HDI representation is a movement in the right direction. We should however not forget that South Africa belongs to all those who live in it – the full spectrum of the rainbow nation should not be lost.

3. Denel has maintained the strategic and sovereign industrial capabilities and ensured alignment of these capabilities with the 2014 Defence Review. This has been done while cultivating a good working relationship with the SANDF and DOD, who still account for over 40% of Denel's revenues. I urge the Board to ensure that this state of affairs is maintained. We cannot afford to have this relationship strained.

4. Excellent execution of strategic acquisition projects. This has been done on the back of Denel's ability to attract and retain some of the best executive talent in this country. Please ensure that it is retained.

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I noted to the previous board and executive management the following areas that require further effort:

1. Research and Development: Denel is a high technology enterprise and it is accepted truth with these enterprises that investment in research and development is a key driver for business sustainability.

2. Transformation: We must always remind ourselves that SOCs are operating within a complex socio economic environment given our past. Your excellence will not only be judged in terms of how big your revenue and profits are but on whether our people are benefiting from these revenues. I therefore expect Denel to pay special attention to enterprise and supplier development directed to bring the previously disadvantaged groups at the core of your supply chain.

   The defence industry is one of the least transformed in the country. What concerns me is that some players are so arrogant about their lack of appetite to embark on meaningful transformation. Denel has the necessary weight and muscles to correct such unhelpful attitudes by ensuring that you transact mainly with entities and individuals who propagate transformation and inclusivity.

3. Skills development: The defence industry, like all the productive sectors of the economy, has become increasingly vocal about how fewer students are focused on STEM (science, technology, engineering and mathematics), and how that may eventually harm sustainable continuity. Denel makes a vital contribution to the skills base of the country, especially through the training of artisans and qualified engineers, of which are critical. We encourage you to continue your contribution to skills development in the country by training beyond the needs of Denel.

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COMPLIANCE WITH LAWS THAT GOVERN THE SECTOR

Trading with arms is a sensitive matter. The integrity of Denel as a responsible trader in arms will stand or fall on the SOC's strict compliance with our own laws, foreign laws where you conduct business as well international treaties. South Africa's arms control regime is managed in terms of the National Conventional Arms Control Act. The National Conventional Arms Control Committee (NCACC), a committee made of Cabinet Ministers is tasked with ensuring strict adherence to the Act. This shows how serious Government is in making sure that local companies trade responsibly

Denel still has a handful of serious and unresolved cases in of alleged underhand activities in trying to sell armaments to other countries. The two major cases have been running for over a decade now. These do not only tarnish the SOC's image but that of the country as well, for as long as they remain unresolved. I therefore wish to request the Board to give impetus in trying to get finality on these matters. The Department is available to assist Denel in this regard. I want to urge the Board to ensure that the SOC has robust framework in how it appoints marketing agents in order to mitigate against costly litigations and reputational risks.

GOVERNANCE, ACCOUNTABILITY AND ETHICS

The Board is accountable for the performance of the Company, with Directors being responsible for overseeing the management of the business and affairs of the Company.

Thus, the Board is urged to focus on getting on with decision making on business matters and not attempt to get the Shareholder Representative to make such decisions. I value consultation and the need for the Shareholder to be alert to issues of the Company. However, discussions must translate into formal decision making, when relevant.

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Between the Board, through the Chairperson, and myself as Minister, there must be mutual professional respect for each other's roles and responsibilities. Therefore, such consultations and discussions, as indicated above, should not be an attempt to bulldoze or strong-arm the Shareholder Representative into taking decisions.

Since my appointment as Minister, I have witnessed how Boards can become divided by factions amongst the Non-Executive Directors themselves and between the Directors and Management. This behaviour and relationship challenges should not be allowed to hinder the Board's ability to perform.

The SOC procurement budgets for both big and small items may often be subject to attempts by rent seekers to influence the positions they take:

1. I note the submission by the company of documentation relating to disclosure of interest, among other things. The management of conflicts of interest must be transparent and accountable. I expect Directors, Management and Staff alike to adhere to policies and procedures of disclosure and recusal.

2. However, in the instance of having a new Board, I take the opportunity to request Internal and External Audit to carefully assess the materiality of contracts being held by Directors (through related or inter-related companies, directly or indirectly), and provide me with the assessment and recommendations, within the next month.

3. In the same submission, the Board has provided me with the composition of Board Committees. I understand that the business of company must proceed, while I consider the submission and provide feedback.

Relationship Management in the best interest of the Company, being mindful of government's national objectives:

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1. I must stress that the Board must develop and maintain a healthy relationship with the GCE and the Executive Management team as a whole. Constructive tension is necessary to sustain a successful business.
2. However, Directors should not be influenced by individual EXCO members or factions within EXCO or by "technical teams" who may have their own agendas.
3. Directors must be wary of being "captured" by EXCO members who serve in Board Committees.

Directors must, with speed, get to know as much as possible about Denel and local and global defence and aerospace industry and not just about what lands on your formal agendas. If necessary, undertake further training and development so that you are able to fulfil your fiduciary duties to the best of your ability.

CONCLUSION

In conclusion, i wish to encourage everyone in Denel to fully embrace the new Denel mantra of **"From Good to Great"** which is based on Denel's long term strategy. It should serve as a common rallying message for all to make Denel a true successful story.

I thank you

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COMMISSION OF INQUIRY
INTO STATE CAPTURE

Appendix A

DENEL GROUP

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20 November 2014

Ms Lynne Brown, MP
Minister of Public Enterprises
Department of Public Enterprises
Suite 301, Infotech Building
1090 Arcadia Street
Hatfield

Dear Minister Brown

TRANSFORMATION AND RISK MITIGATION PLAN ITO ANTICIPATED RETIREMENTS

In response to your request at Denel's Annual General Meeting to present a risk mitigation plan regarding retirements, and initiatives to accelerate the achievement of representivity within Denel, please find attached the plan highlighting the following key aspects:

1. Workforce profile analysis and mitigating measures;
2. Talent acquisition and attraction;
3. Talent Pipeline model;
4. Internal Training; and
5. Attraction, Development and retention of women.

Minister I am pleased to advise you that the Board considers Transformation in a serious light and that the report that is being presented has been deliberated and considered at both the Personnel, Remuneration and Transformation Committee and the Board, prior to being signed off for your consideration.

Yours sincerely

Martie J Janse van Rensburg
Chairman of the Denel Board (Interim)

cc: Mr Bulelani Magwanishe – Deputy Minister of Public Enterprises
Ms Matsietsi Mokholo – Acting Director General: Department of Public Enterprises
Mr Kgathatso Tlhakudi - Deputy Director General: Manufacturing Enterprises

Annexure A

1. BACKGROUND:

At the Denel AGM (Annual General Meeting) in August 2014, the Minister Lynne Brown requested Denel to provide the department with a risk mitigation plan regarding retirements. This report is highlighting Denel's current workforce profile and also indicates the mitigating measures taken to address areas of concern with respect to retirements.

The mandatory retirement age at Denel is 65 years but employees are able to go on early retirement from the age of 50 with consent from the employer and from 55 years old without consent from the employer. Due to the financial volatility experienced in the economy, most employees work until the mandatory retirement age. Denel's Retirement Fund (DENRET) has modelled its investment strategy accordingly and investments are changed at the age of 55 years to accommodate this phenomenon.

The median age of Denel employees is 46 years. For Denel this signifies a good balance between younger inexperienced employees and more mature seasoned professionals.

2. WORKFORCE PROFILE ANALYSIS AND MITIGATING MEASURES

Denel requires a high calibre set of skills to manufacture, design, develop or integrate products such as artilleries, missiles, aircraft, unmanned aerial vehicle systems and optical payloads based on high-end technology. Hence 74% of its workforce comprises of technically skilled professionals.

A high degree of experience is also of critical importance if Denel was to execute its contracts within the required timelines and according to the standard and quality as expected. This can be attested by the low levels of injuries and fatalities during production, testing and usage.

The skills that are considered core and critical in Denel's business are:

- Engineers and Scientist,
- Artisans and Technicians,
- Project and Programme Managers; as well as
- Technical Line Management.

2.1 Succession Planning:

Denel's Succession Planning policy ensures both Vertical and Horizontal succession occurs. Vertical succession focusses on addressing the hierarchy of the organisation to ensure that Senior Leadership successors are identified and developed.

Horizontal succession focuses on the age profile of the organisation.

The first category, **CATEGORY 1**, is critical positions occupied by individuals that are between age group 61-65 years and for individuals to succeed any individuals in the aforementioned age group in critical positions. In this category at least two (2) successor, per identified position, must be identified and developed for a specific position.

In this category, **CATEGORY 1**, Employees between 60 – 63, the senior incumbent will transfer the skills to the identified successor, whilst also simultaneously executing the job, then from age 64 – 65, the successor will take over and execute the job and the senior incumbent will assume a status of a sounding board, for the successor who has assumed the position. During this time, the potential retiree, will be tasked to document all the processes/procedures,

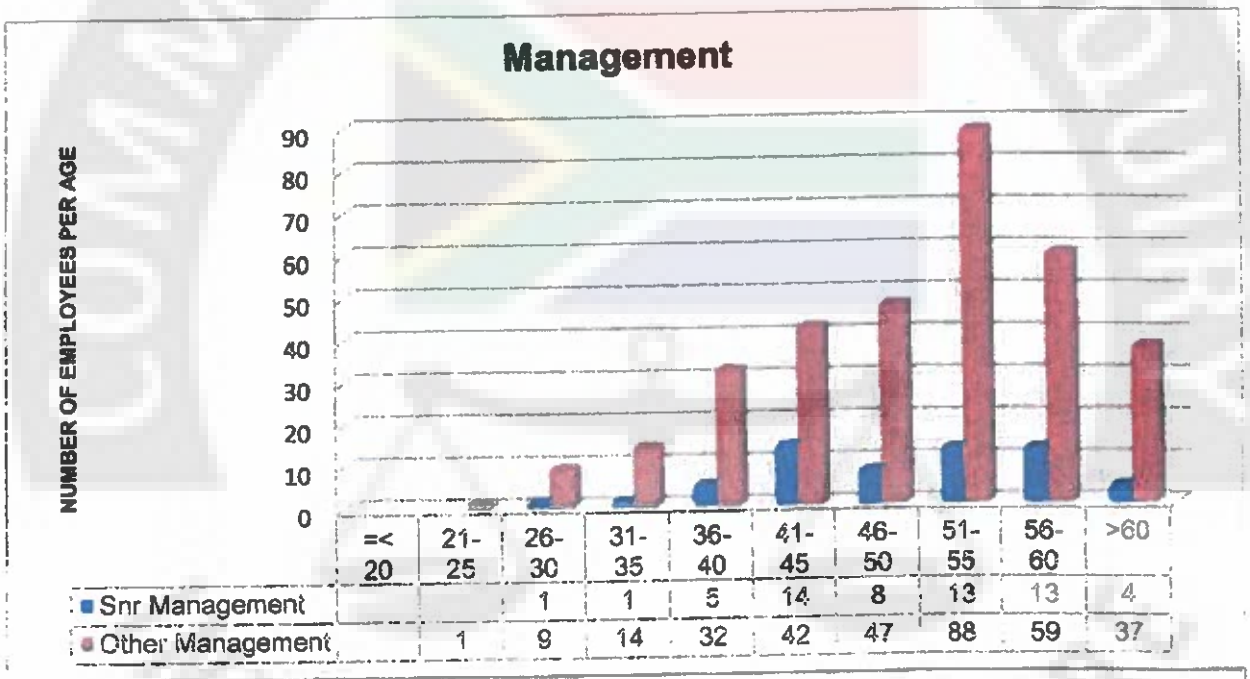
best practices, all necessary know how related to the function, forming the **knowledge hub** to help retain institutional knowledge for the company. In this category the senior incumbent will sign a new performance contract.

The second category, **CATEGORY 2,** is critical positions occupied by individuals that are between age group of 56 – 60 years and for individuals to succeed any individuals in the aforementioned age group in critical positions. In this category at least two (2) successors per identified position, must be identified and developed for a specific position.

The third category **CATEGORY 3** is critical positions occupied by individuals that are between age group 48 – 55 years and for individuals to succeed any individuals in the aforementioned age group in critical positions. In this category a pool of at least three (3) successors, per identified position, must be identified and developed.

2.2 Age Analysis

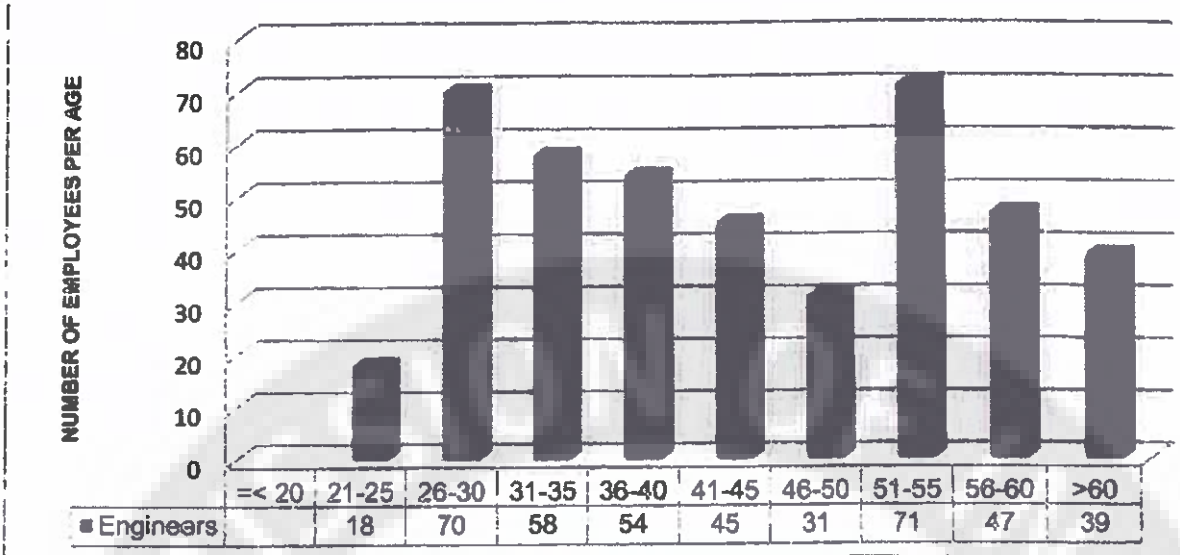
The graphs below illustrate the composition of all employees within the core and critical categories relative to their prospects to retirements. Mitigating measures are also provided to avert risk associated with the retirements.



Analysis & remedial action:
This category comprises of **388** Employees, (median age of **51** years);
Senior Management consists of **59** people and other management which includes both technical and administrative management comprises of **329** people.

- 11% will be retiring in the next 5 years
- 19% will be retiring in the next 10 years
- Risks are managed through the succession planning policy.

Engineers & Scientists

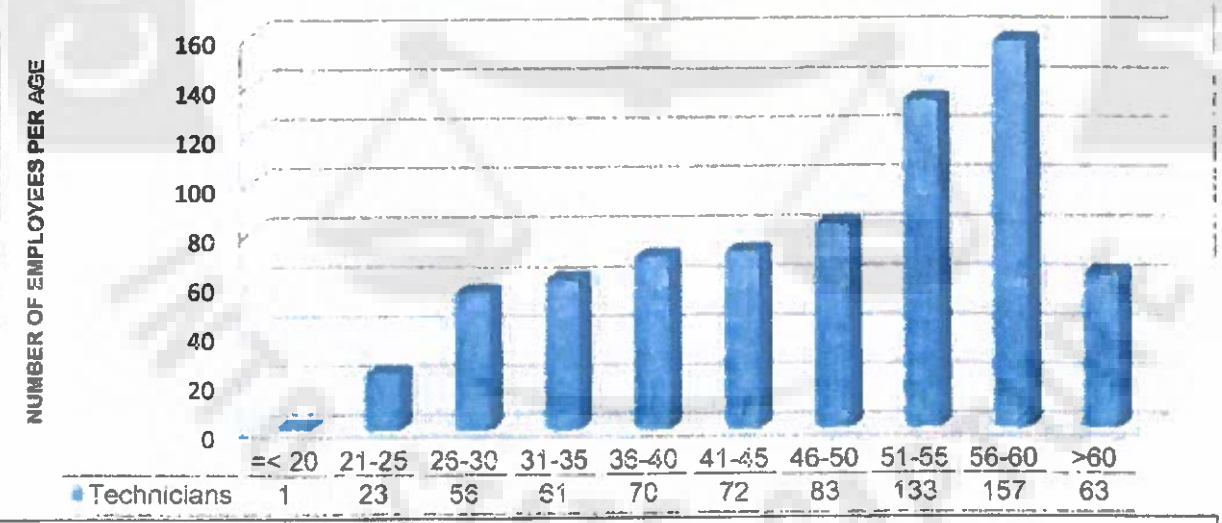


Analysis & remedial action:

This category comprises of **433** employees, (median age of **41** years);

- **9%** will retire in the next 5 years and
- 10% are retiring in the next 10 years
- There is a good spread in terms of age in this occupational category
- Mentorship programmes for skills transfer are in place

Technicians

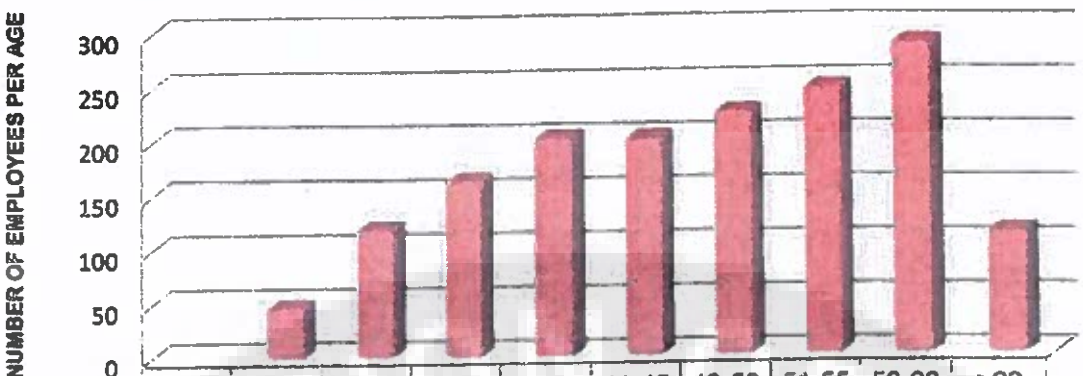


Analysis and remedial action:

This category comprises of **719** employees (median age of **50** years)

- 9% will retire in the next 5 years, whilst
- 22% will retire in the next 10 years
- Mentorship programmes for skills transfer are in place
- Our skills development pipeline programmes focus on youth (e.g. Bursaries)

Artisans

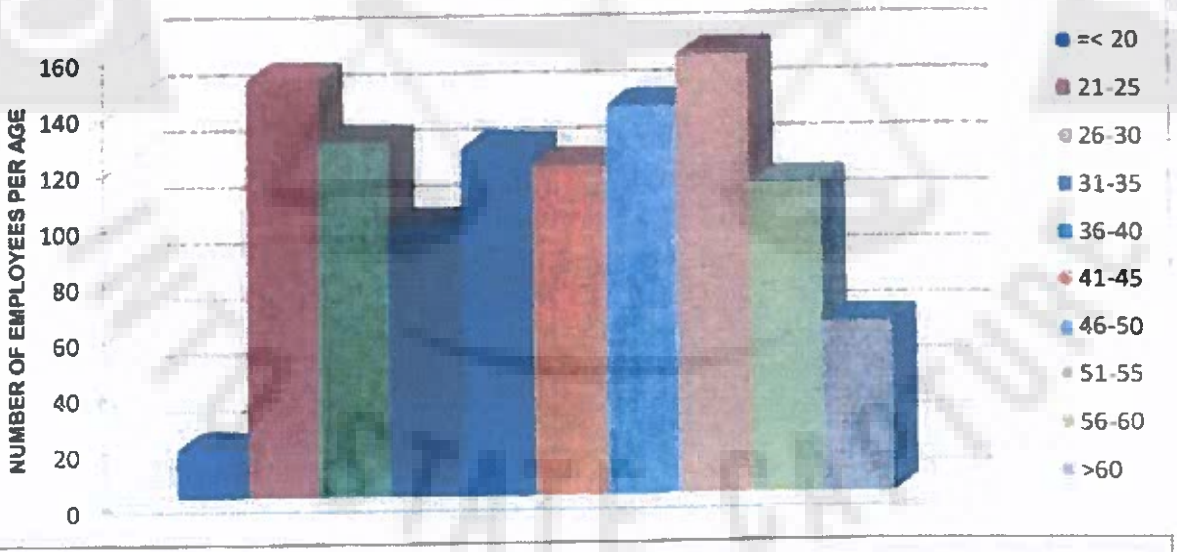


	=< 20	21-25	26-30	31-35	36-40	41-45	46-50	51-55	56-60	>60
Artisans		46	118	162	201	200	224	245	286	112

Analysis and remedial action:
This category comprises of 1 594 employees(median age of 47 years)

- 7% will retire in the next 5 years whilst
- 18% will retire in the next 10 years
- Skills transfer to younger employees is a continuous process
- Our Artisanship programmes focus more on youth (i.e. 35 years and younger)
- Our apprentice programme offered by DTA (Denel Technical Academy) provides a pool of talent to source from.

Support Staff



Analysis:
Support staff comprises of 1 100 employees which constitutes 26% of the workforce.

- There is a good blend between younger and more experience staff within thesupport functions;
- 6% will retire in the next 5 years, whilst
- 10% will retire in the next 10 years
- Skills transfer to younger employees is a continuous process
- This category does not pose a risk to Denel as these skills are readily available in the market

3. TALENT ACQUISITION & ATTRACTION:

Youth development programmes are an essential vehicle to draw technical resources from. For Denel, the scarcity of these resources becomes more pronounced as one considers that the Defence and Aerospace Industries are a somewhat closed and niche market both in South Africa and globally. Competence is developed over a long period of time. It is a challenge to recruit competent and experienced talent from the open labour market.

It is therefore imperative for Denel to be adept at attracting, developing and retaining this scarce talent if it is to achieve its goals of sustainable profitable growth, operational excellence and becoming a respected South African Company.

Skills attraction remains an integral part of achieving business objectives at Denel. Skills attraction focuses on the following key priorities:

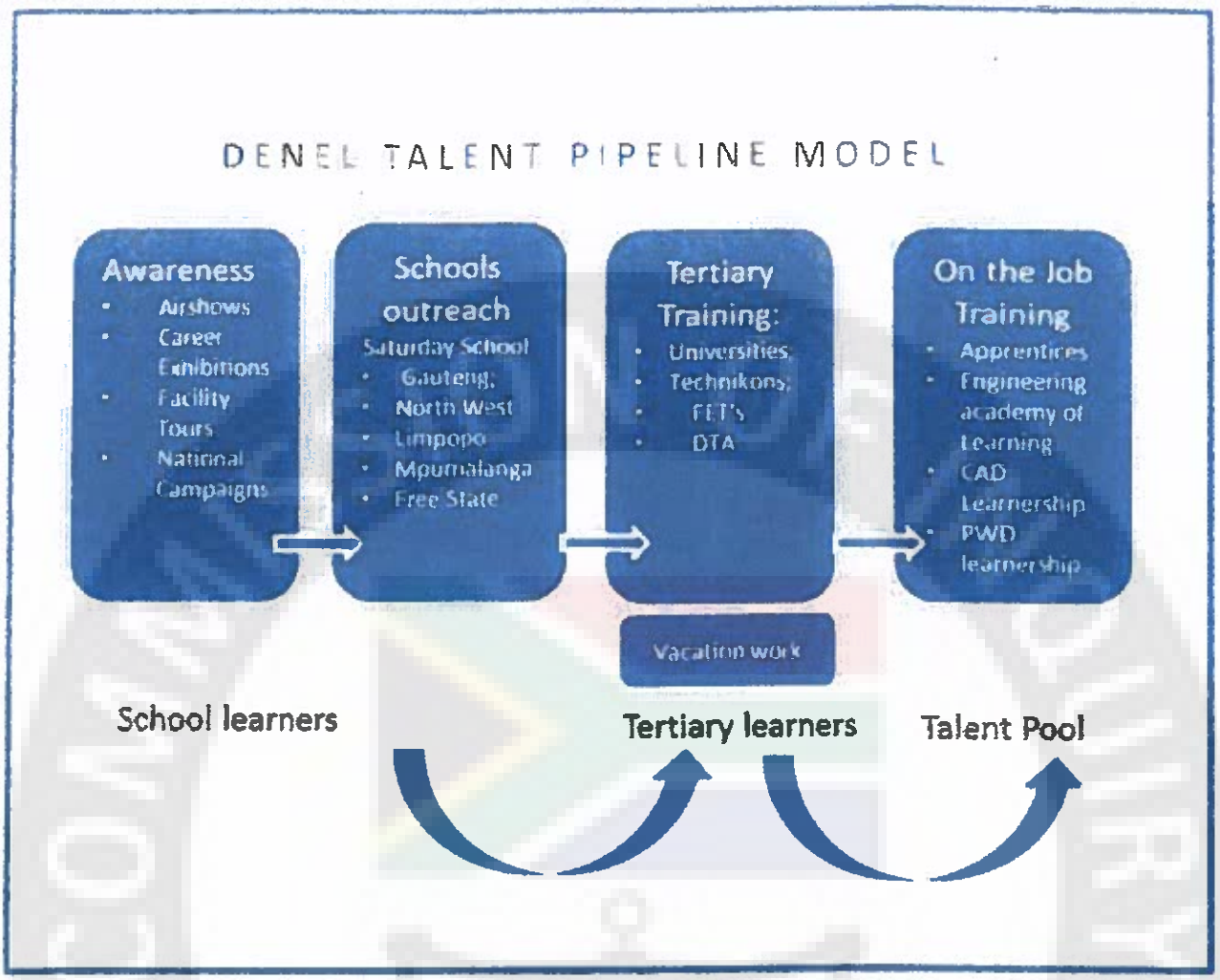
- Employment equity designated groups;
- Employment of females;
- Employment of employees with disabilities;
- Employment of young black employees i.e. under the age of 35 years;

Denel will continue to attract talent through the following recruitment channels such as utilising its own skills development pipeline; head-hunting; recruitment websites; social media platforms; recruitment agencies etc.

4. TALENT PIPELINE MODEL

The diagram below illustrates Denel's Talent Pipeline modes and comprises of four elements namely:

1. Creating awareness amongst the youth;
2. Schools Outreach Programme;
3. Tertiary Education; and
4. On the job Training.



4.1 Awareness

Denel targets specific sources to attract its pool of talent and create its skills pipeline.

Denel is involved in numerous Corporate Social Investment activities which creates awareness of the importance of mathematics and science amongst youth. Denel exhibits at various career expos showcasing the products and services which stimulates interest amongst youth, participates in the various National Campaigns; conducts facility tours, and hosts learners at Air shows and other trade fairs. These activities assist Denel in acquiring talent for its various skills programmes.

4.2 Schools Outreach Programme:

The **School Outreach Programme (SOP)** seeks to improve the standards and pass rate for learners by providing extra tuition in mathematics and science. The programme serves as a feeder to the various Denel bursary programmes. In Gauteng, Denel engineers are involved in tutoring learners on Saturdays and volunteer their personal time without any reward. The programme is also running in the North-West, Limpopo, Free State and Mpumalanga provinces with learners from grade 11 to 12 participating. In the provinces, learners from surrounding schools are bussed to a central school, where teachers from the community provide the extra tuition. There are a total of **455** learners currently participating in the Mathematics and Science outreach programme in the 5 provinces

These learners then form part of Denel's skills development pipeline and are eligible for a bursary to study at a Tertiary Institution (University/ Technikon) or at Denel Technical Academy.

4.3 Tertiary Institutions:

As Denel operates in the high tech space, cooperation with academic institutions is pivotal to ensuring that human capital and technology development are in sync. These relationships also provide a platform for the attraction of top talent. The company played an active role in participating in various top university career fairs nationally including Pretoria, Cape Town, Stellenbosch, Kwazulu Natal, Witwatersrand, Johannesburg, Potchefstroom and Nelson Mandela Metropolitan Universities, where our employer value proposition was proudly displayed. Students often visit our facilities where our products are showcased and are able to interact with employees and gain a better understanding of their chosen career.

4.4 Technical Training

Denel's flagship programme is its artisan training academy, within the Denel Technical Academy (DTA). DTA offers South African Civil Aviation Authority (SACAA) certified courses and several other advanced and type training courses. DTA has been purposely structured and resourced to deliver technical training, and is not currently geared to deliver other skills development programmes e.g. management training. The academy creates a foundation for future employability of young learner's, trainees and apprentices and offers the first year theoretical and practical training required to complete a trade qualification. At DTA, learners have to spend a minimum of 1400 hours/35 weeks at the school.

During the period learners have a combination of theory and practice which varies according to the trade they are enrolled for. The split between theory and practice could be between 20% to 50% i.e. Aircraft Structural workers are required to have 20% of theoretical instruction and 80% of their time is spent on practical work. Aircraft mechanical workers require 45% theoretical training and 55% practical training.

These requirements are stipulated by the SAQA (South African Qualifications Authority) and have to be met in order for the qualification to be granted. After successful completion of the first year, learners are then required to perform on the job training for a further 24 to 36 months. Thereafter they return to DTA for a six week intensive trade test preparation period. DTA is also registered as a trade test facility.

Recently there has been a review of the DTA Strategy to ensure alignment with the technical needs of the Denel Group and the country. Previously DTA primarily focused on Aerospace training but has increased its capacity to focus on Engineering related trades due to market forces.

During the 2013/2014 financial year, Denel trained 231 apprentices enrolled in various fields of artisanship and 764 learners on short courses. DTA offers rudimentary training opportunities for the first year of apprenticeship in the following fields*:

• Aircraft avionician	• Aircraft electrician
• Aircraft instrument mechanic	• Aircraft mechanic
• Aircraft radiotrician	• Aircraft structural worker
• Electrician	• Fitter and turner
• Machine tool millwright	• Toolmaker and jig maker
• Turner and machinist	• Welder

Applications for the January 2015 intake will close at the end of October 2014. Approximately 140 first year learners will be fully funded by Denel and the NSF to complete a trade qualification. 147 apprentices in the various years of qualification were sponsored by Denel during the 2013/2014 financial year.

Denel is able to recruit top talent from DTA for its apprenticeship programme. Increasing the apprenticeship scheme is critical to ensure that sufficient apprentices are trained for industry, which is in line with the developmental agenda of the State.

4.5 Bursaries

Bursaries for students in relevant technical disciplines are used as a means of creating a skills pool for future needs. The aim is to employ these bursars upon successful completion of their studies.

Students are taken into the bursary programme annually and are individually mentored and supported throughout their studies. Vacation work is also made available to these learners to familiarise them with a real workplace environment. It is our practise that the bursars who complete their university studies are employed within the group. The purpose of the bursary scheme is to have a readily available pipeline of qualified engineering students who (post-matric) can apply for engineering degrees in the following disciplines:

- Electronic
- Mechanical
- Industrial
- Software/Computer
- Mechatronic

Bursaries cover, tuition; accommodation; books; a computer allowance and as well as a stipend. Applications for January 2015 closed on the 15th of August 2014. Denel's hands-on approach ensures bursars are fully supported so that they obtain their qualifications and join the group. During the 2013-2014 financial year, Denel sponsored 82 bursary students in various years of study towards obtaining degrees in the disciplines mentioned above.

Many of the Denel divisions require advanced technical skills to conduct their business. Accordingly, processes are required to ensure that highly skilled technical staff stay abreast of advances in technology. Bursaries are also offered to employees to assist their long term development and enable them to make a stronger contribution in their current and future roles.

4.6 Internships

Graduates mostly from technical disciplines, are employed on internship programmes by various divisions. This allows the graduates to acquire critical workplace skills, whilst simultaneously affording divisions the opportunity to assess the graduates' employability, although they are not bound to employ these graduates on a full-time.

- **CAD (Computer Assisted Drawing) Learnership:**

  This learnership commenced during 2013 with six learners completing this one year programme. The learners successfully completed both their theoretical and practical component of the programme, and commenced permanent employment at Denel. Due to the success of this programme, it will be conducted annually.

- **Administration Learnership- PWD (People with Disabilities):**

  Another first for Denel, this learnership programme started in August 2014, in order to improve our representivity of PWD's. This one year administration learnership will also provide both practical and theoretic training for these learners. On successful completion learners would be offered permanent employment.

4.7 Engineering Academy of Learning (EAL)

The EAL is a work-based platform that provides for the training of graduate engineers in the form of an Internship. This programme enrols 35 graduates each year. The EAL was established to develop and grow graduate engineers to enable them to be productive in as short a time as possible. The EAL uses a multifaceted approach to develop graduates by combining formal courses, on the job training and a development project into a one year internship programme for graduate engineers. Interns spend 50% of their time working within a department on actual projects, and the remaining 50% of their time executing a training product development project and attending various training courses.

5. INTERNAL TRAINING:

Denel has re-aligned its Learning and Development Strategy and processes to encourage development and create a learning organization. The L & D strategy will ensure that training interventions are aligned and ultimately supports the Corporate Strategy. Special emphasis is being placed on the growth and development of younger employees as well as black people. During the 2013-2014 Financial year, Denel spent over R42 million on employee training.

5.1 Leadership, Management and Supervisory Skills Development:

A leadership Management and Supervisory Development Framework was developed by Denel and has been implemented since March 2009. Specific functional and behavioural competencies were developed for all three levels of leadership. The programme has been re-modelled to ensure achievement of the Denel strategy and new competencies and methods of development have been introduced.

With the Competency Framework as a foundation these programmes will undoubtedly enhance Denel's pursuit for growth and sustainability. Partnerships have been established with business schools and other service providers in order to support this leadership and management initiative. The table below indicates the methods of leader development.

1. **Developmental Relationships** • Mentorship • Professional Coaches • Peer Learning partners • Social identity networks • Communities of practice	2. **Developmental Assignments** • Job rotations • Expanded work responsibilities • Temporary assignments • Action learning projects • Leadership roles outside work
3. **Feedback Processes** • 360 degree feedback • Assessment centers • Performance appraisals	4. **Formal Programs** • University programs • Skills training

5. Self Development Activities • Reading (books, articles, online resources) • Speakers (knowledge experts) • Professional conferences • Trade shows	

5.2 Succession Planning

Denel has acknowledged that Succession Planning is a business imperative to ensure survival, growth and profitability of a company. The objective of Succession Planning is to create a pool of quality successors for critical and strategic positions to serve a purpose of immediate availability when a position becomes vacant, eliminating a strategic void, to purposefully develop individuals in preparation for future strategic positions.

The company has identified (Group-wide) key positions for Succession Planning, as well as individuals who are approaching retirement age (managing risk). Incumbents, predominantly young ACIs with high potential have been identified to be groomed as future successors. This includes positions of Deputy CEOs, who have been selectively identified to replace current divisional CEOs at the appropriate time.

5.3 Executive Coaching

Formal Executive coaching relationships have and continue to be established for Denel Executives and Managers as part of the leadership and management development programmes. Divisions implement coaching initiatives as informed by their respective developmental needs. Coaching relationships will continue to align employee behaviour with the macro strategy of the Group.

5.4 Individual Training & Development and Career Paths

Each employee has a personal development plan to target learning interventions.

Career paths have been developed to encourage younger employees to choose the paths that would best contribute to the success of the Group and best suits the individual. An example of a career path in Denel is as follows:

- Line management
- Project management
- Programme management
- Technical expert

5.5 Workplace skills plans

Divisions, as part of their skills development processes, develop workplace skills plans which deal with training that is core or statutory for that specific business. Divisions are registered with their respective SETAs, which ensures that training obligations are managed appropriately and aligned to the SETA requirements.

5.6 Mentorship

Each Denel division has a mentorship plan that is constantly tracked and evaluated by the divisional Training and Transformation Committee. These programmes assist in the identification of future technical and managerial leaders and on the development of technical competence and productivity.

6. ATTRACTION, DEVELOPMENT AND RETENTION OF WOMEN

In order to improve the representivity of women within the organisation, Denel participates in various programmes. These programmes target female learners from school to university graduates to broaden the talent pool from which Denel can appoint female employees. Various programmes are also run within the organisation to ensure that female employees are developed and retained within the organisation.

Denel also sponsors WomEng, a non-profit, volunteer organisation aimed at attracting, developing and nurturing the next generation of women engineering leaders. This organisation presents an invaluable platform for the advocacy, advancement and education of females entering the engineering industry.

The table below reflects Denel's programmes and investment to address gender representation within the organisation:

Programme	Qty	Cost of programme	Targeted allocation %	Actual allocation towards women
Schools Outreach Programme	450	R500 000	70%	R350 000
Bursaries	90	R10 800 000	50%	R5 400 000
Artisanship	35	R3 500 000	50%	R1 750 000
Graduate Assisted Training Learnership	7	R2 100 000	50%	R1 050 000
Ad Hoc Learnership (PWD)	12	R1 200 000	100%	R1 200 000
Leadership Development Programme	65	R2 925 000	60%	R1 755 000
Engineering Academy of Learning	35	R12 000 000	50%	R6 000 000
TOTAL SPEND				R17 505 000*

** Excludes ordinary skills development expenditure i.e. statutory training; internal bursaries; job related training spend or sponsorships.*

STATE CAPTURE

DENEL SOC LIMITED

Annual General Meeting to be held on	:	23 July 2015
Memorandum Number	:	6
Agenda Item Number	:	8.5
File Reference	:	

BOARD SOCIAL AND ETHICS REPORT

1. INTRODUCTION

As per the requirement of s 72(4) of the Companies Act, State Owned Companies have to establish Social and Ethics Committee which makes it a statutory committee. The committee membership has to be confirmed by the Shareholder at the Annual General Meeting. Denel SOC Ltd established the Committee on 23 November 2011.

The Committee comprises of the following three Non-Executive Directors:

- Prof Stella Nkomo (Chairperson)
- Dr Gert Cruywagen
- Mr Mavuso Msimang

2. MANDATE

The purpose of the Committee is:

- To advise the Board in regard to responsible corporate citizenship and the ethical relationship between the company and society. The Board Social and Ethics Committee ("Committee") will manage the company's legal and moral obligations for its economic, social and natural environment, including the objectives and standards of the company's conduct and activities.

2.1 Main responsibilities are as follows:

The Committee will manage and monitor the company's activities to achieve and maintain world-class standards in the company's social and ethics environment, with due regard to all relevant legislation, policies, legal requirements and codes of best practice. The Committee's terms of reference were approved by the Board and is reviewed on an annual basis.

3. HIGHLIGHTS FOR 2014/15 FINANCIAL YEAR

These following items cover the main 5 areas of focus that the Committee is mandated to oversee. They are:

3.1 Fraud and Corruption Prevention;
3.2 Corporate Social Investment;
3.3 Transformation including BBBEE Status;

3.4 Enterprise Development; and
3.5 Occupational Health and Safety;
3.6 Stakeholder Management;

3.1 Fraud and Corruption

The Committee reviewed the Companies fraud and corruption prevention strategy, which is informed by Denel's values of integrity, the principles of the UN Global Compact and the requirement of the PFMA to prevent financial misconduct and fraud. In the year under review, the Committee noted that Denel became a member of SA Ethics institute, which further entrenches the company's commitment to be seen as a good corporate citizen.

The Committee also reviewed the confidential fraud and corruption hotline disclosures and were comfortable that out of the nine cases reported through the hotline, none were fraud related, but rather HR matters that were addressed accordingly.

The Committee is comfortable that the CCM process, diligent management assessments, as well as external and internal audit procedures which include the Auditor General requirements of supply chain fraud risk assessment, highlighted no instances of fraud and are effective in complementing fraud and corruption detection.

3.2 Corporate Social Investment (CSI)

In terms of making an even greater impact, the Committee proposed that the group moves towards a fully integrated / consolidated CSI function. The Committee noted that the company initiated some events which have seen all divisions working together in ensuring a maximized utilization of resources and the sustainability of CSI.

The Committee noted that in addition, the CSI function has been integrated into the Group Corporate Communication function to enhance the brand image and reputation of the company while also positively impacting on the company's public license to operate. An integrated Corporate Communication and Corporate Social Investment strategy will be shared with the Committee at its next meeting. Refer **Annexure A** i.t.o. CSI consolidated spend.

The group hosted the following consolidated initiatives in the quarter under review.

- **Inaugural Denel Top Young Achiever Awards** - These awards which were attended by the Deputy Minister of Public Enterprises, Mr Bulelani Magwanishe were aimed at recognizing all learners who had achieved outstanding results in all our programmes for the year 2014.

- **Inaugural Denel Career Expo** - The focus of the career expo was at creating awareness of the various careers available within the Denel group to Grade 9 – 12 learners and was attended by over 1000 learners from schools in the Gauteng North region.

- **Denel participation in DPE led engagements** - In ensuring continued awareness amongst the youth especially in rural communities, Denel continues to support DPE led initiatives in collaboration with other SOCs, e.g. centred around career exhibitions showcasing the opportunities' available for learners.

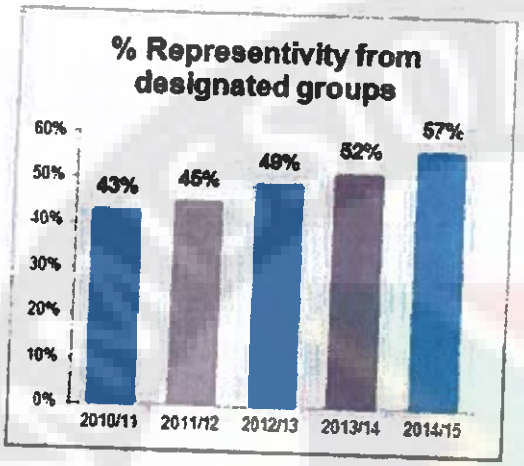
3.3 Transformation Including Year to Date B-BBEE Performance

Denel's Transformation Programme is comprised of two components. The one component focuses on B-BBEE compliance and the other on improving the workplace climate. This

report provides a consolidated overview of the results achieved by Denel and its divisions with regards to Climate Improvement results and B-BBEE performance for 2014/15.

- **Climate improvement performance** - The Group has once again improved its index score from **77.64%** to **80.51%** overall.
- **B-BBEE performance** - Denel is proud to have been awarded a **Level-2** B-BBEE status in recognition of its contribution towards transformation. The improved rating from level 3 to 2 confirms Denel's growing commitment not only to making its workplace more representative but also to empower and support its suppliers and to care for the communities in which it operates.

The table below reflects the % representivity from designated groups.



3.4 Enterprise Development

In FY15 the total number of companies that benefitted from the Group's Enterprise and Supplier Development programme was 114. Out of the 114 Black-Owned companies that participated in the programme, 25 were being developed to supply products and services into the core business of Denel divisions. In the previous financial year the number of companies that were developed to supply into the core business was 20, which equates to a 25% improvement. As pointed out in previous reports, the strategic focus is to increase the number of ESD beneficiaries that will supply into the core business.

It is worth noting that there was a significant increase in the Spend on the ESD programme in FY15. The total Spend or Cost of the programme rose from R6m in FY14 to R17.3m in FY15. The significant increase in the Group Spend on the ESD programme was a consequence of the increased focus to accelerate the growth in the number of Black Suppliers for the core business of Denel divisions.

In the light of the recent amendments to the BBBEE Codes, the number of ESD beneficiaries has been increased from 5 to 9 for each division with the exception of Denel Industrial Properties and Denel Overberg Test Range (OTR). Denel Industrial Properties can develop as many as 100 in each financial year due to the nature of Suppliers that it uses. On the other hand, Denel OTR has a very limited number of products and services it utilises, and consequently it does not make sense to expect it to develop the same number of companies as the other divisions in the Group. Naturally, with the increased number of ESD beneficiaries, there will be a corresponding increase in the investment on the ESD programme.

The timing of the Denel Group Supplier Day, which took place on the 5th of March this year, was most opportune as it has made it possible for Denel to identify eligible companies for development from a bigger pool than ever before To ensure the successful

implementation of Denel's ESD programme, we have initiated a more focussed progress reporting against approved plans as well as monitoring the screening of companies that submitted their profiles for registration at the Group's Supplier Day.

3.5 Occupational Health and Safety

The safety risk management process

Denel requires its business units to adopt a comprehensive approach to OHS to protect employees and visitors on site from occupational injuries and prevent occupational diseases to preserve employee well-being. This process involves continuous assessment of the work environment and prioritisation of identified health and safety risks, where appropriate redesigning the work environment to eliminate hazards, provide protective equipment/clothing and safe work procedures. Also to detect, prevent, treat and monitor occupational diseases, Denel has established occupational health centres at each campus operated by qualified occupational health practitioners and occupational health doctors.

Occupational Heath process

Pre-employment, periodic and exit medical examinations were conducted in Denel's occupational health centres and no major deviations were identified. The programme includes high-risk occupations and establishing health baselines to ensure appropriate placement. Divisions conducted medical examinations, occupational hygiene surveys and risk assessments as part of the occupational health programme without major deviations being identified. SHE training was also provided according to operational requirements to heighten awareness among employees.

Loss Time Injury Frequency Rate (LTIFR) performance

Whilst other divisions achieved LTIFR target of <.08 Denel Land Systems and Denel Aerostructures lost time due to finger injuries sustained on duty falling short of the target. Hand tools have been introduced, illumination improved, work procedures updated, and employees trained and made aware of lock-out procedures to mitigate the risk. In line with the growing volumes of contracts in the new year and new employees Denel will place more focus on incident management to prevent accidents in the new year.

Environmental Management

Denel is committed to continuously improve its management activities and operations to minimising waste, prevent pollution and minimise damage to the environment. Environmental responsibilities are addressed throughout the design, manufacture, and transportation processes and by including environmental impact studies and environmental risk assessments in the business units' processes, where applicable as part of an integrated environmental management process.

3.6 Stakeholder management

3.6.1 Group Corporate Communication Plan

The Denel Group Corporate Communication team is positioning the Denel brand through a multi-media communication campaign to reach the general South African public. Preparations are currently underway to launch the campaign on Television, Radio, Print and Social Media networks within the next two months, covering commercial and community media platforms. The focus of the Campaign will be on the Group's good story, which will cover successful achievements in various programmes to reflect Denel's

contribution to the South African Government's developmental programme. (Skills, Bursaries, CSI, etc).

3.6.2 Stakeholder Management Programme

The key objective behind the Denel Group Stakeholder Management programme is to increase brand awareness while at the same time strengthening relationships with stakeholders at all levels of the business. This is an investment into Denel's public license to operate, which often yields returns when the business requires support from outside of its formal structures. Both the divisions and Denel Corporate Office have hosted various groups as part of the ongoing Stakeholder Engagement Programme.

4. CONCLUSION

The Committee's mandate is reviewed annually for relevance and the annual work plan for the following financial year is developed and agreed to in advance, in terms of the priorities and areas that need special attention, e.g. employment equity, BBBEE and fraud prevention measures.

EM Africa
GROUP COMPANY SECRETARY

Date: 30/06/2015

R Saloojee
GROUP CHIEF EXECUTIVE OFFICER

Annexure A

EDUCATION INITIATIVES

Maths and Science Outreach programme

R2.7m - Impacting 455 learners across provinces

- The programme is aimed at addressing the technical skills shortage due to non-participation and poor performance by learners in Mathematics and Physical Science especially in the previously disadvantaged communities. The programme is currently running in the North West, Limpopo, Mpumalanga & Free State Provinces. In Gauteng Engineers employed at various Denel business entities are involved in tutoring these learners on Saturdays without expectation of a reward.

Donation of computers

R7k - (10 computers) Mbenge Primary School in the Eastern Cape

- To assist with computer literacy in rural areas.

Mini Chess programme

R42k - Philena Primary School in Gauteng

- Assist with Maths and science skills

Maths formula booklets

R114k - 3 000 learners

- Denel donates Maths formula booklets which explain concepts to learners in a simplified manner.

Mobile laboratories

R70k - 50 learners per centre in Mpumalanga

- Mobile laboratories were donated to assist centres where there are no facilities

Telematics

R151k - 1 800 learners in North West

- Interactive learner support system which offers revision sessions

Technogirl

R50k - 250 Female grade 9-11 learners

- This is an initiative of the Department of Women Affairs which involves a job-shadowing programme for girls. It provides structured job-shadowing during school holidays to assist learners to make informed career choices and encourages learners to take maths and science subjects

Teacher support

R94k - Grade 0-7 learners at schools in the Western Cape

- Denel pays the salary for extra teachers so that the school can accommodate more learners from the area. Learners from the area would have to commute extensively if they are not accommodated in these local schools

SPORT INITIATIVES

Denel race community marathon

R63k - Impacting 3 000 employees and community

- Denel annually sponsors a road race in Centurion. Participants can participate in either a formal 10 or 21km or the fun run/walk races. Denel also donated water for a community marathon.

INFRASTRUCTURE DEVELOPMENT

Provision of a facility for pre-school children

R32k - Impacting 40 children - Mooiplaas informal settlement

- Denel donated a Wendy house and bought groceries for children at the Mooiplaas informal settlement. This crèche has 42 children.

Provision of a library

R318k - OR Tambo Primary School in Ekhurhleni

- Supplied a fully furnished library to encourage reading. Employees assisted by donating books.

Supporting the building of a school

R211k - Jesus is Lord school school in Limpopo

- The community had no school in the area and learners had to walk many kilometres to attend school.

HEALTH INITIATIVES

Provision of dignity packs

R11k - Impacting 600 learners - Grade 10-12 learners

- Denel donates sanitary protection / dignity packs to learners in disadvantaged communities to avoid absenteeism due to lack of sanitary protection. Girls who cannot afford sanitary protection miss approximately five days of school a month, which amounts to 60 missed school days a year

AWARENESS INITIATIVES

Career exhibitions

R508k - Impacting 30 000 Grade 10-12 learners

- Denel participates in various career expos nationally in order to expose learners to the various careers available for science engineering technology.

Air shows

R477k - Impacting 5 000 Grade 10-12 learners

- Learners from disadvantaged communities get exposed to the world of aviation through air shows. The events ensure that learners are provided with information about the company and possible future careers and they also get to do aviation-related activities.

Joint aviation awareness programme (JAAP) and International Civil Aviation Day (ICAD)

R30k - Impacting 25 000 Grade 10-12 learners

- Partnership with other aviation organisations, e.g. SAA, SAX, Mango, ATNS, SAAF, etc. to create awareness and expose learners to aviation-related careers.

DENEL SOC LIMITED

Annual General Meeting to be held on	:	23 July 2015
Memorandum Number	:	5
Agenda Item Number	:	8
File Reference	:	

PRESENTATION OF THE ANNUAL FINANCIAL STATEMENTS

1. PURPOSE

A Board meeting was held on 26 June 2015, to consider and approve the annual financial statement (separate document) including the following reports:

- the Directors' report, and
- the report of the external auditors
- the report by the Audit and Risk Committee
- the subsidiary list

for the financial year ending on 31 March 2015.

2. RESOLUTION REQUIRED

That the annual financial statements of the company for the financial year ended 31 March 2015, and all matters undertaken and discharged by the Directors on behalf of the company be and are hereby noted.

F Mhlontlo
GROUP FINANCIAL DIRECTOR

Date: 1/7/2015

R Saloojee
GROUP CHIEF EXECUTIVE OFFICER


COMMISSION OF INQUIRY
INTO STATE CAPTURE

DENEL GROUP

LIST OF DENEL SUBSIDAIRES, JONT VENTURES AND ASSOCIATE COMPANIES

1. **100% Owned Subsidiaries**
   - Denel Aerostructures - manufacturing of components for A400M and other OEMs.
   - Densecure – Insurance vehicle for Denel and subsidiaries.
   - Denel Vehicle Systems (previously named LSSA).

2. **Joint Ventures**
   - Tawazun Dynamics – JV in UAE manufacturing precision guided munitions (Denel owns 49%).
   - LMT – Partnership with Pamodzi (BEE) and management (Denel owns 51%).

3. **Associate Companies**
   - Turbomeca Africa – design, manufacturing and sales of gas turbines and engines (Denel owns 49%).
   - Airbus DS Optronics – development and production of optronics, optical and precision engineered products (Denel owns 30%).
   - Rheinmetall Denel Munitions – design, development of large and medium calibre ammunition, mortar, infantry systems and plant engineering (Denel owns 49%).

INTO STATE CAPTURE

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P O Box 8322. Centurion. 0046. South Africa. Tel: +27 (0)12 671 2700 Fax: +27 (0)12 671 2751
Directors: Ms M J Janse van Rensburg (Acting Chairman), Mr R Saloojee (Group Chief Executive Officer), Adv G Badela
Dr G C Cruywagen, Ms Z B Mathenjwa, Mr Z Mhlontlo, Mr N J Motseki, Mr M Msimang, Mr B F Ngwenya, Prof S M Nkomo
Adv M S Ntshikila, Mr M V Ratshimbilani

Executive Director
Group Company Secretary: Ms E M Amos

DENEL SOC LIMITED

Annual General Meeting to be held on	:	23 July 2015
Memorandum Number	:	7
Agenda Item Number	:	9
File Reference	:	

ROTATION OF THE NON-EXECUTIVE DIRECTORS

1. BACKGROUND

Directors are normally appointed for a specific period and may be re-elected, if they make themselves available for this purpose, at the expiration of their term of office. At the 2014 Annual General Meeting (AGM) the Minister requested that the expiring Denel Directors' tenure be extended to the 2015 AGM to enable the Minister to undertake a review of the Board and a proper rotation scheduled be implemented.

2. DISCUSSION

2.1 Retirement by rotation

The following members' terms of office expired at the 2014 AGM, and were subsequently re-elected to hold office until the conclusion of the next Annual General Meeting. In a letter dated 25 May 2015 to the Acting Chairperson, the Shareholder confirmed the completion of the review and the retirement by rotation of the following Board members, with the exception of Mr Motseki who has been re-elected, i.t.o. section 13.11.1:

Ms MJ Janse van Rensburg (Acting Chairperson)
Dr GC Cruywagen
Adv G Badela
Ms ZB Mathenjwa
Mr NJ Motseki
Mr M Msimang
Mr BF Ngwenya
Prof SM Nkomo
Adv MS Ntshikila
Mr MV Ratshimbilani

2.2 Resignation by default

The following Board members who retire by rotation and by default have to resign from the following Committees:

2.2.1 Audit and Risk Committee

Dr GC Cruywagen
Ms MJ Janse van Rensburg
Ms ZN Mathenjwa

2.2.2 Personnel, Remuneration and Transformation Committee

Prof SM Nkomo
Adv G Badela
Adv MS Ntshikila
Mr MV Ratshimbilani

2.2.3 Social and Ethics Committee

Prof SM Nkomo
Dr GC Cruywagen
Mr M Msimang

The Shareholder to note the Board members that retire by rotation, including their resignation from the Board Committees as detailed above.

3. RESOLUTION REQUIRED

That the Shareholder notes the Board members that retire by rotation, including their resignation from the Board Committees.

EM Africa
GROUP COMPANY SECRETARY

R Saloojee
GROUP CHIEF EXECUTIVE OFFICER

Date: 30/06/2015

DENEL SOC LIMITED

Annual General Meeting to be held on	:	23 July 2015
Memorandum Number	:	8
Agenda Item Number	:	10

APPOINTMENT OF EXTERNAL AUDITORS FOR 2015/16

1. BACKGROUND

In terms of King III, the appointment of the external auditors must be approved by the Shareholder at every Annual General Meeting (AGM).

2. DISCUSSION

The external audit was put out to tender during 2011/12 financial year. SizweNtsalubaGobodo was appointed as Denel's external auditor for the next five years, subject to annual renewal at the AGM. The external audit fee for the year ended 31 March 2015 was R10.8m against budget of R10.8 and increase of 6% based on previous year of R10.2.

In line with the Auditor General directive dated 11 February 2015, and subsequent letter to the Group CEO dated 9 March 2015, informing him that the AGSA opts not to perform the audit of Denel SOC limited for 2015/16 financial year and for the company to proceed to appoint an audit firm registered with the independent Regularity Board of Auditors, i.t.o. section 18.1 of the Memorandum of Incorporation.

The proposal is that SizweNtsalubaGobodo having performed Denel's audit for the last three years is still eligible to perform the 2015/16 audit, which is in-line with the Department of Public Enterprises intention that all SOCs must change their audit firm every five years.

3. RECOMMENDATION

It is recommended that the Shareholder approves the appointment of SizweNtsalubaGobodo as Denel's external auditor for the 2015/16 financial year as well as the audit fee for the year be noted.

F Mhlontlo
GROUP FINANCIAL DIRECTOR

Date: 26 June 2015

R Saloojee
GROUP CHIEF EXECUTIVE OFFICER

AUDITOR-GENERAL SOUTH AFRICA

Mr Fikile Mhlontlo
Group Financial Director
Denel SOC Limited group
PO Box 8322
Centurion
0046

9 March 2015

Reference: Denel/ Sec 4(3)/App of External Auditor

Dear Mr Mhlontlo

Appointment of external auditor for Denel SOC Limited

In line with the *Auditor-General Directive*, Denel SOC Limited submitted an updated consultation checklist in respect of the appointment of Denel SOC Limited's external auditor for the financial year ended 31 March 2015.

The AGSA acknowledges receipt of the completed checklist. It was identified from the completed *Consultation of the Auditor-General on the appointment of an auditor*, dated 24 February 2015, that Denel SOC Limited has appointed SizweNtsalubaGobodo as its external auditors.

The Auditor-General of South Africa does not object to the appointment of the above audit firm for the financial year ending 31 March 2015, subject to the following conditions:

1. You are required to bring to the attention of your appointed auditors the content of *General Notice 125 of 2015*, issued in *Government Gazette No. 38464* on 11 February 2015 or any new general notices issued by the Auditor-General from time to time (attached hereto).
2. On completion of the audit, you are required to submit three copies of your audited annual report to the Auditor-General of South Africa.

The Department of Public Enterprises has notified the AGSA that it intends to enforce its state-owned entities to change its auditors (audit firm) every five years as required in the *Protocol on corporate governance in the public sector* paragraph 5.2.19.5. This is subject to an annual appointment process as per the Audit Directive.

Yours sincerely

Tsakani Ratsela
Deputy Auditor General

Enquiries: Zolisa Zwakala
Telephone: +27 (0) 12 426 8355
Fax: +27(0)86 772 3984
Email: ZolisaZ@agsa.co.za

DENEL GROUP

Tel: +27 12 671 2791
Fax: +27 12 671 2833
Email: [redacted]
Ref: AGSA ExternalAuditApp/Feb 15

24 February 2015

Mr Thembekile Kimi Makwetu
The Auditor General of South Africa
300 Middel Street
New Muckleneuk
PRETORIA
0181

Dear Mr Makwetu

DENEL SOC LTD – APPOINTMENT OF AUDITOR

This letter communicates the appointment and discharge of Denel's auditors as required by sections 25 and 26 of the Public Audit Act. The AGSA has within its rights over the years elected not to perform the Denel audit, and as such, Denel appoints external auditors through an open tender.

We wish to advise that the Denel Board having considered the term of office of the current auditor, took a decision to put the audit out to an open tender for the 2012/13 up to the 2016/17 financial years, subject to the appointment confirmed annually at the AGM. The tender process was undertaken in consultation with DPE and resulted in the appointment of SizweNtsalubaGobodo as external auditor for Denel. To promote the development of the audit profession SizweNtsalubaGobodo will outsource 15% of the audit work to Kwinana and Associates, a black owned firm that will work under their supervision.

We hereby confirm that the shareholder has approved for the financial year 2013/14 and 2014/15 the appointment of SizweNtsalubaGobodo as external auditor for Denel.

The checklist as required, when appointing auditors in private practice is attached. We request your concurrence with this course of action.

Yours faithfully

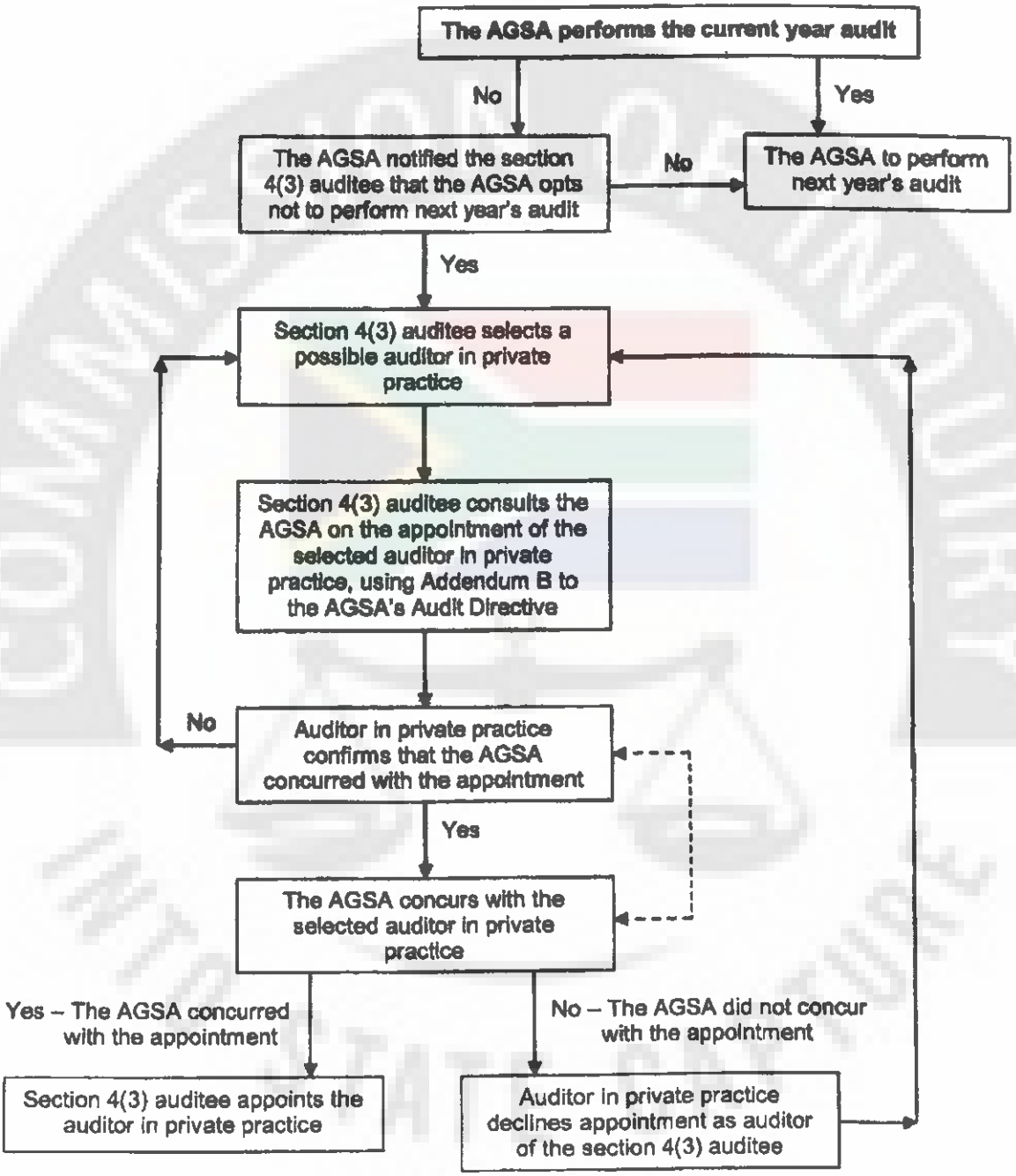
[redacted] Mbiontlo
GROUP FINANCIAL DIRECTOR

cc: Mr Riaz Saloojee — Group Chief Executive Officer — Denel
Ms Elizabeth Africa — Company Secretary — Denel
Dr DC Brouwer — Chairman — Denel Audit and Risk Committee

[redacted]

ADDENDUM B: CONSULTATION OF THE AUDITOR-GENERAL ON THE APPOINTMENT OR DISCHARGE OF AN AUDITOR IN PUBLIC PRACTICE IN TERMS OF SECTIONS 25 AND 26 OF THE PUBLIC AUDIT ACT, 2004 (ACT NO. 25 OF 2004)

SCHEMATIC ILLUSTRATION OF THE AUDITOR APPOINTMENT PROCESS



INSTRUCTIONS TO ENTITY

1. This checklist should be completed and submitted with supporting documentation to the AGSA business executive responsible for the audit of the portfolio of the relevant executive authority.
2. The checklist should be accompanied by a copy of your policy on the appointment of auditors and the allocation of non-audit services to auditors.

INFORMATION REQUIRED

3. Particulars of entity:

	Denel SOC Ltd
	PO Box 8322, Centurion, 0046
	Denel Corporate Office, Irene Campus, Nellmapius Drive, Irene, Pretoria
	012 – 671 2833
	012 – 671 2791 (GFD - Fikile Mhlontlo)
	fikilem@denel.co.za
	Martie Janse van Rensburg
	082 567 5430
	Lynne Brown
	012 - 431 1000
	Department of Public Enterprises
	Orcilla Ruthnam
	2014 and 2015
	2
	n/a

DISCHARGE OF AUDITOR

4. Name of the audit firm discharged:

n/a

5. Number of years engaged on the audit to date:

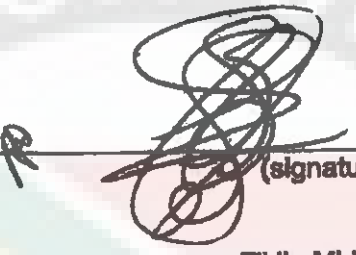
n/a

6. Provide the notice to the auditor, giving the reasons for the impending discharge.

7. Provide written concurrence by the executive authority for the planned discharge.

21. Name of the senior audit manager in charge of audit for the last five years:

	Shephard Moyo
	Shephard Moyo
	Shephard Moyo
	Ghitesh Deva
	Jacques Coetzee

Completed by:  (signature)

Completed by: Fikile Mhlontlo (name)

Designation: Group Financial Director

Date: 24 February 2015

COMMISSION OF INQUIRY INTO STATE CAPTURE

AUDITOR-GENERAL SOUTH AFRICA

Mr Riaz Saloojee
Group Chief Executive Officer
Denel SOC Limited group
PO Box 8322
Centurion
0046

9 March 2015

Reference: Denel/ Sec 4(3)/2015-16

Dear Mr Saloojee

AG Directive (*General Notice 125 of 2015*, issued in *Government Gazette No. 38464* on 11 February 2015)

The purpose of this letter is to inform you of the revision and publication of the new AG Directive (*General Notice 125 of 2015*, issued in *Government Gazette No. 38464* on 11 February 2015). The new AG Directive is effective for financial periods beginning on or after 1 April 2014 and is applicable until further notice. A similar directive will not necessarily be issued annually.

The general purpose of the AG Directive is to clarify the following:

- The nature of the audit functions performed in the public sector
- The standards, criteria and processes applied in performing audits in the public sector
- The responsibilities of auditors in public practice and the manner in which they are required to perform public sector audits.

More specifically, the AG Directive addresses the following:

- Audit functions performed in terms of the Public Audit Act (PAA)
- Audits of public entities and other institutions not performed by the AGSA
- Auditees for which legislation is not prescriptive in respect of the financial statements
- Timing and submission of information for audit purposes
- Assessment and recognition of the financial reporting frameworks applicable in the public sector.

Please take note of paragraph 17 which states that the AGSA opts not to perform the audits of any auditees referred to in section 4(3) of the Public Audit Act (PAA), which are already not audited by the AGSA for the 2015-16 and following financial years, unless advised otherwise by the AGSA prior to the start of the auditees financial year. Therefore we will not be performing the audit of Denel SOC Limited for 2015-16 and you should proceed to appoint an audit firm registered with the Independent Regularity Board for Auditors (IRBA) as stipulated in section 25(1)(b), read with section 25(4) of the PAA.

Please notify me of the suggested appointment, including information on the extent of other services that will be provided during the period of the appointment. In this regard, the document Consultation with the Auditor-General of South Africa on the appointment or discharge of the registered auditor, addendum B, must be completed and sent to me by **30 April 2015**.

The legislative requirements relating to the auditee are also taken into consideration by the AGSA before consent is provided. The AGSA may consult with the responsible executive authority on the appointment of the audit firm.

The previous AG Directive (*General Notice 283 of 2014*, issued in *Government Gazette No. 37505* on 2 April 2014) and TGM 11 of 2014 that provided guidance on the previous AG Directive are hereby withdrawn.

Yours sincerely

Zolisa Zwakala
Business Executive: National E

Enquiries: Rizana Moosa
Telephone: +27 (0) 12 422 9470
Email: RizanaM@agsa.co.za

COMMISSION OF INQUIRY INTO STATE CAPTURE

DENEL SOC LIMITED

Annual General Meeting to be held on	:	23 July 2015
Memorandum Number	:	13
Agenda Item Number	:	14
File Reference	:	

PERFORMANCE OF DIRECTORS

1. PURPOSE

The purpose of this submission is to inform the Shareholder of the following issues concerning the performance of Directors, i.t.o. section 12.1.1.13 of the Memorandum of Incorporation:

- Board evaluation
- Meeting attendance
- Declarations of interest

2. BOARD EVALUATION

A comprehensive Board evaluation was undertaken by the Deloittes': Governance section and reported at the Board meeting on 26 June 2015. A copy of the final evaluation report was provided to the Shareholder.

As the Denel Board effectiveness review is performed every year by an independent consultant, the next review is scheduled to take place in early 2016.

3. MEETING ATTENDANCE

Please refer to Memorandum 14 for the schedule indicating attendance of individual Directors at Board and Board Committee meetings.

4. DECLARATIONS OF INTEREST

Please refer to Memorandum 15 for the declarations of interest of the individual Directors.

5. RESOLUTION REQUIRED

That the Shareholder notes the various aspects of the Directors' performance as addressed above.

EM Africa
GROUP COMPANY SECRETARY

R Salojee
GROUP CHIEF EXECUTIVE OFFICER

Date: 30/06/2015

Deloitte.

Denel State Owned Company Limited

Board Effectiveness Evaluation

Year ending 31 March 2015



June 2015

Deloitte.

Private Bag X6
Gallo Manor 2052
South Africa

Deloitte & Touche
Registered Auditors
Risk Advisory
Building 7
Deloitte Place
The Woodlands
Woodlands Drive
Woodmead Sandton
Docex 10 Johannesburg

Tel: +27 (0)11 806 5000
Fax: +27 (0)11 806 5202
+27 (0)11 209 8507
www.deloitte.com

1 June 2015

Ms Martie van Rensburg
Board Chairperson
Denel SOC Ltd
Private Bag X191
Pretoria
0001

Dear Ms van Rensburg

Denel SOC Ltd: Results of the Board Effectiveness Evaluation, year ending 31 March 2015

1. Introduction

Denel State Owned Company Limited ('Denel SOC Ltd') performs a Board Effectiveness Evaluation annually in accordance with good governance practice as provided by The King Code on Corporate Governance, 2009 (King III Code). The aim of the Board Effectiveness Evaluation is to assess the functioning of the Board and Board Committees as well as identify areas of improvement in order to enhance the oversight bodies.

King III includes the governance principle that "The evaluation of the board, its committees and the individual Directors should be performed every year".

The assessment was performed by an external service provider. For the year ended 31 March 2015 Deloitte & Touche ('Deloitte') was appointed to perform the Denel Board Effectiveness Evaluation. We have recently completed the Board Effectiveness Evaluation for Denel.

This report sets out the results of our review.

National Executive: *LL Bam Chief Executive *AE Swiegers Chief Operating Officer *GM Pinnock Audit
DL Kennedy Risk Advisory *NB Kader Tax TP Pillay Consulting *K Black Clients & Industries
*JK Mazzocco Talent & Transformation *MJ Jarvis Finance *M Jorden Strategy S Gwala Managed Services
*TJ Brown Chairman of the Board *MJ Comber Deputy Chairman of the Board
Regional Leader: MN Alberts

A full list of partners and directors is available on request * Partner and Registered Auditor

B-BBEE rating: Level 2 contributor in terms of the Chartered Accountancy Profession Sector Code

Member of Deloitte Touche Tohmatsu Limited

2. Scope

The scope of the Board Effectiveness Evaluation included an assessment of the Board as a whole and the individual Board committees. In addition, we interviewed a representative sample of Directors to get their individual input and performed a desk review of the governance framework and documents.

The Board Effectiveness Evaluation assessment included the following Board committees:

- Audit and Risk Committee;
- Personnel, Remuneration and Transformation (PRT) Committee; and
- Social and Ethics Committee.

3. Approach

Our approach in the assessment of the Board and the Board Committees included the dissemination and completion of an online assessment questionnaire for each Board and Board Committee members. In addition to the online assessment, Deloitte reviewed supporting documentation as well as conducted individual Director interviews.

The steps taken when performing the assessment were as follows:

- Compiled self-assessment questionnaires which met best practice governance and Board effectiveness requirements, to suit Denel's specific needs;
- Distributed the on-line questionnaires to all Board Directors for their completion;
- Interviewed selected Directors (nine in total);
- Performed a high level documentation review;
- Collated, aggregated and analysed results and developed our conclusions;
- Compiled a draft report;
- Discussed draft report with Chairman, CEO and Company Secretary to confirm our findings and conclusions;
- Presentation of results to the Denel Board meeting on 26 June 2015; and
- Issued finalised report to the Chairman of the Board.

3.1 Interviews

Structured interviews were conducted with selected Board and Committee Directors, to clarify and increase our understanding of questionnaire responses, and overall Board functioning.

The following Directors of the Board and Committees were interviewed:

#	Name	Role
1	Ms MJ Janse van Rensburg*	Chairman of the Board and Director of the Audit and Risk Committee
2	Professor SN Nkomo*	Board Director, Chairman of the Personnel, Remuneration and Transformation Committee and Chairman of the Social and Ethics Committee
3	Doctor G Cruywagen*	Board Director, Chairman of the Audit and Risk Committee and Director of the Social and Ethics Committee
4	Mr M Ratshimbilani*	Board Director and Director of the Personnel, Remuneration and Transformation Committee
5	Ms Z Mathenjwa*	Board Director and Director of the Audit and Risk Committee
6	Mr N Motseki*	Board Director
7	Mr R Saloojee	Group Chief Executive Officer (Executive Director)
8	Mr F Mhlontlo	Group Financial Director (Executive Director)
9	Ms N Davies	Group Executive: Human Resources

* Non-executive Director

3.2 Questionnaires

The online assessment was based on the questionnaires designed by Deloitte to align with the Board and Board Committee terms of references, as well as best practice assessment areas. The assessment was distributed on the 5th and 6th May 2015 and closed on the 26th May 2015. The Board assessment template included the following sections:

- Board size and composition, attributes and culture;
- Charter;
- Agenda and meeting preparation;
- Board meetings;
- Board functioning and processes;
- Board committees;
- Leadership: the role of the chairman;
- Support: the company secretary;
- Board effectiveness and evaluation; and
- Board orientation and development.

With the exception of Mr Motseki, Adv. Badela and Adv. Ntshikila, all Board Directors completed the assessment distributed to them (9 out of 12 completed the questionnaire).

The results of the evaluation questionnaires were collated by Deloitte and have been summarised in *Annexure A*.

The areas of the Board Committees assessment through the questionnaires, were as follows:

- Committee composition attributes and culture;
- Terms of reference and accountability;
- Agenda and meeting preparation Committee meetings;
- Committee functioning and processes;
- Board interaction and accountability; and
- Leadership and support.

All three Directors of the Audit and Risk committee completed the questionnaire. For the Personnel, Remuneration and Transformation Committee 3 of the 5 Directors completed the questionnaire and for the Social and Ethics committee all Directors completed the assessment.

3.3 Documentation review

Included in the Board and Board Committee assessment, was the inspection of key documentation as well as the attendance of the Board and Board committee meetings, provided by the Company Secretary.

Included in the documentation review was the following:

- Board and Board Committee Charters;
- Board and Board Committee work plans;
- Board and Committee packs;
- Board and Committee agendas;
- Board and Committee meeting minutes;
- Board induction, orientation, ongoing development documents (when applicable);
- Strategy session packs;
- Delegation of Authority, Authorities framework;
- Results of the previous Board Assessments;
- Timetable of Board meetings for the year;
- Attendance register – Board and Committee meetings;
- Shareholder Compact;
- Memorandum of Incorporation; and
- Director interest declarations.

4. Statement of Responsibility

We take responsibility for this report which is prepared on the basis of the limitations set out below. The matters raised in this report are only those which came to our attention during the course of our work and are not necessarily a comprehensive statement of all the weaknesses that may exist or all improvements that might be made.

Any recommendations made for improvements should be assessed by you for their full impact before they are implemented.

Effective and timely implementation of our recommendations by the Board and management is important for the maintenance of the reliable governance and internal control system.

This report and the work connected therewith are subject to the terms and conditions of the engagement between Denel and Deloitte. The report is produced solely for the use of Denel for the purpose of the Board Effectiveness Evaluation. Its contents should not be quoted or referred to in whole or in part without our prior written consent. Deloitte & Touche will accept no responsibility to any third party, as the report has not been prepared, and is not intended for any other purpose.

5. Executive summary

The Denel Board is consider to be highly effective both in providing the necessary oversight as well as direction to Denel. This has been confirmed and corroborated through the Board Effectiveness Evaluation. The results of the online assessment were positive and interviews conducted confirmed the sentiment of the effectiveness of the Board and Board Committees.

In general, the responses to an overwhelming majority of the questions indicated that Directors either "agreed" or "strongly agreed" with the assessment statements, with the average scores of the Board and Committee level significantly better than the norm based on other assessments that we have performed.

At the time of our review the Directors' terms had been extended and the Chairman was functioning in an acting capacity. Despite the transitional phase the Board was viewed as continuing to operate in an effective manner and able to discharge its oversight responsibilities.

There is a clear distinction between Board role and authority and management role and authority. The Board are satisfied with the responsiveness and information provided by the executive management team.

The Board of Directors indicated that they see the contribution of Board Committees as effective and valuable. During every Board meeting the Chairperson of the Board Committee will provide a report and meeting minutes are included in the pack for information.

Overall the Directors were highly complementary of the Board Chairman and mentioned that the leadership provided by the Chairman is well regarded.

The Board assessment was complimentary of the support provided by the Company Secretary.

Our assessment has highlighted the positive attributes of the Board and Board Committees. In addition we have included areas for consideration and improvement to enhance the functioning of the Board and Board Committees.

Key areas for consideration

Most Directors believe the Board would benefit from having more skills in the areas of formally qualified financial and auditing skill as well as defence. Some Directors commented that the Board is overweight in legal skill.

Based on our review of the declaration of interest documentation, the individual Director interests are clearly evidenced, however the assessment and declaration of spouse, partner or close family member is not explicit. Even though this may be clear in the practice of declaration, the documentation of the declaration should be improved.

The current Board's term will expire July 2015 and a new Board will be appointed at the AGM in August 2015 by the Minister. The succession of the Board as a whole as well as the Chairman was noted as an area of significant concern. With the reappointment of the Board the uncertainty regarding continuity was raised as a key risk area. The continuity and retention should be considered to retain the current momentum and if possible consideration should be given to retaining a representative sample of the

existing Board to ensure a smooth transition. Common practice is to rotate a third of non-executive Directors on an annual basis. However, we would recommend that at least 1/3rd of the existing Board members be considered for reappointment.

Even though there is no formally documented training programme for directors, training is provided on an ad-hoc basis when the need arises.

The detailed results of the individual questions has been provided in Section two of this report.

6. Previous year's findings

The table below contains certain areas of improvement that were noted during June 2014 assessment as well as the implementation status:

Finding	Status
Poor Board meeting attendance	**Resolved**, during our review and inspection of the documentation we noted that the attendance to the meetings was satisfactory. Board meetings were held on 26 June 2014, 10 Sep 2014, 19 Nov 2014 and 11 Feb 2015. Only 3 apologies were received for the meeting held on 26 June 2014 and one apology for the meeting held on 19 Nov 2014.
Conflict of Interest	**Resolved**, No conflicts of interest were noted during the interviews, analysis of the questionnaires and the document review process.
Ongoing learning and development	**Partially Resolved**, we noted that there is no formal documented plan for the ongoing learning and development for Board Directors.

The matters above, as well as additional matters, are dealt with more fully in the remainder of this report.

We would like to thank the Board Directors and the Company Secretary for their participation in and open contribution to this assessment, and the support and assistance we have received.

Should you require further information regarding this report or the work performed, please contact Mark Victor, on 082 772 3003 or Claire Hoy, on 083 410 2139.

Yours sincerely,



Mark Victor
Director
Risk Advisory
Deloitte & Touche

7. Section A: Summary of results

The table below summarises the strengths and areas of improvement noticed through the response of the questionnaires, as well as an analysis of the questionnaires and interviews conducted.

Legend:

[illegible]	Strongly Agree
1.6 – 2.5	Agree
2.6 – 3.5	Not sure
3.6 – 4.5	Disagree
[illegible]	Strongly disagree

7.1 The Board

Assessment Area	Average score
Part 1: Board Composition, Attributes and Culture	1.67
Part 2: Board Charters: Terms of Reference	1.56
Part 3: Agenda And Meeting Preparation	[illegible]
Part 4: Board Meetings	[illegible]
Part 5: Board Functioning And Processes	1.53
Part 6: Board Committees	[illegible]
Part 7: Leadership And Support	[illegible]
Part 8: Board Effectiveness And Evaluation	1.68
Part 9: Board Orientation And Development	1.67

Board composition, size and diversity

The majority of the Board Directors confirmed that the size and diversity of the Board was optimal and enabled the Board to operate as a cohesive unit. The collective skills set of the existing Board was assessed as complimentary. The Directors are comfortable with the balance between executive, non – executive and independent Directors. Based on the interviews conducted as well as the online assessment it is evident that the Board's culture is strong and enables the effectiveness of the governance structure.

Most Directors believe the Board would benefit from having more skills in the areas of formally qualified financial and auditing and defence. Some Directors commented that the Board is overweight in legal skill. One Director commented that the gender equality could be improved.

Terms of reference

The majority of the Board Directors believe that the Board terms of reference and responsibilities are clear and understood by all. The Board has a detailed work plan for the year that has been aligned to the roles and responsibilities per the Board charter. The charter is reviewed and approved annually by the Board.

Our documentation review identified one misalignment between the Memorandum of Incorporation and the Board charter relating to the minimum number of Directors. The charter indicates two Directors as minimum number whereas the MOI indicates three. This should be rectified.

Board meetings, agenda and meeting preparation

The Directors are satisfied with the ability to influence and inform the Board meeting agenda. The majority of the Directors believe that the agenda is appropriately structure to allow for sufficient time to discuss the important matters. The agenda is developed based on the Board approved work plan for the year.

The Chairman offers members the opportunity to include items of interest that may not be on the prepared agenda. Important matters, as indicated by Board members receive due consideration and may be prioritised where this is deemed necessary. Three Directors commented that the agenda is not ordered with sufficient time to discuss complex and critical issue.

On the whole the board packs are received timeously, allowing sufficient time to prepare diligently for board meeting. Denel has migrated to electronic documentation distribution through the use of IPad's.

Overall the Directors are complimentary of the Board sessions. In general the Directors believe that the Board operates as a cohesive unit, however two members commented that certain items are debated and discussed for too long a period, impacting on this cohesiveness.

Declaration of interest

All Directors have either 'strongly agreed' or 'agreed' to the assessment of the Directors' assessment and confidence in the highest ethical standards being applied in Board deliberations and decisions taken.

The Board charter states that 'any Directors shall disclose his/her direct or indirect personal or private business interest or that of any spouse, partner or close family member in any matter before the Board and withdraw from the proceedings of the Board when such matter is considered.' Based on our review of the declaration of interest documentation, the individual Director interests are clearly evidence however the assessment and declaration of spouse, partner or close family member is not. Even though this may be explicit in the practice of declaration, the documentation of the declaration should be improved. King III describes an independent non-executive Director as a Director free from any business or other relationship which could be seen by an objective outsider to interfere materially with the individual's capacity to act in an independent manner. The detailed declaration for independent Directors is particularly important.

Board functioning and processes

Directors have a good understanding of the key business issues facing Denel.

The Boards' direction and guidance, as well as oversight include both strategic matters and current operating results and performance. Based on the assessment results some Directors believe that the in-year process relating to strategic planning and monitoring could be improved. The strategic monitoring and feedback to the Board is included in the CEO report.

Board committees

The Board has the appropriate committees to assist the Board in fulfilling its mandate and which have:

- Appropriate leadership and composition;
- Clear terms of reference and responsibilities;
- In the opinion of Executive and Non-executive Directors, have fulfilled their mandates; and
- Reported appropriately to the Board on their deliberations and decisions.

The Directors are comfortable with the level of feedback received by the Board relating to the matters dealt with at a committee level. Denel has enhanced the transparency of the committee meetings by providing the minutes of the meetings in the Board packs with the Committee Chairman's reports.

Some Directors have raised comments relating to the potential duplication of areas within the SEC, PRT and Audit and Risk Committee. The mandates of the Committees may need to be communicated to the Board as a whole as well as confirmation that certain topics or areas may require the various Committee attention as the conversation and focus would be different. The company Secretary has developed a clear RACI matrix and continued communication of the roles should be maintained.

Based on best practice we recommend a commonality in membership across these committees to ensure the common tread is communicated and shared within the committees. This is an area that the Denel Board Committees have achieved.

Leadership: the role of the chairman

Overall the Directors were highly complementary of the Board Chairman and mentioned that the leadership provided by the Chairman is well regarded. The Chairman facilitates open debate and discussions at the meetings and the meetings are viewed as efficient and effectively led. The Chairman was viewed as available and accessible to all Directors.

Succession Planning

King III recommends that a programme ensuring a staggered rotation of non-executive Directors should be put in place by the board to the extent that it is not already regulated by the company's memorandum of incorporation or relevant regulation. Rotation of board members should be structured so as to retain valuable skills, maintain continuity of knowledge and experience and introduce people with new ideas and expertise. In addition King III recommends that 'At least one-third of non-executive Directors should retire by rotation yearly, usually at the company's AGM or other general meetings, unless otherwise prescribed through any applicable legislation'.

The current Board Director's term will expire July 2015 and a new Board will be appointed at the AGM in Aug 2015 by the Minister. This was a concern to most Directors, because a new Board might not be able to maintain the momentum of the current Board, and may not be in the best interest of Denel.

The GCEO term will expire January 2017, which was a concern to Directors because the strategic plans developed by the GCEO will not be completed by the current GCEO due to the timing of the contracts.

Company secretarial support

The Directors' assessed the Company Secretary as performing well and adequately supporting the Board as well as the individual Directors. Through inspection of documentation we confirmed that the Company Secretary has maintained the Board and Committee charters up to date, considered training needs of Directors and maintained an induction programme for new Directors.

Board effectiveness and evaluation

The Directors assessed the collective understanding and performance of the Board as effective. The Board is comfortable that the recommendations emanating from previous Board effectiveness assessments have been implemented.

Board orientation and development

A Board continuing development programme is in place that focuses on improving and keeping the Board up to date with governance, regulatory and operation developments.

There is currently no formal training and development plan for Directors. Training is provided on an ad hoc basis when the need arises.

7.2 Audit and Risk Committee

Assessment Area	Average score
Part 1: Committee Composition, Attributes And Culture	
Part 2: Terms Of Reference And Accountability	
Part3: Agenda And Meeting Preparation	
Part 4: Audit And Risk Committee Meetings	
Part 5: Committee Functioning And Processes	
Part 6: Board Interaction And Accountability	
Part 7: Leadership And Support	

Overall it was noted that the Audit and Risk committee functions very well. The functioning of the Committee as a cohesive unit, its productivity and contribution to the Board and the company as a whole received good ratings.

It was noted that the Committee has a good relationship with both the internal and external auditors, and that they value their input.

Risk is a standing item on the agenda and Directors indicated that enough time is spent on audit, non-audit and risk matters. IT governance is also an item on the Committee work plan and will be on the agenda at least once per annum.

It was noted through our interviews that the meetings may be attended by too many people. However, it was confirmed that all invitees attending the meetings make relevant input as required.

We also noted that there is only one person on the Audit and Risk committee who has a formal financial qualification. Although the other Directors are financially astute and apply good financial judgement, this concern was raised during our interviews with Directors. It was also noted that no second opinion is obtained with regards to accounting or auditing matters. It would be beneficial to the committee to appoint an additional member with a formal financial qualification.

The Chairperson of the Board is also a member of the Audit and Risk committee because of her financial background. We do not view this as an independence issue.

7.3 Personnel, Remuneration and Transformation Committee

Assessment Area	Average score
Part 1: Committee Composition, Attributes And Culture	
Part 2: Terms Of Reference And Accountability	
Part3: Agenda And Meeting Preparation	
Part 4: Committee Meetings	
Part 5: Committee Functioning And Processes	
Part 6: Board Interaction And Accountability	
Part 7: Leadership And Support	

Overall the results of the Personnel, Remuneration and Transformation Committee were complimentary. Three of the five members completed the online assessment and the Chairman of the Committee was interviewed.

Based on the results of the assessment the Committee has focused on monitoring and evaluating the implementation of policies aimed at achieving the company's transformation vision, values and objectives.

The assessment highlighted the calibre of the Chairman of the PRT. The Directors were complimentary of the experience provided by the Chairman as well as the necessary guidance and leadership.

Through our interviews we understand that substantial effort has been put in place to ensure executive succession planning through initiatives such as the creation of deputy executive positions. The Committee has operated in a manner to establish the mechanisms and positioning for the future of Denel and to ensure achievement of the Shareholder compact.

INQUIRY INTO STATE CAPTURE

7.4 Social and Ethics Committee

Assessment Area	Average score
Part 1: Committee Composition, Attributes And Culture	
Part 2: Terms Of Reference And Accountability	
Part3: Agenda And Meeting Preparation	
Part 4: Social And Ethics Committee Meetings	
Part 5: Committee Functioning And Processes	2.00
Part 6: Board Interaction And Accountability	1.67
Part 7: Leadership And Support	

Overall the assessment results of the Social and Ethics Committee were positive and the areas of Leadership and support were assessed as performing very positively.

The Committee assessment was completed by all three members. The assessment indicates a committee that is functioning well and has achieved its mandate. The Chairman received complimentary feedback in providing effective leadership.

Based on our interviews conducted the Committee has become more effective in embedding its roles and responsibilities and deepening the social and ethical impact of the Denel within the broader environment. The Committee has engaged with organisations such as the Ethics Institute of South African to ensure the breadth of ethical performance is understood and the role of the Committee effective.

The composition of the SEC includes the Chairperson of the PRT as well as the Chairperson of the Audit and Risk Committee. This strengthens the collaboration and understanding of the issues dealt with within these committees. Some members feel that there is possibly duplication in the Committee processes however as mentioned by the Chairpersons the nature of the conversation would be different.

The Committee workplan details the responsibilities of stakeholder engagement, enterprise development, ethics management and transformation.

7.5 Director and Chairperson Assessment

Assessment Area	Average score
Part1: Knowledge And Skills	
Part 2: Execution Of Duties	
Part 3: Chairman's Assessment	

Through the questionnaires and interviews conducted it was noted that Directors understands the roles, responsibilities, duties, legal obligations and objectives. Directors acts in good faith, ethically and legally in the best interest of Denel.

We noted during our document review that independence is declared before every meeting. However, the independence of family members is not declared. This should be considered to ensure Directors always act in the best interest of Denel.

The Chairperson's leadership is well regarded and highly rated by all Directors. She provides strong leadership without limiting the collective responsibility of Board decisions. Directors assessed the Chairperson as available and accessible at all times. The Chairperson plays an active role in planning the agenda and motivate Directors to participate in the debate and collaborations during Board meetings.

The assessment highlighted certain areas that are not within the direct control of the Chairperson and are mandated by the DPE and the Minister. This resulted in certain assessment areas being rated as 'not sure'.

In addition the Directors commented that there has no instance requiring the Chairman to take a lead role in removing non-performing or unsuitable Directors from the Board.

One Director rated the Chairman assessment as 'not sure' due to the fact that the Denel Board had two Chairman during the period making the assessment difficult to complete.

7.6 Executive Director Assessment

Assessment Area	Average score
Part 1: Executive Director Assessment	

The questionnaires indicated that the executive Directors provide sufficient additional information, insight and clarification into issues, to ensure appropriate understanding of the matter to support effective decision making.

Overall the Board Directors are comfortable that the executive Directors proactively and transparently table issues and developments at the Board to ensure that the Board and all individual Directors can effectively discharge their accountability.

The executive Directors also successfully transition from being executive and line manager to being a Director of Denel.

COMMISSION OF INQUIRY INTO STATE CAPTURE

8. Section B: Detailed results

The table below details the results as per the questionnaires completed by Directors.

Average score legend:

	Strongly Agree
	Agree
2.6 – 3.5	Not sure
3.6 – 4.5	Disagree
	Strongly disagree

Assessment legend:

	Strongly Agree
2	Agree
3	Not sure
4	Disagree
5	Strongly disagree

8.1 The Board

The Board assessment was sent to 12 Directors and 9 responses were received.

Part 1: Board Composition, Attributes & Culture	M1	M2	M3	M4	M5	M6	M7	M8	M9	Average
01. Is the composition of this board appropriate in terms of relevant skills, knowledge, experience and qualifications?	2	2	2		2	4	2	2		2.00
02. Is the composition of this board appropriate in terms of diversity and representivity?	2	2				2	3	2		1.67
03. Does the board have an appropriate balance of executive and non-executive membership and input?		2			2					1.22
04. Do all Directors, particularly non-executive Directors, have the time and capacity required to devote properly to their obligations?		2	2		2	4	2	2	2	2.00

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	M1	M2	M3	M4	M5	M6	M7	M8	M9	Average
05. In addition to the board papers, do the executive Directors provide sufficient additional information, insight and clarification into issues facing the board, to ensure appropriate understanding of matters to support effective decision making?	2		2	2			2		1	1.44
06. Do the Board and particularly the non-execs have access to other executives and is there appropriate attendance and involvement from other executives at Board meetings?	2	2		2		2	2	2	1	1.67
Part 2: Board Charters: Terms Of Reference										
07. Is the Board charter clear in terms of duties, roles and responsibilities of the Board?	2		2	2			2	2	1	1.56
08. Does the charter cover all the appropriate areas?	2	2	2	2			2	1	1	1.56
09. Has the board complied with and fulfilled its charter?	2	2		2	2		2	1	1	1.56
10. Has the board reviewed and complied with Denel's approval framework, authorisation framework, delegation of authorities, etc.?	2	2	2	2			2	1	1	1.56
Part 3: Agenda And Meeting Preparation										
11. Does the agenda preparation ensure that the board can discharge its responsibilities as per their charter?	2	2		2			2	1	1	1.44
12. Does the agenda setting process allow for appropriate issues to be raised as necessary?	2	2		2			2	1	1	1.44
13. Can and do board members influence the content of the agenda?		2		2			3	2	1	1.56
14. Is the agenda ordered with sufficient time to discuss complex and critical issues?		2		2	2	2	3	1	1	1.67
15. Is it clear from the agenda when decisions are required from the board?		2						1	1	1.11
16. Are the papers received to support agenda items of a high quality i.e. providing the right level of information, in a clear and concise manner?		2					2	2	1	1.33

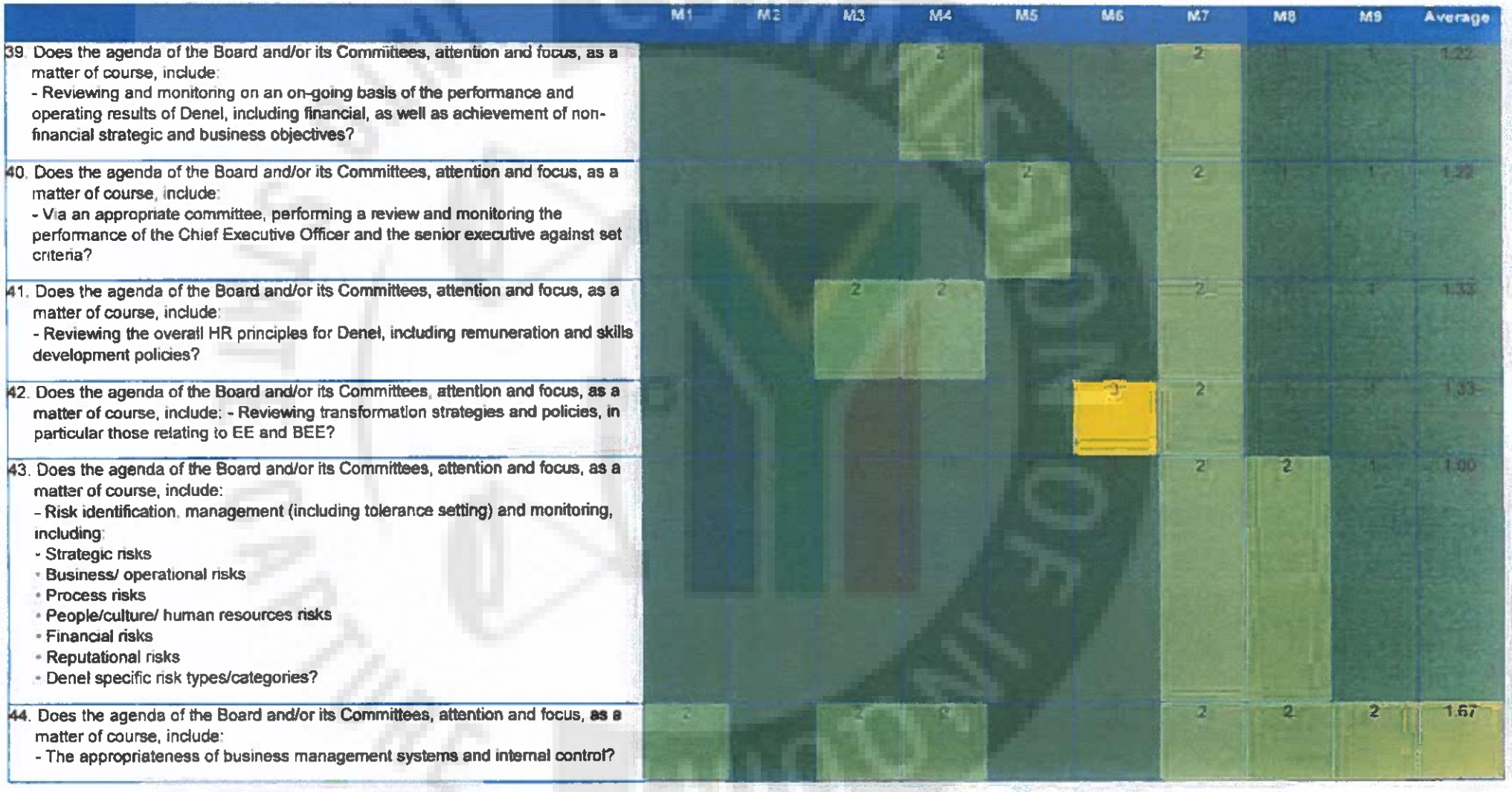
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	M1	M2	M3	M4	M5	M6	M7	M8	M9	Average
17. Do Directors receive the board pack timeously, allowing sufficient time to prepare diligently for board meetings?		2		2			3	2	1	1.56
Part 4: Board Meetings										
18. Is sufficient time scheduled for each board meeting to deal with all agenda items?		2		2			2	1	2	1.89
19. Does the board meet often enough (i.e. at least four times a year) to effectively fulfil its responsibility in terms of its charter?		2	2			2	2	1	1	1.44
20. Are board meetings productive?		2					2	1	1	1.22
21. Does the board work as a cohesive unit?		2			2	2	2	2	2	1.67
22. Are Directors confident that the highest ethical standards are applied in board deliberations and decisions?		2		2	2		3	1	2	1.67
23. Is management responsive to the board's views and recommendations?		2	2	2	2		2	2	2	1.78
24. Has the board acted in the best interests of the company and the "shareholder" throughout the year?		2					2	1	1	1.00
Part 5: Board Functioning And Processes										
25. Does the Board review recommendations for non-executive Director remuneration relative to appropriate benchmarks as recommended by the Remuneration Committee?	2	2	4		4	3	2	1	4	2.56
26. Does the Board through the audit committee consider IT governance requirements and oversee critical IT decisions made?	2	2	2	2			2	2	2	2.22
27. Does the board devote sufficient time respectively to strategic direction, planning and monitoring i.e. to forward looking issues, as well as to current performance and operational issues?		2	2		4	2	2	1	1	1.78
28. Does the executive team develop and propose the strategic direction and the strategy of Denel to the board, with due consideration of challenges, opportunities and alternative options, for the board's consideration, review, input and approval?					2		2	1	1	1.22

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	M1	M2	M3	M4	M5	M6	M7	M8	M9	Average
29. Do the Board and/or its Committees consideration and monitoring include the top three or four key strategic or business issues currently relevant to and facing Denel?		2	2	2			2	1	2	1.56
30. Does the board, as a whole, spend sufficient time considering these key current issues?	2	2	2	2	2	2	2	1	2	1.67
31. Does the board receive appropriate and the correct level of information relating to these key current issues?	2	2	1	2	2	1	2	1	1	1.33
32. Are the annual and interim results and annual/integrated report considered by the Board and publicly reported in a timely manner in accordance with statutory and regulatory requirements after due consideration to the group's position as a going concern and its financial position in the year ahead?	1	1	1	2	1	1	2	2	1	1.33
33. Does the agenda of the Board and/or its Committees, attention and focus, as a matter of course, include; - Reviewing the overall HR principles for Denel, including remuneration and skills development policies?	1	1	2	2	1	1	2	1	1	1.33
34. Does the Board ensure that internal control procedures, technology issues and sustainability programs are addressed regularly and assessed by the Audit and Risk Committee of the Board?	2	1	1	1	2	1	2	2	2	1.56
35. Does the Board through the audit committee review the code of conduct and ethics performance to facilitate the adherence to these?	2	1	2	3	1	1	3	2	2	1.89
36. Does the Board review recommendations for executive and non-executive Director remuneration relative to appropriate benchmarks as recommended by the Remuneration Committee?	1	2	4	1	2	1	2	2	4	2.11
37. Does the Board through the audit committee consider IT governance requirements and oversee critical IT decisions made?	2	2	2	2	1	1	2	2	2	1.56
38. Does the agenda of the Board and/or its Committees, attention and focus, as a matter of course, include: - Consideration and approval of the medium and long term strategy and direction of Denel?	2	2	2	1	1	1	2	1	1	1.44

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	M1	M2	M3	M4	M5	M6	M7	M8	M9	Average
39. Does the agenda of the Board and/or its Committees, attention and focus, as a matter of course, include: - Reviewing and monitoring on an on-going basis of the performance and operating results of Denel, including financial, as well as achievement of non-financial strategic and business objectives?				2			2			
40. Does the agenda of the Board and/or its Committees, attention and focus, as a matter of course, include: - Via an appropriate committee, performing a review and monitoring the performance of the Chief Executive Officer and the senior executive against set criteria?					2		2			
41. Does the agenda of the Board and/or its Committees, attention and focus, as a matter of course, include: - Reviewing the overall HR principles for Denel, including remuneration and skills development policies?			2	2			2			
42. Does the agenda of the Board and/or its Committees, attention and focus, as a matter of course, include: - Reviewing transformation strategies and policies, in particular those relating to EE and BEE?						3	2			
43. Does the agenda of the Board and/or its Committees, attention and focus, as a matter of course, include: - Risk identification, management (including tolerance setting) and monitoring, including: • Strategic risks • Business/ operational risks • Process risks • People/culture/ human resources risks • Financial risks • Reputational risks • Denel specific risk types/categories?							2	2		
44. Does the agenda of the Board and/or its Committees, attention and focus, as a matter of course, include: - The appropriateness of business management systems and internal control?	2		2	2			2	2	2	1.67

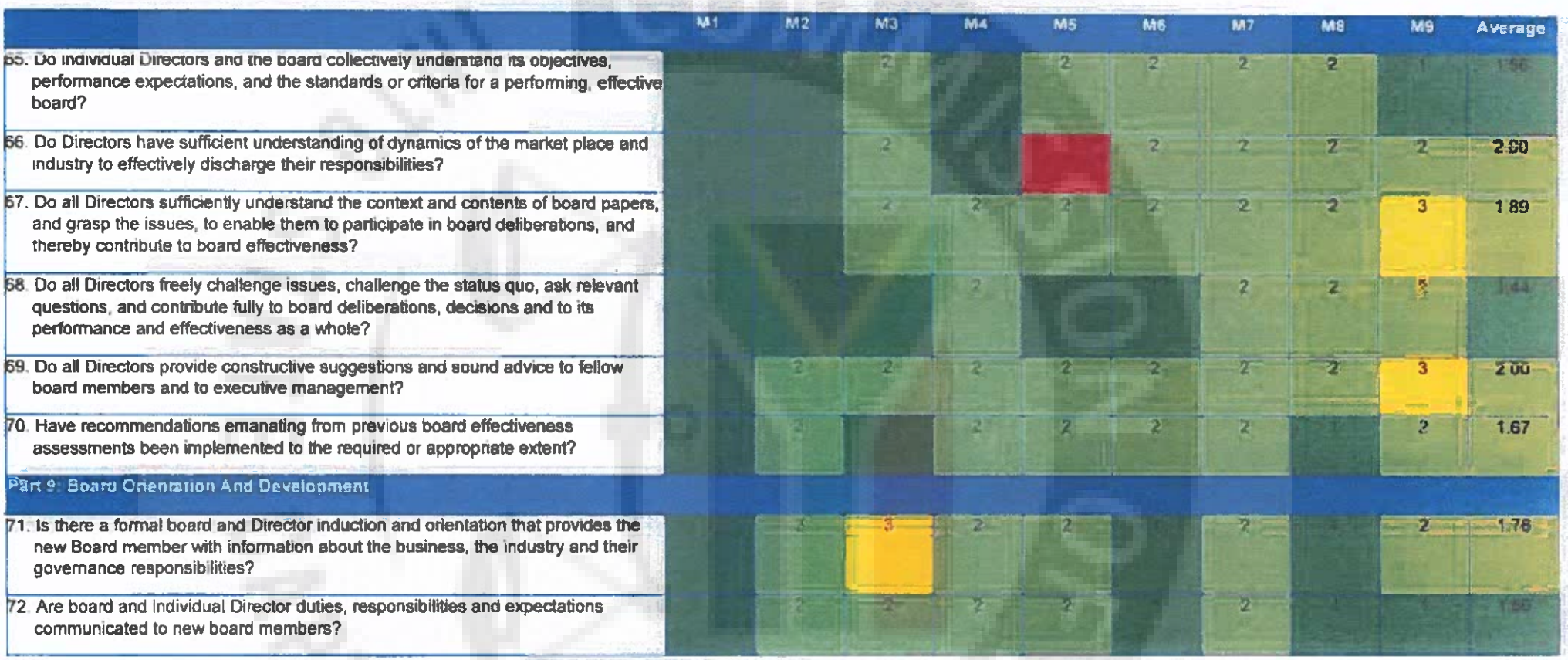
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	M1	M2	M3	M4	M5	M6	M7	M8	M9	Average
45. Does the agenda of the Board and/or its Committees, attention and focus, as a matter of course, include: - Shareholder relationship and communication?	2			2			2	2	1	1.44
46. Does the agenda of the Board and/or its Committees, attention and focus, as a matter of course, include: - Effective, open and transparent, communication of relevant issues with both internal and external stakeholders?					2		2	2	1	1.33
47. Does the agenda of the Board and/or its Committees, attention and focus, as a matter of course, include: - Compliance with applicable laws, regulations, codes of best practice etc. including corporate governance?				2			2	2	1	1.00
48. Does the agenda of the Board and/or its Committees, attention and focus, as a matter of course, include: - Via an appropriate committee, executive management succession, board and chairman succession?	2			2	2		3	2	1	1.67
49. Does the agenda of the Board and/or its Committees, attention and focus, as a matter of course, include: - Appropriateness of, monitoring of and adherence to the values and code of ethics/ conduct of Denel?	2		2	2			2		2	1.33
50. Does the agenda of the Board and/or its Committees, attention and focus, as a matter of course, include: - Corporate citizenship and sustainability responsibilities of Denel?	2			2		3	2	2	1	1.56
51. Does the agenda of the Board and/or its Committees, attention and focus, as a matter of course, include: - Bringing to the attention of the Board any declarations of opinion or responses to be provided to regulatory authorities before inclusion in any documents?	2		2	2	2		2	2	1	1.67
52. Does the agenda of the Board and/or its Committees, attention and focus, as a matter of course, include: - If the Board is unable to comply with any of the responsibilities determined by the Public Finance Management Act, it shall promptly report the inability, together with reason to the Shareholders and National Treasury.	2			2			2	2	1	1.44
53. Does the Board define levels of materiality, reserving specific powers to itself and delegating matters with the necessary written authority to management?	2			2	1	1	2	2	1	1.44

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Part 6: Board Committees	M1	M2	M3	M4	M5	M6	M7	M8	M9	Average
54. Does the board have sufficient and appropriate committees to focus on and deal with specific issues on its behalf?	2						2	1	1	1.22
55. Does each board committee have a clear mandate, charter and/or terms of reference?	2						3	1	2	1.22
56. Does each committee Chairperson report appropriately to the board on the activities, deliberations and decisions/ recommendations of each committee?	3						2	2	1	1.44
57. Are Directors, and the board as a whole, satisfied with the effectiveness and contribution of each of its committees? Are all committees well regarded by the board?	2						2	2	2	1.44
Part 7: Leadership And Support										
58. Is the board leadership distinct from management; is there a clear distinction between board role and authority, and management role and authority?	2						2	2	1	1.33
59. Is the board chairman available and accessible to Directors?	2			2			2	2	1	1.44
60. Are meetings run efficiently and effectively?		2			2		2	1	1	1.33
61. Are board meetings conducted in a manner that encourages open discussion, healthy debate, and allows each board member to add value clearly to discussions and decisions?					2		2	1	1	1.22
62. Do Directors feel supported and appropriately recognised for their contribution by the chairman and by other members of the board?	2	2		2	2		2	2	2	1.78
63. Is the Group secretary available and accessible, and does he/she effectively support the board in governance and procedural matters?	2						2	1	1	1.22
Part 8: Board Effectiveness And Evaluation										
64. Are annual board, board committee and Director effectiveness assessments performed?							2	1	2	1.22

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	M1	M2	M3	M4	M5	M6	M7	M8	M9	Average
65. Do individual Directors and the board collectively understand its objectives, performance expectations, and the standards or criteria for a performing, effective board?			2		2	2	2	2	1	1.56
66. Do Directors have sufficient understanding of dynamics of the market place and industry to effectively discharge their responsibilities?			2			2	2	2	2	2.00
67. Do all Directors sufficiently understand the context and contents of board papers, and grasp the issues, to enable them to participate in board deliberations, and thereby contribute to board effectiveness?			2	2	2	2	2	2	3	1.89
68. Do all Directors freely challenge issues, challenge the status quo, ask relevant questions, and contribute fully to board deliberations, decisions and to its performance and effectiveness as a whole?				2			2	2	2	1.44
69. Do all Directors provide constructive suggestions and sound advice to fellow board members and to executive management?		2	2	2	2	2	2	2	3	2.00
70. Have recommendations emanating from previous board effectiveness assessments been implemented to the required or appropriate extent?		2		2	2	2	2	1	2	1.67
Part 9: Board Orientation And Development										
71. Is there a formal board and Director induction and orientation that provides the new Board member with information about the business, the industry and their governance responsibilities?		2	3	2	2		2	1	2	1.78
72. Are board and individual Director duties, responsibilities and expectations communicated to new board members?		2	2	2	2		2	1	1	1.56

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8.2 Audit and Risk Committee

All 3 members of the audit and risk committee completed the assessment.

	M1	M2	M3	Average
Part 1: Committee Composition, Attributes And Culture				
01. Is the Audit and Risk Committee (hereafter referred to as "the Committee") size in line with King III, your Charter and the Companies Act?	1	1	1	1.00
02. Is the composition of the Committee appropriate in terms of experience and qualifications of the members as required by legislation?	2	4	1	2.33
03. Is there appropriate attendance and involvement in the meetings from: • Executive management • External Audit/Internal Audit • Risk Management / Officer	1	1	1	1.00
04. Does the Committee foster an open, co-operative relationship with management, external audit and internal audit?	1	1	1	1.00
05. Is management responsive to the Committee's views and recommendations?	1	1	1	1.00
06. Are all the members of the audit committee independent non-executive Directors, and not the Chairman of the Board?	4	4	1	3.00
Part 2: Terms Of Reference And Accountability				
07. Are the terms of reference relating to the Committee clear?	1	1	1	1.00
08. Do the terms of reference cover all the appropriate areas in terms of the Companies Act and King III requirements?	1	1	1	1.00
09. Does the Committee review its Terms of Reference annually, or as needed, and determine whether its responsibilities are adequately described, including: • Compliance with new laws or legal developments • Corporate governance requirements and developments • Industry developments and/or regulations • Balance between "Audit Committee" and "Risk Committee" responsibilities, dealing fully and adequately with both • Accounting and auditing requirements, changes etc. (IFRS) • Monitor compliance with the company's code of conduct	1	1	1	1.00
Part3: Agenda And Meeting Preparation				
11. Does the chairman of the Committee participate in the agreeing / approving of the agenda?	1	1	1	1.00

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	M1	M2	M3	Average
12. Do the agenda and its preparation ensure that the Committee can discharge its responsibilities as per the terms of reference?				
13. Does the agenda setting process allow for appropriate issues to be raised as necessary?				
14. Can and do members influence the content of the agenda?				
15. Is the agenda ordered with sufficient time to discuss complex and critical issues?				
16. Is it clear from the agenda when decisions/ recommendations are required from the Committee?				
17. Are the papers received to support agenda items of a high quality, providing the right level of information, in a clear and concise manner?				
18. Do you receive the pack timeously, allowing sufficient preparation time?		2		
Part 4: Audit And Risk Committee Meetings				
18. Is sufficient time scheduled for the meetings?				
19. Does the Committee meet often enough to effectively fulfil its responsibility?	2			
20. Are the Committee meetings productive?				
21. Does the Committee work as a cohesive unit?				
22. Are you confident that the highest ethical standards are applied in the Committee deliberations and decisions/ recommendations?				
23. Has the Committee acted in the best interests of the company and the shareholder throughout the year?				
24. Does the Committee meet with internal and external auditors at least once a year without management being present?				
Part 5: Committee Functioning And Processes				
25. Has the Committee complied with and fulfilled its terms of reference?				
26. Does the Committee enquire from the external auditors and management regarding the quality, experience and sufficiency of staff in finance and external audit?				
27. Does the Committee have explicit authority to investigate matters within its powers, as identified in the terms of reference?				

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	M1	M2	M3	Average
28. Does the committee have adequate resources to investigate such matters and does the committee have full access to information?				
29. Does the committee review and approve of all non-audit services provided by internal and external audit?				
30. Does the Committee review the management reports written by the external auditors to ensure that all significant matters raised are properly addressed?				
31. Has the Committee considered their role in overseeing integrated reporting?				
32. Has the Committee ensured the adequacy of procedures for review of corporate disclosures and compliance in terms of the Public Finance Management Act, Company's Act, International Financial Reporting Standards and any other applicable legislation?				
33. Is the Committee permitted to consult with specialists or consultants (subject to a board-approved process)?				
34. Are relationships between external assurance providers and the organization monitored by the Committee?	2			
35. Does the Committee review and oversee compliance with accounting and auditing policies, standards and practices, including reporting?				
36. Does the Committee review quarterly management accounts?	2	2		1.67
37. Does the Committee review significant transactions prepared in accordance with Denel's Delegation of Authority?				
38. Does the Committee have a process for the review of significant issues, if any, with management and the external auditors prior to finalization of the interim and annual financial statements?				
39. Are the possible/suggested adjustments to the financial statements that resulted from the audit process, whether processed or not, reviewed by the Committee?				
40. Are the Committee consulted when circumstances arise that result in management seeking a second opinion on accounting or auditing matters?	3	3		2.33
41. Does the Committee's annual review of the external auditor include the following: • independence • performance • appointment • fees • relationship				
42. Is the committee considering assurance required over sustainability information reported in the annual/integrated report		2		
43. Does the Committee approve the Risk Management Strategy, Policy and Plan?				
44. Does the Committee understand and consider the significant risks faced by the company and management's response to these risks?				
45. Does the Committee understand and consider management's process for identifying risks and mitigating these risks?				
46. Does the Committee review and oversee the adequacy and effectiveness of the policies, structures and processes for risk management in the organization?				

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	M1	M2	M3	Average
47 Does the Committee receive sufficient information to review and oversee, understand and assess the organization's systems of risk management and internal control?	1	1	1	1.00
48. Does the Committee receive sufficient information to review and oversee, understand and assess the organization's systems of risk management and internal control?	1	2	1	1.33
49 Does the committee receive a combined assurance matrix at least once per annum and does the committee ensure that the combined assurance model is applied, providing a coordinated approach to all assurance activities?	1	1	1	1.00
50. Is the Committee satisfied that they have sufficient assurance on internal controls to make a statement on internal and financial controls in the integrated report?	1	1	1	1.00
51. Does the Committee understand the review of and the testing of risk management and internal control systems and processes performed by management, the external and internal auditors, to enable them to assess the process of reasonably detecting internal control issues or fraud?	1	1	1	1.00
52 Does the committee focus on the extent to which internal and external auditors review computer systems and applications, the security of such systems and applications and the contingency plan for processing financial information in the event of a system breakdown?	1	1	1	1.00
53. Does the committee assist the Board in carrying out its IT governance responsibilities including: • Ensuring and obtaining assurance that IT risks are adequately addressed • Considering IT risk as it relates to financial reporting and the going concern of the company	1	1	1	1.00
54. Does Internal Audit functionally report to and is it functionally accountable to the Committee?	1	1	1	1.00
55 Does the Committee review and approve the following relating to Internal Audit: • Charter and Terms of reference • Coverage Plan • Staffing • Budget and annual work plan	1	1	1	1.00
56. a. Does the Audit Committee perform an annual assessment of internal audit's effectiveness	1	1	1	1.00
56 b. Does the Audit Committee reviews the results of the quality assurance review from time to time.	2	1	1	1.33
57 Is internal audit providing the Committee with a written assessment of the effectiveness of the governance, risk and control environment, and specifically on internal and financial controls as input into the Committee's statement in the Annual/Integrated Report?	1	1	1	1.00
58 Does the committee ensure that internal audit has: · The support of top management · Sufficient independence to operate under no limitation · Direct access to top management, including the Denel Chief Executive Officer.	1	1	1	1.00

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	M1	M2	M3	Average
59. a. Does the committee: Review all approval for non-audit services in terms of the Denel Policy, this should include reviewing the objectives and scope of the work performed to ensure that there no conflict of interest and that independence is not compromised.	1	1	1	1.00
59. b. Does the committee: Review the audit findings and determine if sufficient and timely action plans are implemented by management to address the major recommendations.	1	1	1	1.00
Part 6: Board Interaction And Accountability				
60. Has the Committee complied with the Board delegation of authority, any decision making process, etc.?	1	1	1	1.00
61. Is the Board well informed about deliberations, conclusions and recommendations of the Committee?	1	1	1	1.00
Part 7: Leadership And Support				
62. Is the Committee chairman available and accessible?	1	1	1	1.00
63. Are meetings run efficiently and effectively?	1	1	1	1.00
64. Are meetings conducted in a manner that encourages open discussion, healthy debate, and allows each Committee member to clearly add value to discussion and decisions?	1	1	1	1.00
65. Do members of this Committee feel supported and appropriately recognised by the Chairman and other Committee members for their contribution?	1	1	1	1.00

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8.3 Personnel, Remuneration and Transformation Committee

The assessment was sent to 5 Directors, of which 3 completed the assessment.

Part 1: Committee Composition, Attributes And Culture	M1	M2	M3	Average
1. Is the composition of the Committee appropriate in terms of relevant experience and qualifications?			1	1.00
2. Is there appropriate attendance and involvement in the meetings from Executive management?			1	1.00
3. Does the Committee foster an open, co-operative relationship with management?			2	1.33
4. Is management responsive to views and recommendations of the Committee?	2		2	1.67
Part 2: Terms Of Reference And Accountability				
5. Are the terms of reference relating to the Committee clear			1	1.00
6. In your view, do the terms of reference cover all the appropriate areas?	2		1	1.33
7. Does the Committee review its Terms of Reference annually, or as needed, and determine whether its responsibilities are adequately described & complete?	2		1	1.33
Part3: Agenda And Meeting Preparation				
08. Do you feel able to prepare diligently for the Personnel, Remuneration and Transformation Committee meetings?			1	1.00
09. Does the agenda setting process allow for appropriate issues to be raised as necessary?	2		1	1.33
10. Can and do members influence the content of the agenda?	2		1	1.33
11. Is the agenda ordered with sufficient time to discuss complex and critical issues?	2		1	1.33
12. Is it clear from the agenda when decisions/ recommendations are required from the Committee?			1	1.00
13. Are the papers received to support agenda items of a high quality, providing the right level of information, in a clear and concise manner?			2	1.33
14. Do you receive the pack timeously, allowing sufficient preparation time?	2		2	1.67
Part 4: Committee Meetings				
15. Is sufficient time scheduled for meetings?			2	1.33
16. Does the Committee meet often enough to effectively fulfil its responsibility?			2	1.33
17. Are the Committee meetings productive?			2	1.33
18. Does the Committee work as a cohesive unit?			2	1.33
19. Are you confident that the highest ethical standards are applied in the Committee deliberations and decisions/ recommendations				1.00
20. Has the Committee acted in the best interests of the company and the shareholder throughout the year?				1.00
Part 5: Committee Functioning And Processes				
21. In your view, has the Committee complied with and fulfilled its terms of reference?			2	1.33
22. a. In performing its duties and responsibilities, does the Committee in terms of remuneration: Consider remuneration policy and ensure that there are strategic objectives for remuneration management within the company's operations.			2	1.33
22. b. In performing its duties and responsibilities, does the Committee in terms of remuneration: Determine and take any action that is reasonably appropriate or necessary in the course of establishing the compensation of the company's executives.			2	1.33

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	M1	M2	M3	Average
22. c. In performing its duties and responsibilities, does the Committee in terms of remuneration: Review and approve corporate goals and objectives relevant to the compensation of the company's Chief Executive Officer, evaluate the performance of the company's Chief Executive Officer in light of these goals and objectives, and set the compensation level of the company's Chief Executive Officer based on this evaluation.			2	1.33
22. d. In performing its duties and responsibilities, does the Committee in terms of remuneration: Review and make recommendations to the Board where necessary, all new employment, consulting, retirement and severance agreements and arrangements proposed for the company's executives. The Committee shall periodically evaluate existing agreements with the company's executives for continuing appropriateness.			2	1.33
22. e. In performing its duties and responsibilities, does the Committee in terms of remuneration: Determine specific remuneration packages for each executive Director and executive officer of the company, including fringe benefits, and to review these annually.	2		2	1.67
22. f. In performing its duties and responsibilities, does the Committee in terms of remuneration: Consider the payment of performance linked non-pensionable bonuses to executive Directors and executive officers of the company, and to set the criteria for, and relative value of such payments.			2	1.33
22. g. In performing its duties and responsibilities, does the Committee in terms of remuneration: Consider other matters relating to the remuneration of or terms of employment applicable to the executive Directors and executive officers that may be referred to the committee by the Board.			2	1.33
23. a. In performing its duties and responsibilities, does the Committee in terms of Transformation: Monitor and evaluate the implementation of policies aimed at achieving the company's transformation vision, values and objectives.	2			1.33
23. b. In performing its duties and responsibilities, does the Committee in terms of Transformation: Review and oversee human resource policies and strategies aimed at creating and sustaining the technical and managerial excellence required to support the attainment of the Government's and the company's global objectives.	2		2	1.67
23. c. In performing its duties and responsibilities, does the Committee in terms of Transformation: Review and give guidance with respect to the human resource policies and strategies aimed specifically at: i. Redressing past inequalities in the South African workplace in the course of creating a competitive workforce which recognises the social profile of South Africa ii. National employment equity plan to consider and address the localisation requirements e.g. demographics, throughout the company in compliance with the applicable legislation.			2	1.33
23. d. In performing its duties and responsibilities, does the Committee in terms of Transformation: Review management's performance as it relates to the implementation of the transformation policy and strategy and to advice on strategies for reward or sanction against performance indices.			2	1.33
23. e. In performing its duties and responsibilities, does the Committee in terms of Transformation: Review the company's performance in the area of human resources development against internal targets, legislative imperatives and the norms applicable to conducting business in other countries.	2		2	1.67
23. f. In performing its duties and responsibilities, does the Committee in terms of Transformation: Consider the implications of external trends; including legislative developments (inter alia the Employment Equity Act).	2		2	1.67
23. g. In performing its duties and responsibilities, does the Committee in terms of Transformation: Consider other matters relating to transformation that may be referred to the Committee by the Board.				1.00

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	M1	M2	M3	Average
23 h. In performing its duties and responsibilities, does the Committee in terms of Transformation: Review and oversee the company's plans and strategies aimed at complying and/or influencing the development of transformation and related legislation that have the potential to negatively impact on the company's rights e.g. Employment Equity Act .	2		2	1.67
23. i. In performing its duties and responsibilities, does the Committee in terms of Transformation: Regularly review and monitor the company's succession plan, transformation plan, training and development plan and report to the Board on the progress thereof, thereby ensuring that the Company addresses issues of employee retention, implements strategies to counteract losses, develop careers and promote mobility in an environment free of discrimination.	2		2	1.67
24. In performing its duties and responsibilities, does the Committee recommend non- executive Directors' fees to the Board in line with SOE remuneration guidelines and also the fees of any Director-related entities providing services to the group.?	2		2	1.67
25. In performing its duties and responsibilities, does the Committee ensure that the relationship between boardroom, executive and employee remuneration remains constant?	2		2	1.67
26. Does the Committee prepare an annual remuneration report explaining the remuneration policies followed and strategic objectives that it seeks to achieve?	3		2	2.00
Part 6: Board Interaction And Accountability				
27. Has the Committee complied with the Board delegation of authority, any decision making process, etc.?			2	1.33
28. Is the Board well informed about deliberations, conclusions and recommendations of the Committee?			2	1.33
29. Is the Committee well regarded by the Board?			2	1.33
Part 7: Leadership And Support				
30. Is the Committee chairman available and accessible?	2		1	1.33
31. Are meetings run efficiently and effectively?			1	1.00
32. Are meetings conducted in a manner that encourages open discussion, healthy debate, and allows each Committee member to clearly add value to discussion and decisions?			1	1.00
33. Do members of this Committee feel supported and appropriately recognised by the Chairman and other Committee members for their contribution?			1	1.00

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8.4 Social and Ethics Committee

All 3 members of the Committee completed the assessment

Part1: Committee Composition, Attributes And Culture	M1	M2	M3	Average
01. Is the Social and Ethics Committee ("the Committee") size and composition in line with the Companies Act and your Charter?		2		
02. Is the composition of the Committee appropriate in terms of experience and qualifications of the members?	2	2	2	2.00
03. Does the Committee foster an open, co-operative relationship with management?				
04. Is management responsive to the Committee's views and recommendations?			2	
Part 2: Terms Of Reference And Accountability				
05. Are the terms of reference relating to the Social and Ethics Committee clear?				
06. Does the Social and Ethics Committee review its Terms of Reference annually, or as needed, and determine whether its responsibilities are adequately described and cover the requirements of the Companies Act including: • Social and economic development; • Responsible and compassionate corporate citizenship; • The environment, health and public safety, including the impact of Denel's activities and of its products or services • Consumer relationships, including Denel's advertising, public relations and compliance with consumer protection laws • Labour and employment.		2	2	1.67
07. Has the Social and Ethics Committee complied with and fulfilled its terms of reference for the year under review?		2		
Part3: Agenda And Meeting Preparation				
08. Does the agenda and its preparation ensure that the Committee can discharge its responsibilities as per the terms of reference?				
09. Do you feel able to prepare diligently for the Social and Ethics Committee meetings?				
10. Does the agenda setting process allow for appropriate issues to be raised as necessary?				
11. Can and do members influence the content of the agenda?		2		
12. Is the agenda ordered with sufficient time to discuss complex and critical issues?		2		
13. Is it clear from the agenda when decisions/ recommendations are required from the Social and Ethics Committee?		2		
14. Are the papers received to support agenda items of a high quality, providing the right level of information, in a clear and concise manner?		2		
15. Do you receive the pack timeously, allowing sufficient time to prepare diligently for Committee meetings?		2		
Part 4: Social And Ethics Committee Meetings				
16. Is sufficient time scheduled for the meetings?		2		
17. Does the Committee meet often enough to effectively fulfil its responsibility?	2	2	2	2.00
18. Are the Committee meetings productive?		2		
19. Does the Committee work as a cohesive unit?		2		
20. Are you confident that the highest ethical standards are applied in the Committee deliberations and decisions/ recommendations in its role as the social conscience for the organization?		2		
21. Has the Committee acted in the best interests of the company and the shareholder, throughout the year?		2		
Part 5: Committee Functioning And Processes				

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	M1	M2	M3	Average
22. Does the Committee ensure adequate correlation and co-operation with the other committees of the Board and are overlaps in functions identified and avoided?	2	2	2	2.00
Part 6: Board Interaction And Accountability				
23. Is the Board appropriately well informed about deliberations, conclusions and recommendations of the Committee?		2		
24. Is the Social and Ethics Committee well regarded by the Board?	2	2	2	2.00
Part 7: Leadership And Support				
25. Is the Social and Ethics Committee chairman available and accessible?				
26. Are meetings run efficiently and effectively?				
27. Are meetings conducted in a manner that encourages open discussion, healthy debate, and allows each Committee member to clearly add value to discussion and decisions?				
28. Do members of this Committee feel supported and appropriately recognised by the Chairman and other Committee members for their contribution?		2		
29. Is the Company Secretary available and accessible?				

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8.5 Director Self Assessment

The Director self assessment was sent to 12 Directors and 9 responses were received as per below:

Part1: Knowledge And Skills	M1	M2	M3	M4	M5	M6	M7	M8	M9	Average
01. The Director understands the roles, responsibilities, duties, legal obligations and objectives of Directors and the Board?		2					2		2	1.33
02. The Director demonstrates relevant knowledge, skills and experience that contribute to the effectiveness of the Denel Board?		2			2	2	2		2	1.89
03. The Director acts confidentially, in good faith, ethically and legally and in the best interests of Denel?		2					2		1	1.22
04. The Director contributes effectively to the strategic direction of the company?		2		2	2		2		2	1.89
05. The Director probes and challenges issues before the Board constructively, prior to making their decision?		2					2		3	1.44
06. The Director takes tough, constructive stands at Board or committee meetings when necessary?		2					2	2	2	1.44
07. The Director discloses all conflicts of interests?							2	2	1	1.22
08. The Director works constructively with other Directors and confronts conflict positively to achieve the goals of the Board, and of Denel?				2			2	2	2	1.44
09. The Director is reliable to fulfil agreed or delegated tasks or actions?		2					2	2	1	1.33
10. The Director understands the socio-economic needs of South Africa, and ensures that Denel positively contributes to the further fulfilment of the country's socio-economic needs and development?							2	2	2	1.33
11. a. Does the Director display the following characteristics: • Integrity		2					2	2	1	1.33
11. b. Does the Director display the following characteristics: • Judgment							2	2	2	1.33
11. c. Does the Director display the following characteristics: • Independence (of mind)			2				2	2	2	1.44
11. d. Does the Director display the following characteristics: • Credibility and trustworthiness			2				2	2	1	1.33
11. e. Does the Director display the following characteristics: • Intuition			2	2			2	2	2	1.56
11. f. Does the Director display the following characteristics: • Willing to handle conflict constructively		2	2	2			2	2	1	1.56
11. g. Does the Director display the following characteristics: • An ability and desire to learn		2	2	2		2	2	2	2	1.78

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	M1	M2	M3	M4	M5	M6	M7	M8	M9	Average
11. h. Does the Director display the following characteristics: • An openness to new ideas		2	2	2	2	2	2	2	2	1.89
11 I. Does the Director display the following characteristics: • Good communication skills		2			2	2	2	2	1	1.56
11 j. Does the Director display the following characteristics: • Decision-making skills		2		2			2	2	1	1.44
11. k. Does the Director display the following characteristics: • Inter-personal skills		2		2			2	2	1	1.44
Part 2: Execution Of Duties										
12. The Director contributes actively and positively to discussions at meetings.		2		2			2	2	1	1.44
13. The Director devotes the time needed for the effective execution of Board responsibilities and is well prepared for Board meetings.		2		2		2	2	2	1	1.56
14. The Director displays an understanding of financial and operational matters and reports.	2	2		2			2	2		1.56
15. The Director attended all the scheduled meetings.		2					2	3	2	1.56
16. The Director acts with due care, skill and diligence.		2					2	2	1	1.33
17. The Director responds to issues in a timely and effective manner		2					2	2	1	1.33
Part 3: Chairman's Assessment										
18. The Chairman provides overall leadership to the Board without limiting the principle of collective responsibility for board decisions?				2			2	3	1	1.44
19. The Chairman ensures the Board's full discharge of its duties?				2			2	3	2	1.56
20. The Chairman provides input to the Minister on the skills, experience and attributes needed when appointing new Board Members?			3	3	3	3	3	3	2	2.44
21. The Chairman ensures that new Directors appointed to the Board are properly inducted and orientated?			3	3	3	3	2	3	1	2.22
22. The Chairman ensures that Board members receive on-going development in relevant areas including new and existing legislation for the industry?	2	2	3	3	2		3	3	1	2.22
23. The Chairman formulates an annual work plan for the Board against agreed objectives and goals, and played an active role in setting the agenda for Board meetings?		2	2	2			2	3	2	1.78
24. The Chairman acts as the main informal link between the Board and the CEO/Minister?	2			2			2	3		1.56
25. The Chairman maintains relations with Denel's shareholder and key stakeholders?	3	2		3			2	3		1.89
26. The Chairman monitors Board, Committee and Director performance/effectiveness?		2		2	2		2	3	3	1.89
27. The Chairman ensures that all Board members play a full and constructive role in the affairs of Denel?		2		2	2		2	3	2	1.78
28. The Chairman ensures that all relevant information and facts are placed before the Board to enable the Board members to reach informed decisions?		2		2			2	3	1	1.56

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	M1	M2	M3	M4	M5	M6	M7	M8	M9	Average
29. The Chairman ensures adequate lead time for effective consideration and discussion of business under consideration?		2		2	2		2	3		1.67
30. The Chairman interfaces effectively with the company secretariat?				2			2	3		1.44
31. The Chairman together with the CEO, represent Denel to external groups, and stakeholders?		2	2	2	2		2	3		1.78
32. The Chairman oversees a formal succession plan for the Board.	3	4	3	2	3	3	3	3	3	3.00
33. The Chairman effectively monitored conflicts of interest?		2	2	2			2	3	2	1.78
34. The Chairman ensured that Directors play a constructive role in the entity's affairs.		2	2	2			2	3	2	1.78
35. The Chairman monitors and evaluates the Board and individual Director's performance.		2	2	3			3	3	2	2.00
36. The Chairman takes a lead role in removing non-performing or unsuitable Directors from the Board.	2	3	4	3	2	3	3	3	3	2.89
37. The Chairman ensures that complete, accurate, timely, relevant, honest and accessible information is placed before the Board.		2	2	2			2	3		1.67
38. The Chairman ensures that good relations are maintained with major shareholders and strategic stakeholders.		2		2			2	3		1.56
39. The Chairman built and maintained stakeholders' trust and confidence.		2		2			2	3		1.56
40. The Chairman ensures that decisions taken by the Board are executed.		2	2	2	2		2	3		1.78

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8.6 Executive Director Assessment

The Director assessment was sent to 12 Directors and 8 responses were received

Executive Director Assessment	M1	M2	M3	M4	M5	M6	M7	M8	Average
01. In addition to the Board papers does this Executive Director provide sufficient additional information, insight and clarification into issues facing the Board, to ensure appropriate understanding of the matter to support effective decision making?		2		2	2		2	2	1.90
02. Does this Executive Director proactively and transparently table issues and developments at the Board to ensure that the Board and all individual Directors can effectively discharge their accountability; as opposed to holding back information that is relevant to the Board, possibly from a defensive executive standpoint?			2	2			2	2	1.90
03. Does this Executive Director successfully "transition" from being an executive and line manager, to being a Director of the company; as opposed to being overly defensive or protective of line management's deliverables and position on issues?			2	2			2	2	1.90

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BOARD MEMBERS ATTENDANCE FOR THE PERIOD 1 APRIL 2014 – 31 MARCH 2015

Board meeting attendance

BOARD MEMBER	BOARD MEETINGS						AGM
	Total	Special 22 May 14	26 Jun 14	10 Sep 14	19 Nov 14	11 Feb 15	15 Aug 14
Mr N R Kunene (Chairperson)	1/2	A	√	-	-	-	√
Ms M J Janse van Rensburg (Acting Chairperson)	5/5	√	√	√	√	√	√
Mr R Saloojee	3/5	A	A	√	√	√	√
Mr G Badela	4/5	√	A	√	√	√	√
Dr G C Cruywagen	5/5	√	√	√	√	√	√
Prof T Marwala	2/2	√	√	-	-	-	√
Ms Z B Mathenjwa	5/5	√	√	√	√	√	√
Mr F Mhlontlo	5/5	√	√	√	√	√	√
Mr N J Motseki	5/5	√	√	√	√	√	√
Mr M Msimang	5/5	√	√	√	√	√	√
Mr B F Ngwenya	5/5	√	√	√	√	√	√
Prof S M Nkomo	5/5	√	√	√	√	√	√
Adv M S Ntshikila	4/5	√	√	√	A	√	A
Ms B Paledi	0/2	A	A	-	-	-	√
Mr M V Ratshimbilani	4/5	√	A	√	√	√	√

A = Apology
Acting Chairperson from 15 August 2014
Mr N R Kunene, Prof T Marwala and Ms B Paledi resigned 15 August 2014

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Audit & Risk Committee attendance

BOARD MEMBER	AUDIT AND RISK COMMITTEE MEETINGS				
	Total	12 Jun 14	25 Aug 14	12 Nov 14	28 Jan 15
Ms M J Janse van Rensburg (Chairperson)	4/4	√	√	√	√
Dr G C Cruywagen (Chairperson)	4/4	√	√	√	√
Ms B Paledi	0/1	A	-	-	-
Ms Z B Mathenjwa	4/4	√	√	√	T
STANDING INVITEES					
Mr R Saloojee	4/4	√	√	√	√
Mr F Mhlontlo	4/4	√	√	√	√

A = Apology
T = Via telecon
Dr G C Cruywagen Chairperson from 15 August 2014
Ms B Paledi resigned 15 August 2014

Personnel, Remuneration and Transformation Committee attendance

BOARD MEMBER	PERSONNEL, REMUNERATION AND TRANSFORMATION COMMITTEE MEETINGS				
	Total	Special 14 May 14	11 Jun 14	5 Nov 14	27 Jan 15
Prof S M Nkomo (Chairperson)	4/4	√	√	√	√
Mr G Badela	4/4	√	√	√	√
Adv M S Ntshikila	3/4	√	√	A	√
Mr M V Ratshimbilani	2/4	√	A	√	A
STANDING INVITEES					
Mr R Saloojee	3/3	-	√	√	√
Mr F Mhlontlo	2/3	-	√	A	√

A = Apology
- = In-committee

Company Confidential

Social and Ethics Committee attendance

BOARD MEMBER	SOCIAL AND ETHICS COMMITTEE MEETING			
	Total	12 Jun 14	22 Oct 14	27 Jan 15
Prof S M Nkomo (Chairperson)	3/3	√	√	√
Dr G C Cruywagen	3/3	√	√	√
Mr M Msimang	3/3	√	√	√
STANDING INVITEES				
Mr R Saloojee	2/3	√	A	√
Mr F Mhlontlo	2/3	√	A	√

A = Apology
- = In-committee

Company Confidential

ANNEXURE "KT2"

ANNEXURE TO BE DISCUSSED DURING HEARING

ANNEXURE "KT3"

TK 592 →
to replace old Cab Memo.

public enterprises
Department:
Public Enterprises
REPUBLIC OF SOUTH AFRICA

DECISION MEMORANDUM

TO : MS. LYNNE BROWN, MP

MINISTER

FROM : MR. MELANCHTON MAKOBE

ACTING DEPUTY DIRECTOR-GENERAL: LGR

FILE REF : 10/1/3/2

IDMS REF : 181390

SUBJECT : CABINET MEMORANDA NOS 3, 4 AND 5 OF 2015: THE APPOINTMENT OF NON-EXECUTIVE DIRECTORS TO THE BOARDS OF SA EXPRESS, DENEL AND ESKOM, RESPECTIVELY

DATE : 11 MAY 2015

---

1. PURPOSE

1.1 To request the Minister to approve an urgent submission of Cabinet Memoranda number 3, 4 and 5 of 2015 on the appointment of the new members to the Boards of South African Express Airways SOC Ltd (SA Express), Denel SOC Ltd (Denel) and Eskom SOC Ltd (Eskom) to the Cabinet Meeting scheduled for 13 May 2015; and

1.2 To request the Minister to sign the letter to the President requesting late and direct submission to the Cabinet meeting of 13 May 2015. The letter to the President is attached hereto as **Annexure "A"**.

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1.3 To request the Minister to sign Cabinet Memoranda 3, 4 and 5, if in agreement with the content thereof. Copies of Cabinet Memoranda are attached hereto as **Annexure "B", "C" and "D".**

2. ANALYSIS AND FINDINGS

2.1 CABINET MEMORANDUM 3 OF 2015: APPOINTMENT OF NON-EXECUTIVE DIRECTOR TO THE SA EXPRESS BOARD

2.1.1 The SA Express Memorandum of Incorporate ("MOI") provides for a minimum of three (3) Directors, and a maximum of twelve (12) Directors, the majority of which shall be Non-Executive Directors and at least two (2) Executive Directors, being the CEO and CFO. There are currently eight (8) Directors on the SA Express Board, six (6) of whom are Non-Executive Directors and two (2) are Executive Directors. It is recommended that three (3) Non-Executive Directors of the Board be re-appointed for purposes of continuity and five (5) new Non-Executive Directors be appointed to the SA Express Board.

2.1.2 Three (3) Non-Executive Directors are recommended for rotation, namely: Ms Karabo Tshailane Nondumo, Ms Nosipho Gxumisa and Dr Bridget Ssamula.

2.1.3 It is recommended that Mr George Mothema, Mr Ezrom Mabyana and Ms Boni Dibate be re-appointed as Non-Executive Directors with effect from 21 May 2015. It is also recommended that Mr Mothema be appointed as the Chairperson of the Board, for a three-year term, subject to annual review by the Minister of Public Enterprises.

2.1.4 It is further recommended that Mr Trevor Abrahams, Dr Rajesh Naithani, Mr Phetolo Ramosebudi, Ms Judith Nomvula Nkabinde and Mrs Given Refilwe Sibiya be appointed as Non-Executive Directors, with effect from 22 May 2015, for a three year term, subject to annual review by the Minister of Public Enterprises.

2.1.5 With these appointments, the SA Express Board will consist of a complement of ten (10) directors, including eight (8) Non-Executive Directors and two (2) Executive Directors. The Board will have two (2) vacancies which will be filled at a later stage. A copy of Cabinet Memorandum 3 of 2015 is attached hereto as **Annexure "B"**.

2.2 CABINET MEMORANDUM 4 OF 2015: APPOINTMENT OF NON-EXECUTIVE DIRECTOR TO THE DENEL BOARD

2.2.1 The Denel Memorandum of Incorporate ("MOI") provides for the minimum of three (3) Directors and a maximum of sixteen (16) Directors. There are currently twelve (12) Directors on the Denel Board, ten (10) of whom are Non-Executive Directors and two (2) are Executive Directors. It is recommended that one (1) Non-Executive Directors be re-appointed for purposes of continuity and nine (9) new Non-Executive Directors be appointed to the Denel Board with effect from 24 July 2015.

2.2.2 The following Non-Executive Directors are recommended for rotation, namely: Dr Gert Cruywagen, Ms Martie Janse van Rensburg, Adv Melissa Ntshikila, Adv Ghandi Badela, Mr Mavuso Msimang, Mr Bafana Ngwanya, Prof Stella Nkomo, Mr Matodzi Ratshimbilani and Ms Ziphozethu Mathenjwa.

2.2.3 It is recommended that Mr Nkopane Motseki be reappointed as Non-Executive Director of the Denel Board with effect from 23 July 2015 for a three-year term, subject to annual review by the Minister of Public Enterprises;

2.2.4 It is recommended that Mr Daniel Mantsha be appointed as Non-Executive Director and Chairperson of the Denel Board with effect from 24 July 2015, for a three-year term, subject to annual review by the Minister of Public Enterprises; and

2.2.5 It is further recommended that Mr Thamsanqa Msomi, Mr Tauyame Mahumapelo, Mrs Pinkie Martha Mahlangu, Lt Gen Themba Michael Nkabinde (rtd), Ms Mpho Kgomongoe, Ms Khumbudzo Ntshavheni, Ms Nonyameko Mandindi and Ms Refiloe Mokoena be appointed as Non-Executive Directors to the Denel Board, with effect from 24 July 2015, for a three-year term, subject to annual review by the Minister of Public Enterprises.

2.2.6 With these appointments, the Denel Board will consist of a complement of twelve (12) Directors comprising ten (10) Non-Executive Directors and two (2) Executive Directors. The Board will have four (4) vacancies which will be filled at a later stage. A copy of Cabinet Memorandum 4 of 2015 is attached hereto as **Annexure "C"**.

2.3 CABINET MEMORANDUM 5 of 2015: APPOINTMENT OF NON-EXECUTIVE DIRECTOR TO THE ESKOM BOARD

2.3.1 The Eskom Memorandum of Incorporate ("MOI") provides for a minimum of three (3) Directors and maximum of fifteen (15) Directors. There are currently eleven (11) Directors on the Eskom Board, nine (9) of whom are Non-Executive Directors and two (2) are Executive Directors. It is recommended that two (2) Non-Executive Directors be appointed to the Board, to address the vacancies and skills gap, particularly in respect of financial management and global electricity industry knowledge.

2.3.2 It is recommended that Mrs Mariam Cassim and Mr Giovanni Leonardi be appointed as Non-Executive Directors to the Eskom Board with effect from 25 May 2015, for a three year term, subject to annual review by the Minister of Public Enterprises.

2.3.3 With these appointments, the Eskom Board will consist of a complement of thirteen (13) Directors, comprising of eleven (11) Non-Executive Directors and two (2) Executive Directors. The Board will have two (2) vacancies which will be filled at a later stage. A copy of Cabinet Memorandum 5 of 2015 is attached hereto as **Annexure "D"**

2.3.4 The Minister should note that on 30 March 2015 Mr Zola Tsotsi resigned as a Non-Executive Director and Chairperson of the Eskom Board and on 20 April 2015 Mr Tinyiko Baloyi was removed as a Non- Executive Director of the Board.

2.3.5 On 31 March 2015 Dr Baldwin Ngubane was appointed as an Interim Chairperson, following the resignation of Mr Tsotsi.

2.4 It should be noted that each Cabinet Memorandum contains the relevant Curriculum Vitae, Experian checks and lists of current and new Boards as per the recommendations.

3. FINANCIAL IMPLICATIONS

No financial implications for this memorandum.

4. CONSULTATION/PROJECT TEAM

Transport Enterprises, Manufacturing Enterprises and Energy Enterprises.

5. RECOMMENDATION

It is recommended that the Minister:

5.1 Note the contents of this memo;

5.2 Approves appointment/retention and rotation of the Board members of South African Express Airways (SA Express), Denel and Eskom SOC LTD;

5.3 Signs the letter to the President requesting late and direct submission to the Cabinet meeting of 13 May 2015; and

5.4 Signs Cabinet Memoranda 3, 4 and 5, if in agreement with the contents thereof.

CABINET MEMORANDA NOS 3, 4 AND 5 OF 2015: THE APPOINTMENT OF NON-EXECUTIVE DIRECTORS TO THE BOARDS OF SA EXPRESS, DENEL AND ESKOM, RESPECTIVELY

Memorandum prepared by:

LAWRENCE NEVONDO
ASD: GOVERNANCE
DATE: 11/05/2015

REVIEWED AND SUPPORTED:

ORCILLA RUTHNAM
CD: GOVERNANCE
DATE: 11/05/2015

MELANCHTON MAKOBE
ADDG: LGR
DATE: 11/05/2015

MS. MATSIETSI MOKHOLO
ACTING DIRECTOR-GENERAL
DATE: 11/05/2015

RECOMMENDED / NOT RECOMMENDED / COMMENTS

MS. LYNNE BROWN, MP
MINISTER
DATE: 11/05/2015

APPROVED / NOT APPROVED / COMMENTS

MR. BULELANI GRATITUDE MAGWANISHE, MP
DATE: 11/05/2015

NOTED / COMMENTS

ANNEXURE “KT4”

DENEL GROUP

29 October 2015
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Minister L. Brown
Minister of Public Enterprises
Department of Public Enterprises
Private Bag x15
HATFIELD
0028

DEPARTMENT OF PUBLIC ENTERPRISES
PRIVATE BAG/PRIVAATSAK X15
2015 -10- 30
HATFIELD 0028
DEPARTEMENT VAN OPENBARE ONDERNEMINGS

Dear Minister Brown

PFMA SECTION 54 (2) PRE NOTIFICATION: PROPOSED FORMATION OF DENEL ASIA

This letter serves as a PFMA Section 54 (2) pre-notification informing the Department of Public Enterprises (DPE) of Denel SOC Limited ("**Denel**") intention to establish an incorporated joint venture company in Hong Kong for purposes of exploiting opportunities in the Asia defense market.

Rationale

The Asia Pacific region is perceived to be the leading global (excluding USA) defense market and a potent force in defense technology innovation. This has resulted in increased defense spending i.e. by 2018 defense budgets across Asia Pacific (excluding USA) are expected to grow by over 19% to about USD 612billion; the procurement budgets are expected to increase by 28%, research and development projected growth is between 28 and 29% from 2014 to 2018.

Denel's growth strategy as set out in its corporate plan, is based on, inter alia, making inroads into global target markets. The current Denel strategy, based on the internal strengths and weaknesses as well as a regional analysis, is to actively pursue opportunities in the Asia-Pacific market in which Denel has been active since the early 1990's with minimal success.

Denel SOC Ltd, Reg No 1992/001337/30, Nellmapius Drive, Irene
P O Box 8322, Centurion, 0046, South Africa. Tel: +27 (0)12 671 2700, Fax: +27 (0)12 671 2751
Directors: Mr L D Mantsha (Chairman), Mr R Saloojee[1] (Group Chief Executive Officer), Ms M Kgomongoe, Mr T D Mahumapelo, Ms P M Mahlangu, Ms N Mandindi, Mr Z Mhlontlo[1], Ms R Mokoena, Mr N J Motseki, Mr T J Msomi, Lt Gen T M Nkabinde (rtd), Ms K P S Ntshavheni

[1]Executive Director
Group Company Secretary: Ms E M Africa

COPY

Countries such as India, Indonesia, Singapore, Thailand, Brunei, Philippines and Vietnam are considered to be primary target markets for Denel whilst markets such as Myanmar, Sri Lanka and Bangladesh, form secondary target markets.

India uses defense spending to develop its domestic industrial base to create high value jobs. India's government dominated defense industrial base has been open to private sector participation only since 2001 and is highly dependent on imports limiting the contribution of defense spending to economic development. To address this limitation, the government has increased foreign direct investment to 49% ownership of a defense company. This has given rise to the "Buy Make India' program. This seems to be a growing trend in the region.

In analysing the Denel business in the Asia Pacific region, the following emerged as barriers to entry into this fast growing market:

- lack of multilateral defense relationships;
- inability to provide funding solutions;
- inability to source local production and development partners (particularly in India);
- frequent engagement with end user and industry from a distance not feasible;
- company visibility in the market place/region from a distance is limited;
- need for a conduit for developing/Aligning with local business networks; and
- active participation in regional initiatives from a distance are not feasible.

Given the above barriers, it makes commercial sense for Denel to enter into a joint venture with a company that is already established in the region and which has an established network of potential business sources that will provide immediate and urgent solutions to the barriers raised above.

Rationale for the formation of Denel Asia

VR Laser Asia approached Denel with a business proposition. After careful consideration, Denel recognised the synergies that exist and the ability to jointly take advantage of existing opportunities.

The advantages of Denel entering the Asia market with VR Laser Asia include:

- the provision of quick access to local potential production and development partners
- a deeper understanding of the local market and industrial landscape
- the ability to align with local business networks
- access to operational funding
- the ability to increase visibility in the market/region

For the above reasons it is proposed that a company, Denel Asia, be registered in Hong Kong in partnership with VR Laser Asia. Therefore, Denel can leverage on VR Laser Asia's infrastructure and presence in the region.

Financing:

- VR Laser Asia will be responsible for all operational costs for a period of 5 years estimated at a R100 million
- Project funding as and when required will be provided by shareholders.

Financial viability

- In light of the R100 million investment by VR Laser Asia into Denel Asia over a 5 year period for operating costs, the operational financial risks to Denel are minimal.
- Overall there is currently potential business amounting to USD 9,2 billion over the next 5 years that offers Denel lucrative opportunities within this region. These opportunities will be concluded on a commercially viable basis

  (See Appendix 2 representing opportunities that Denel feels confident will be secured jointly with VR Laser Asia).

Technology transfer and protection of Denel's IP

- Denel will not alienate its Intellectual Property and technology transfer will be done by way of a licencing agreement between Denel and Denel Asia.
- Applicable royalties of third parties including those of Denel will be addressed.

Risks and mitigation

Risks		**Mitigation/Remarks**
1.	Reputational	• No agents will be involved • Denel has a controlling share

2.	Guarantees	• Reduced balance sheet exposure due to partnering
3.	Penalties	• Both Denel and VR Laser Asia, have the skill, expertise and experience to minimise the possibility of penalties being incurred
4.	Legal Exposure	• Denel SA exposure (Indemnities and no liability in terms of current proceedings and future transactions to be addressed)
5.	PFMA Conditions	• Adhere to all shareholder conditions prior to Shareholders Agreement and ancillary agreements.

Governance Structure:

The salient features of the transaction agreed to in principle with VR Laser Asia and as set out in a co-operation agreement, which remains subject to regulatory approval, are as follows:

Company Structure

A new limited liability company (Denel Asia) is to be registered in Hong Kong. It should be noted that the company will be established and managed in line with corporate governance best practices to reflect an independent organisation accountable to its shareholders.

- Denel, will hold 51% of the issued share capital of Denel Asia with the remaining 49% to be held by VR Laser Asia.
- Denel as majority shareholder will be able to influence the strategic direction of Denel Asia at a shareholder level.
- Upon incorporation, a board of directors will be constituted comprising Denel and VR Laser Asia representatives (with Denel appointing the first Chairman).
- Subject to relevant approvals, the Shareholders agreement, Memorandum of Incorporation (MOI) in relation to Denel Asia as well as a licence agreement are to be concluded,

finalised and signed between Denel and Denel Asia. These will regulate the terms on which Denel will make certain intellectual property available to Denel Asia. Upon execution of the shareholders' agreements, the co-operation agreement will terminate.

Suspensive Condition

- The co-operation agreement is subject to internal and regulatory approvals.

WAY FORWARD

The following activities will take place towards the establishment of Denel Asia:

Action	Timeline
Negotiation and conclusion of the cooperation agreement	Completed and remains subject to board and PFMA approval.
The formation of Denel Asia has been tabled at the Denel Board	10 September 2015
PFMA pre-notification	30 October 2015
Statutory and Regulatory approvals	November 2015
PFMA submission	November 2015

Recommendation

Denel will keep the Department abreast of developments as it progresses and will submit a full PFMA application once the negotiation process including all ancillary agreements (such as the Shareholders Agreement and Licencing Agreement) has been concluded subject to PFMA and other regulatory approvals.

I trust that you will find the above in order and remain at your disposal for any further clarification that may be required.

Yours faithfully

Mr L. D. Mantsha

CHAIRMAN OF THE DENEL BOARD

30/10/2015

cc Ms Matsietsi Mokholo – Acting **Director-General** Department of Public Enterprises

Mr Zwelakhe Ntshepe – Acting GCEO: Denel

COMMISSION OF INQUIRY INTO STATE CAPTURE

Appendix 2

Estimated Project Income

Country		Products		Quantities	Turnover	Expected Order Date	Probability	Status
					USD'm			
India								
(20 year market presence)		Turrets/Vehicles (Infantry Fighting Vehicle Program)	DLS	1000	2 000.000	2018	30%	Strong market requirement but No interaction yet
		T6 Artillery Turrets	DLS	200	760.000	2017	50%	Historical investment of +-R200m. Evaluations, Technical & commercial negotiations completed.
		T5-52 Truck Mounted Artillery Gun	DLS	814	2 849.000	2018	60%	Limited trials completed in India by Tata. Influence required to tighten specification.
		G6-52 Wheeled Artillery Gun	DLS	300	2 100.000	2017	60%	Historical investment of +-R200m. Evaluations, Technical & commercial negotiations completed.
		SS77 Machine Gun	DLS	9600	144.000	2016	60%	Quotation submitted.
		35mm Air Defence Cannon	DLS	400	140.000	2017	50%	Informal RFI received. Discussion in process.
		Automatic Grenade Launcher	DLS	3000	135.000	2016	30%	Unexplored opportunity
		NTW20 Anti-Material Rifle	DLS	700	28.700	2016	65%	Signed contract to be reinstated.
		Unmanned Aerial Vehicle	Dene	0	-	-		To be explored
		155mm Ammo	RDM	0	-	-		ToT completed for ERFB. Opportunity for Assegai TOT.
		Bi-Modular Charges	RDM	0	-	-		Datapack already transferred.
					8 156.700			
Bangladesh								
		105mm Towed Artillery Gun	DLS	36	64.800	2017	30%	RFI issued.
		155mm Towed Artillery Gun	DLS	36	90.000	2017	30%	RFI issued.
		105mm Ammo	RDM	0	-	-		RFI issued.
		155mm Ammo	RDM	0	-	-		RFI issued.
		Bi-Modular Charges	RDM	0	-	-		RFI issued.
					154.800			
Singapore								
		GI2 Naval Cannon Systems	DLS	25	24.100	2016	60%	Follow on order expected.
					24.100			
Thailand								
		GI2 Naval Cannon Systems	DLS	40	8.000	2016	70%	Follow on order expected.
		GI30 Naval Cannon	DLS	25	75.000	2016	50%	Explore opportunity.
		105mm Towed Howitzer	DLS	92	165 600	2018	30%	Requirement exists. Opportunity to be explored.
		155mm Towed Howitzer	DLS	18	45.000	2020	30%	Requirement exists. Opportunity to be explored.
		155mm Self- Propelled Howitzer	DLS	6	42.000	2023	30%	Requirement exists. Opportunity to be explored.
		35mm DPG Naval Cannon	DLS	10	50.000	2016	30%	Technical presentation made. Budgetary price submitted.
					385.600			
Indonesia								
		PK-20 Turret	DLS	142	89.460	2016	60%	Product Certified. Explore ToT.
		MT 105mm Armour Turret	DLS	138	372.600	2017	50%	Opportunity exists for medium tank. Explore co operation with Rheinmetall
					462.060			
Philippines								
		GI2 Naval Cannons	DLS	18	17.010	2017	40%	RFI issued. Explore opportunity
		GI30 Naval Cannon	DLS	12	36.000	2018	30%	RFI issued. Explore opportunity
					53.010			
Vietnam								
		35mm DPG Naval Cannon	DLS	10	50.000	2017	30%	Technical presentation made.
					50.000			
Myanmar								
		35mm DPG Naval Cannon. Manufacturing licence.	DLS	1	10.000	2016	70%	Technical Presentation made. Negotiation invitation awaited.
					10.000			
				TOTAL	9 296.270			

Probability legend	Definition
0-30%	Requirement identified. Opportunity to be explored.
30-60%	Requirement confirmed. Discussions/exploration on-going.
>60%	Negotiations in process.

STATE CAPTURE

ACKNOWLEDGEMENT OF RECEIPT

Letter re. Pre-Notification – PFMA Application

	Name (Print)	Signature	Date and time
Minister L Brown **Minister of DPE**	Keromamang		30/10/2015 16:00
Minister N Nene **Minister of Finance**			30/10/15

KT-200





DENEL GROUP

29 October 2015
Tel +27 12 671 2858
Fax +27 12 671 2751
zwelakhen@denel.co.za

The Honourable Mr Nhlanhla Nene
Minister of Finance
Department of National Treasury
Private Bag X115
PRETORIA
0001

Dear Minister Nene

PFMA SECTION 54 (2) PRE NOTIFICATION: PROPOSED FORMATION OF DENEL ASIA

This letter serves as a PFMA Section 54 (2) pre-notification informing the Department of Public Enterprises (DPE) of Denel SOC Limited ("**Denel**") intention to establish an incorporated joint venture company in Hong Kong for purposes of exploiting opportunities in the Asia defense market.

Rationale

The Asia Pacific region is perceived to be the leading global (excluding USA) defense market and a potent force in defense technology innovation. This has resulted in increased defense spending i.e. by 2018 defense budgets across Asia Pacific (excluding USA) are expected to grow by over 19% to about USD 612billion; the procurement budgets are expected to increase by 28%; research and development projected growth is between 28 and 29% from 2014 to 2018.

Denel's growth strategy as set out in its corporate plan, is based on, inter alia, making inroads into global target markets. The current Denel strategy, based on the internal strengths and weaknesses as well as a regional analysis, is to actively pursue opportunities in the Asia-Pacific market in which Denel has been active since the early 1990's with minimal success.

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Directors: Mr L D Mantsha (Chairman), Mr R Saloojee[1] (Group Chief Executive Officer), Ms M Kgomongoe, Mr T D Mahumapelo, Ms P M Mahlangu, Ms N Mandindi, Mr Z Mhlontlo[1], Ms R Mokoena, Mr N J Motseki, Mr T J Msomi, Lt Gen T M Nkabinde (rtd), Ms K P S Ntshavheni,

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COPY

Countries such as India, Indonesia, Singapore, Thailand, Brunei, Philippines and Vietnam are considered to be primary target markets for Denel whilst markets such as Myanmar, Sri Lanka and Bangladesh, form secondary target markets.

India uses defense spending to develop its domestic industrial base to create high value jobs. India's government dominated defense industrial base has been open to private sector participation only since 2001 and is highly dependent on imports limiting the contribution of defense spending to economic development. To address this limitation, the government has increased foreign direct investment to 49% ownership of a defense company. This has given rise to the "Buy Make India' program. This seems to be a growing trend in the region.

In analysing the Denel business in the Asia Pacific region, the following emerged as barriers to entry into this fast growing market:

- lack of multilateral defense relationships;
- inability to provide funding solutions;
- inability to source local production and development partners (particularly in India);
- frequent engagement with end user and industry from a distance not feasible;
- company visibility in the market place/region from a distance is limited;
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Given the above barriers, it makes commercial sense for Denel to enter into a joint venture with a company that is already established in the region and which has an established network of potential business sources that will provide immediate and urgent solutions to the barriers raised above.

Rationale for the formation of Denel Asia

VR Laser Asia approached Denel with a business proposition. After careful consideration, Denel recognised the synergies that exist and the ability to jointly take advantage of existing opportunities.

The advantages of Denel entering the Asia market with VR Laser Asia include:

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For the above reasons it is proposed that a company, Denel Asia, be registered in Hong Kong in partnership with VR Laser Asia. Therefore, Denel can leverage on VR Laser Asia's infrastructure and presence in the region.

Financing:

- VR Laser Asia will be responsible for all operational costs for a period of 5 years estimated at a R100 million
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- In light of the R100 million investment by VR Laser Asia into Denel Asia over a 5 year period for operating costs, the operational financial risks to Denel are minimal.
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  (See Appendix 2 representing opportunities that Denel feels confident will be secured jointly with VR Laser Asia).

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Risks and mitigation

Risks		Mitigation/Remarks
1.	Reputational	• No agents will be involved • Denel has a controlling share
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4.	Legal Exposure	• Denel SA exposure (Indemnities and no liability in terms of current proceedings and future transactions to be addressed)
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- Denel as majority shareholder will be able to influence the strategic direction of Denel Asia at a shareholder level.

- Upon incorporation, a board of directors will be constituted comprising Denel and VR Laser Asia representatives (with Denel appointing the first Chairman).
- Subject to relevant approvals, the Shareholders agreement, Memorandum of Incorporation (MOI) in relation to Denel Asia as well as a licence agreement are to be concluded, finalised and signed between Denel and Denel Asia. These will regulate the terms on which Denel will make certain intellectual property available to Denel Asia. Upon execution of the shareholders' agreements, the co-operation agreement will terminate.

Suspensive Condition

- The co-operation agreement is subject to internal and regulatory approvals.

WAY FORWARD

The following activities will take place towards the establishment of Denel Asia:

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PFMA pre-notification	30 October 2015
Statutory and Regulatory approvals	November 2015
PFMA submission	November 2015

Recommendation

Denel will keep the Department abreast of developments as it progresses and will submit a full PFMA application once the negotiation process including all ancillary agreements (such as the Shareholders Agreement and Licencing Agreement) has been concluded subject to PFMA and other regulatory approvals.

I trust that you will find the above in order and remain at your disposal for any further clarification that may be required.

Yours faithfully

Mr L. D. Mantsha
CHAIRMAN OF THE DENEL BOARD
30/10/2015

cc Ms Matsietsi Mokholo – Acting **Director-General** Department of Public Enterprises
Mr Lungisa Fuzile – Director General: National Treasury
Mr Zwelakhe Ntshepe – Acting GCEO: Denel
Mr Odwa Mhlwane – Acting Group Financial Director: Denel

COMMISSION OF INQUIRY INTO STATE CAPTURE

Appendix 2

Estimated Project Income

Country		Products		Quantities	Turnover	Expected Order Date	Probability	Status
India					USD'm			
(20 year market presence)		Turrets/Vehicles (Infantry Fighting Vehicle Program)	DLS	1000	2 000.000	2018	30%	Strong market requirement but No interaction yet
		T6 Artillery Turrets	DLS	200	760.000	2017	50%	Historical investment of +-R200m. Evaluations, Technical & commercial negotiations completed.
		T5-52 Truck Mounted Artillery Gun	DLS	814	2 849.000	2018	60%	Limited trials completed in India by Tata. Influence required to tighten specification.
		G6-52 Wheeled Artillery Gun	DLS	300	2 100.000	2017	60%	Historical investment of +-R200m. Evaluations, Technical & commercial negotiations completed
		S577 Machine Gun	DLS	9600	144.000	2016	60%	Quotation submitted.
		35mm Air Defence Cannon	DLS	400	140.000	2017	50%	Informal RFI received. Discussion in process.
		Automatic Grenade Launcher	DLS	3000	135.000	2016	30%	Unexplored opportunity
		NTW20 Anti-Materiel Rifle	DLS	700	28.700	2016	65%	Signed contract to be reinstated.
		Unmanned Aerial Vehicle	Dend	0	-	-		To be explored
		155mm Ammo	RDM	0	-	-		ToT completed for ERFB. Opportunity for Assegai TOT.
		Bi-Modular Charges	RDM	0	-	-		Datapack already transferred.
					8 356.700			
Bangladesh								
		105mm Towed Artillery Gun	DLS	36	64.800	2017	30%	RFI issued.
		155mm Towed Artillery Gun	DLS	36	90.000	2017	30%	RFI issued.
		105mm Ammo	RDM	0	-	-		RFI issued.
		155mm Ammo	RDM	0	-	-		RFI issued.
		Bi-Modular Charges	RDM	0	-	-		RFI issued.
					154.800			
Singapore								
		G12 Naval Cannon Systems	DLS	25	24.100	2016	60%	Follow on order expected.
					24.100			
Thailand								
		G12 Naval Cannon Systems	DLS	40	8.000	2016	70%	Follow on order expected.
		G130 Naval Cannon	DLS	25	75.000	2016	50%	Explore opportunity.
		105mm Towed Howitzer	DLS	92	165.600	2018	30%	Requirement exists. Opportunity to be explored.
		155mm Towed Howitzer	DLS	18	45.000	2020	30%	Requirement exists. Opportunity to be explored.
		155mm Self- Propelled Howitzer	DLS	6	42.000	2023	30%	Requirement exists. Opportunity to be explored.
		35mm DPG Naval Cannon	DLS	10	50.000	2016	90%	Technical presentation made. Budgetary price submitted.
					385.600			
Indonesia								
		PK-20 Turret	DLS	142	89.460	2016	60%	Product Certified. Explore ToT.
		MT 105mm Armour Turret	DLS	138	372.600	2017	50%	Opportunity exists for medium tank. Explore co operation with Rheinmetall.
					462.060			
Philippines								
		G12 Naval Cannons	DLS	18	17.010	2017	40%	RFI issued. Explore opportunity
		G130 Naval Cannon	DLS	12	36.000	2018	30%	RFI issued. Explore opportunity
					53.010			
Vietnam								
		35mm DPG Naval Cannon	DLS	10	50.000	2017	30%	Technical presentation made.
					50.000			
Myanmar								
		35mm DPG Naval Cannon. Manufacturing licence.	DLS	1	10.000	2016	70%	Technical Presentation made. Negotiation invitation awaited.
					10.000			
				TOTAL	9 296.270			

Probability legend	Definition
0-30%	Requirement identified. Opportunity to be explored.
30-60%	Requirement confirmed Discussions/exploration on-going.
>60%	Negotiations in process.

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Estimated Project Income

Country		Products		Quantities	Turnover	Expected Order Date	Probability	Status
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		T5-52 Truck Mounted Artillery Gun	DLS	614	2 849.000	2018	60%	Limited trials completed in India by Tata. Influence required to tighten specification.
		G6-52 Wheeled Artillery Gun	DLS	300	2 100.000	2017	60%	Historical investment of +-R200m. Evaluations, Technical & commercial negotiations completed.
		5577 Machine Gun	DLS	9600	144.000	2016	60%	Quotation submitted.
		35mm Air Defence Cannon	DLS	400	140.000	2017	50%	Informal RFI received. Discussion in process.
		Automatic Grenade Launcher	DLS	3000	135.000	2016	30%	Unexplored opportunity
		NTW20 Anti-Material Rifle	DLS	700	28.700	2016	65%	Signed contract to be reinstated.
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		155mm Towed Artillery Gun	DLS	36	90.000	2017	30%	RFI issued.
		105mm Ammo	RDM	0	-	-		RFI issued.
		155mm Ammo	RDM	0	-	-		RFI issued.
		Bi-Modular Charges	RDM	0	-	-		RFI issued.
					154.800			
Singapore								
		GI2 Naval Cannon Systems	DLS	25	24.100	2016	60%	Follow on order expected.
					24.100			
Thailand								
		GI2 Naval Cannon Systems	DLS	40	8.000	2016	70%	Follow on order expected.
		GI3D Naval Cannon	DLS	25	75.000	2016	50%	Explore opportunity.
		105mm Towed Howitzer	DLS	92	165.600	2018	30%	Requirement exists. Opportunity to be explored.
		155mm Towed Howitzer	DLS	18	45.000	2020	30%	Requirement exists. Opportunity to be explored.
		155mm Self- Propelled Howitzer	DLS	6	42.000	2023	30%	Requirement exists. Opportunity to be explored.
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		PK-20 Turret	DLS	142	89.460	2016	60%	Product Certified. Explore ToT
		MT 105mm Armour Turret	DLS	138	372.600	2017	50%	Opportunity exists for medium tank. Explore co operation with Rheinmetall.
					462.060			
Philippines								
		GI2 Naval Cannons	DLS	38	37.010	2017	40%	RFI issued. Explore opportunity
		GI30 Naval Cannon	DLS	12	36.000	2018	30%	RFI issued. Explore opportunity
					53.010			
Vietnam								
		35mm DPG Naval Cannon	DLS	10	50.000	2017	30%	Technical presentation made.
					50.000			
Myanmar								
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				TOTAL	9 296.270			

Probability legend	Definition
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30-60%	Requirement confirmed. Discussions/exploration on-going.
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STATE CAPTURE

ACKNOWLEDGEMENT OF RECEIPT

Letter re. Pre-Notification – PFMA Application

	Name (Print)	Signature	Date and time
Minister L Brown **Minister of DPE**	Keromamang		30/10/2015 16:00
Minister N Nene **Minister of Finance**			30/10/15

KT-209

ANNEXURE “KT5”

public enterprises

Department:
Public Enterprises
REPUBLIC OF SOUTH AFRICA

DECISION MEMORANDUM

DEPARTMENT OF PUBLIC ENTERPRISES
PRIVATE BAG/PRIVAATSAK X15
2015 -11- 20
HATFIELD 0028
DEPARTEMENT VAN OPENBARE ONDERNEMINGS

TO : **MS LYNNE BROWN**
MINISTER

FROM : **MS VUYO TLALE**
ACTING DDG: MANUFACTURING ENTERPRISES

FILE REF : **14/1/7/2**

IDMS REF : **185375**

SUBJECT : **DENEL: PFMA PRE-NOTIFICATION - PROPOSED FORMATION OF DENEL ASIA**

DATE : **16 OCTOBER 2015**

---

1. PURPOSE

1.1 To advise Minister on the contents of the letter from the Chairperson of the Denel Group, Mr Daniel Mantsha dated 29 October 2015 with regard to discussions between Denel and VR Laser Asia about establishing an incorporated joint venture company (Denel Asia) in Hong Kong for the purpose of exploiting opportunities in Asia defence market. The letter from Denel is attached hereto and marked as **Annexure "B"**; and

1.2 To request the Minister to sign the letter to the Chairperson of the Denel Group, Mr Lungisani Daniel Mantsha (copying the Minister of Finance), to grant in-principle approval for Denel to continue the discussions with VR Laser, subject to the conditions discussed in paragraph 3.10, if she is in agreement with the contents thereof. The letter is attached hereto and marked as **Annexure "A"**.

2. SUMMARY

2.1 The letter from Denel serves as a PFMA pre-notification for a possibility to establish an incorporated joint venture Company (Denel Asia) between Denel and VR Laser Asia in Hong

Kong for the purpose of exploiting opportunities in the Asia Defence market. Denel will hold 51% of the issued share capital in the joint venture company.

2.2 The two companies have agreed in principle on a number of transaction features, including, company structure, financing, technology transfer and protection of Denel's Intellectual Property.

2.3 After approval of relevant regulatory requirements, a new limited liability company (Denel Asia) will be registered in Hong Kong. Denel will hold 51% of the issued share capital with the remaining 49% held by VR Laser Asia. Upon incorporation, a Board of Directors will be constituted comprising of Denel and VR Laser Asia representatives with Denel appointing the first Chairperson.

2.4 The two companies estimate that the NewCo will require R100 million capital injection over a five (5) year period for operational costs. VR Laser Asia will be responsible for all the operational costs.

2.5 Project funding as and when required will be provided by Shareholders.

2.6 According to Denel, the advantages of entering the Asia market with VR Laser Asia include:

2.6.1 The provision of quick access to local potential production and development partners;

2.6.2 A deeper understanding of the local market and industrial landscape;

2.6.3 The ability to align with business network;

2.6.4 Access to operational funding;

2.6.5 The ability to increase visibility in the market/region; and

2.6.6 Leverage on VR Laser Asia's infrastructure and presence in the region.

2.7 At a meeting with the Department, Denel indicated that it received an unsolicited bid from VR Laser on this collaboration. Denel has undertaken to keep the Department updated with regard to the progress and will submit a full PFMA application once all due diligences and negotiations processes, including ancillary agreements have been successfully concluded.

2.8 At face value, the proposal is attractive. However, there are numerous fundamental gaps that need to be clarified by Denel in its full Section 54 PFMA application before a comprehensive advice can be given to the Minister with regard to the merits of the application.

2.9 Furthermore, Denel must seek approval of the Minister of Finance to establish Denel Asia in terms of Section 51 (g) of the PFMA before the approval of Section 54 (2) can be granted. Denel seems to have overlooked this requirement.

2.10 In terms of Denel's R1.85 billion Government Guarantee conditions, the Minister of Finance must also give his concurrence to any PFMA transactions and pre-notifications. Denel submitted a similar PFMA pre-notification letter to the Minister of Finance dated 29 October 2015. A copy is attached hereto and marked **Annexure "C"**.

3. ANALYSIS AND FINDINGS

3.1 The letter from Denel is not clear on the company, VR Laser Asia's background. From the desktop research the department found that VR Laser Asia is subsidiary of a South African company named VR Laser Services (Pty) Ltd. The South African based entity operates as a steel plate processing centre offering precision laser cutting, plasma cutting, machining, welding and fabrication, profile cutting and chamfering, and armour plate services.

3.2 VR Laser Services (Pty) Ltd operates as a subsidiary of VR Steel Group a company based in Gauteng. VR Laser Services (Pty) Ltd is involved in the supply of steel components for the infantry combat vehicles project Hoefyster in which Denel is the prime contractor.

3.3 The Department's initial CIPC check on ownership indicates that the directors of this company are Salim Aziz Essa, Pushpaveni Ugeshni Govender and Kamal Kant Singhala. The ownership structure could not be determined.

3.4 The Asia-Pacific region is experiencing a significant uptick in defence spends with the biggest contributor being China, India, Indonesia, Singapore, Thailand and Japan. By 2020, the center of gravity for the global defence spending landscape is expected to have continued its gradual shift away from the developed economies of Western Europe and North America towards emerging markets, particularly in Asia. In terms of overall growth in each region between 2015 and 2020, Asia Pacific is expected to solidify its role as the key driver of growth in the defence sector.

3.5 The Asia-Pacific is one of top regions identified in Denel's business growth strategy. The company has been exploring some Market opportunities for its defence and high-technology products in the region. In February 2014, Denel Aerostructures, signed a memorandum of understanding with the Strand Group in Malaysia to pool skills and resources and jointly pursue international contracts in aircraft design and manufacturing. During the year 2012

Denel Land Systems signed a €340 million (R3.5 billion) contract with Malaysia to supply a range of turret and integrated weapon systems. The Malaysian contract remains the single largest export contract for Denel since its incorporation in 1992. According to 2015/16 second quarterly report, Denel is pursuing a R1 billion order for the Umkhonto missile in Vietnam.

3.6 Accessing the Pacific-Asian defence market is likely to be a challenge for the envisaged new entity. Global defence original equipment manufacturers (OEMs) are targeting the growing Asian defence market to compensate for the stagnation at their home markets. These OEMs are also bringing substantial offset and funding proposals which small companies, such as Denel are unable to provide.

3.7 The value proposition of VR Laser Asia is not clear on how it plans to break into this highly competitive market given its own limited global reach. The pre-notification makes mention of the advantages of entering into partnership with VR Laser Asia, but it is not clear on how the NewCo (Denel Asia) will approach the market. The Department will wait for the business plan before expressing an opinion on whether the transaction makes commercial sense or not.

3.8 The Department is not comfortable with the impression that, project funding will be provided by Shareholders. Furthermore, the letter does not indicate whether the project funding by Shareholders will be in proportionate to their shareholding. It is also not clear whether the R100 million investments by VR Laser Asia in the establishment of Denel Asia is a loan and what the repayment terms are; and whether it is sufficient to cover the five (5) years operational costs considering that the entity will be chasing orders to a tune of R100 billion.

3.9 It should be noted that this transaction or similar to it is not proposed in the 2015/16 Corporate Plan. Furthermore, the current liquidity challenges facing the SOC could make it difficult for Denel to enter into another transaction. As it is, Denel has not yet closed the transaction with SAAB Grintek on the 51% acquisition of the Command and Control capability at a cost of R50 million.

3.10 However, based on the information submitted by Denel, the Department recommends that Denel should be granted in-principle approval to continue discussions with VR Laser subject to the following conditions:

3.10.1 Denel to obtain approval from the Minister of Finance in terms of Section 51(g) of the PFMA to establish a new entity;

3.10.2 Once the Minister of Finance has granted approval in terms of Section 51(g), the negotiations and the regulatory processes being completed, Denel must submit a section 54(2) PFMA application;

3.10.3 The application should include, amongst other things:

a) a comprehensive detailed business case to enable the Minister to express an opinion on the joint venture transaction;

b) a comprehensive due diligence report on the financial regulatory legal requirement and regulatory laws governing foreign owned entities in Hong Kong;

c) funding plans, all the transaction documents (including the MOU and Cooperation agreements);

d) the process followed to select VR Laser as a partner of choice;

e) the proposed structure of the proposed new company and breakdown of estimated operational costs (five year horizon budget indicating clear cost allocation of both parties);

f) a comprehensive due diligence of VR Laser which includes its financial standing, capabilities and ownership, defence and security product/service range and client base in Asia;

g) registration details of the company and shareholding of VR Laser Asia. This is important in order to ensure that all matters relating to the structure are addressed to protect Denel's status as the holding company;

h) the reason(s) for a Continent specific *versus* a Country specific arrangement and indicate preference of Hong Kong as a preferred domicile;

i) after VR Laser approached Denel with this business proposition, did the SOC undertake any studies that led to the conclusion that this partner is the most suitable; and

j) reason(s) why this transaction or similar to it is not proposed in the 2015/16 Corporate Plan.

3.10.4 The Board must also ensure that there is adequate governance oversight regarding the processes that underpin transaction discussions. Issues of conflict of interest, real or perceived, should be adequately monitored. All efforts should be made to minimise risk exposure for both Denel and the Shareholder.

4. FINANCIAL IMPLICATIONS

None for the Department

5. CONSULTATION/PROJECT TEAM

The assessment process has been led by the Manufacturing Enterprises Branch. Inputs from Legal, Governance and Risk Branch (LGR) pertaining to cross-cutting matters were received.

6. RECOMMENDATION

It is recommended that Minister:

6.1 notes the contents of this memorandum;

6.2 notes the recommendation by the Team is that Denel should continue with the Due Diligence and discussions with VR Laser;

6.3 notes that the approval does not grant Denel permission to conclude on the transaction as the business case is still outstanding; and

6.4 sign the letter to the Chairperson of the Denel Group, Mr Lungisani Daniel Mantsha, copying the Minister of Finance, to grant in-principle approval for Denel to continue the discussions with VR Laser, if she is in agreement with the contents thereof. The letter is attached hereto and marked as **Annexure "A"**; and

DENEL: PFMA PRE-NOTIFICATION - PROPOSED FORMATION OF DENEL ASIA

Memorandum prepared by:

MR WEEKEND BANGANE
CD: DEFENCE
DATE: 16/11/2015

MR PHAHLANI MKHOMBO
CD: LEGAL COUNSEL
DATE: 17/11/2015

REVIEWED AND SUPPORTED:

MS VUYO TLALE
ADDG: ME
DATE: 16/11/2015

MS MATSIETSI MOKHOLO
DDG: LGR
DATE: 18/11/2015

MR. KGATHATSO TLHAKUDI
ACTING DIRECTOR-GENERAL
DATE: 20/11/2015

RECOMMENDED / NOT RECOMMENDED / COMMENTS

MS. LYNNE BROWN, MP
MINISTER
DATE: 23/11/2015

APPROVED / NOT APPROVED / COMMENTS
Please stay close to this action because Weekend has asked many relevant questions, esp. re-funding of DenelAsia. (copy of memo please.)

MR. BULELANI GRATITUDE MAGWANISHE, MP
DEPUTY MINISTER
DATE: 25/11/2015

NOTED / COMMENTS

MINISTRY
PUBLIC ENTERPRISES
REPUBLIC OF SOUTH AFRICA

Private Bag X15, Hatfield, 0028 Tel: (012) 431 1118/1150 Fax: (012) 431 1039
Private Bag X9079, CAPE TOWN, 8000 Tel: (021) 461 6376/7/469 6760 Fax: (021) 465 2381/461 1741

Mr Lungisani Daniel Mantsha
Chairperson of the Denel Board
Denel SOC Ltd
P O Box 8322
Centurion
0046

Tel: (011) 11 781 0099 / (012) 671 2938
E-mail: dan@lungisanimanthsaattorneys.co.za / info@lugisanimantshaattorneys.co.za / fortune@denel.co.za / tanyav@denel.co.za

Dear Mr Mantsha

Re: PFMA Section 54 (2) Pre-Notification on the Proposed Formation of Denel Asia

The above matter has reference.

I concur with yourself that Pacific Asia defence market will remain on upward trajectory for the foreseeable future. It would therefore make strategic business sense for Denel to position itself to take advantage of the envisaged growth.

However, accessing the Asian market is likely to be daunting for the new entity. Global defence original equipment manufacturers (OEMs) are targeting the growing Asian defence market to compensate for the stagnation at their home markets. They bring with them substantial offset and funding proposals which small companies such as Denel may not be able to provide. The value proposition of VR Laser Asia wanting a tie up with Denel is not clear especially on how it plans to break into this highly competitive market given its own limited global reach.

Given the strategic importance of the Asia-Pacific defence market, I hereby grant in-principle approval for Denel to continue discussions with VR Laser and Denel can submit a section 54 (2) PFMA application to both myself as the Executive Authority and the Minister of Finance.

In order to protect Denel's status as the holding company, the application should include, amongst other things:

a) a comprehensive detailed business case to enable the Minister to express an opinion on the joint venture transaction;

b) a comprehensive due diligence report on the financial regulatory legal requirement and regulatory laws governing foreign owned entities in Hong Kong;

c) funding plans, all the transaction documents (including the MOU and Cooperation agreements);

d) the process followed to select VR Laser as a partner of choice;

e) the proposed structure of the proposed new company and breakdown of estimated operational costs (five year horizon budget indicating clear cost allocation of both parties);

f) a comprehensive due diligence of VR Laser which includes its financial standing, capabilities and ownership, defence and security product/service range and client base in Asia;

g) registration details of the company and shareholding of VR Laser Asia;

h) the reason(s) for a Continent specific versus a Country specific arrangement and indicate the preference of Hong Kong as a preferred *domicile*;

i) any studies that were undertaken by the SOC that led to the conclusion that this partner is the most suitable, after VR Laser approached Denel with this business proposition; and

j) reason(s) why this transaction or similar to it is not proposed in the 2015/16 Corporate Plan.

Thereafter, Denel is required to apply and get approval from the Minister of Finance in terms of Section 51(g) of the PFMA, which is a prerequisite when establishing a new entity. Once such approval has been obtained, all the negotiations, agreements and regulatory processes can be completed.

The Board must also ensure that there is adequate governance oversight regarding the processes that underpin transaction discussions. Issues of conflict of interest, real or perceived, should be adequately monitored. All efforts should be made to minimise risk exposure to both Denel and the Shareholder.

Yours sincerely

MS LYNNE BROWN, MP
MINISTER OF PUBLIC ENTERPRISES
DATE: 23/11/2015

cc Mr Nhlanhla Nene, MP
.: Minister of Finance

Tel: (012) 315-5559
Email: minreq@treasury.gov.za

cc Mr Zwelakhe Ntshepe
.: Acting Group Chief Executive Officer
Denel SOC Ltd

Tel: 012 671-2938
Email: ZwelakheN@denel.co.za / CharleneT@denel.co.za

Keromamang Mhlongo

From: Keromamang Mhlongo
Sent: 23 November 2015 02:30 PM
To: 'dan@lungisanimanthsaattorneys.co.za'; 'info@lungisanimantshaattorneys.co.za'; fortune@denel.co.za; TanyaV@denel.co.za
Cc: 'zwelakheN@denel.co.za'; CharleneT@denel.co.za; Minreg.Registry@treasury.gov.za; Weekend Bangane; Phahlani Mkhombo; Charmaine Yssel; Masenya Selatswa
Subject: Re:PFMA Section 54(2)Pre-notification on the Proposed formation of Denel Asia
Attachments: SKMBT_C36415112314120.pdf

Dear Mr Mantsha.

On behalf of Minister Lynne Brown, Minister of Public Enterprises kindly find attached letter on the above mention subject for your attention.

Please acknowledge receipt.

Thank you.

Kind regards.

Keromamang Mhlongo.
Registry.
Ministry of Public Enterprises.

+27 (0)12 431 1118 | +27 (0) 21 469 6760 +27 (0) 12 431 1039 | ministry.registry@dpe.gov.za

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public enterprises
Department:
Public Enterprises
REPUBLIC OF SOUTH AFRICA

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ANNEXURE "KT6"

MINISTRY
PUBLIC ENTERPRISES
REPUBLIC OF SOUTH AFRICA

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Mr Lungisani Daniel Mantsha
Chairperson of the Denel Board
Denel SOC Ltd
P O Box 8322
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0046

Tel: (011) 11 781 0099 / (012) 671 2938
E-mail: dan@lungisanimanthsaattorneys.co.za / info@lugisanimantshaattorneys.co.za / fortune@denel.co.za / tanyav@denel.co.za

Dear Mr Mantsha

Re: PFMA Section 54 (2) Pre-Notification on the Proposed Formation of Denel Asia

The above matter has reference.

I concur with yourself that Pacific Asia defence market will remain on upward trajectory for the foreseeable future. It would therefore make strategic business sense for Denel to position itself to take advantage of the envisaged growth.

However, accessing the Asian market is likely to be daunting for the new entity. Global defence original equipment manufacturers (OEMs) are targeting the growing Asian defence market to compensate for the stagnation at their home markets. They bring with them substantial offset and funding proposals which small companies such as Denel may not be able to provide. The value proposition of VR Laser Asia wanting a tie up with Denel is not clear especially on how it plans to break into this highly competitive market given its own limited global reach.

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In order to protect Denel's status as the holding company, the application should include, amongst other things:

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g) registration details of the company and shareholding of VR Laser Asia;

h) the reason(s) for a Continent specific versus a Country specific arrangement and indicate the preference of Hong Kong as a preferred *domicile*;

i) any studies that were undertaken by the SOC that led to the conclusion that this partner is the most suitable, after VR Laser approached Denel with this business proposition; and

j) reason(s) why this transaction or similar to it is not proposed in the 2015/16 Corporate Plan.

Thereafter, Denel is required to apply and get approval from the Minister of Finance in terms of Section 51(g) of the PFMA, which is a prerequisite when establishing a new entity. Once such approval has been obtained, all the negotiations, agreements and regulatory processes can be completed.

The Board must also ensure that there is adequate governance oversight regarding the processes that underpin transaction discussions. Issues of conflict of interest, real or perceived, should be adequately monitored. All efforts should be made to minimise risk exposure to both Denel and the Shareholder.

Yours sincerely

MS LYNNE BROWN, MP
MINISTER OF PUBLIC ENTERPRISES
DATE: 23/11/2015

cc Mr Nhlanhla Nene, MP
.: Minister of Finance

Tel: (012) 315-5559
Email: minreq@treasury.gov.za

cc Mr Zwelakhe Ntshepe
.: Acting Group Chief Executive Officer
Denel SOC Ltd

Tel: 012 671-2938
Email: ZwelakheN@denel.co.za / CharleneT@denel.co.za

Keromamang Mhlongo

From: Keromamang Mhlongo
Sent: 23 November 2015 02:30 PM
To: 'dan@lungisanimanthsaattorneys.co.za'; 'info@lungisanimantshaattorneys.co.za'; fortune@denel.co.za; TanyaV@denel.co.za
Cc: 'zwelakheN@denel.co.za'; CharleneT@denel.co.za; Minreg.Registry@treasury.gov.za; Weekend Bangane; Phahlani Mkhombo; Charmaine Yssel; Masenya Selatswa
Subject: Re:PFMA Section 54(2)Pre-notification on the Proposed formation of Denel Asia
Attachments: SKMBT_C36415112314120.pdf

Dear Mr Mantsha.

On behalf of Minister Lynne Brown, Minister of Public Enterprises kindly find attached letter on the above mention subject for your attention.

Please acknowledge receipt.

Thank you.

Kind regards.

Keromamang Mhlongo.
Registry.
Ministry of Public Enterprises.

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Department:
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ANNEXURE "KT7"

DENEL GROUP

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Email: zwelakhen@denel.co.za
Ref: Ltr/DPE/Denel Asia/2015

10 December 2015

The Honourable Ms Lynne Brown (MP)
Minister of Public Enterprises
Department of Public Enterprises
Private Bag X15
HATFIELD
0028

PER HAND

Dear Honourable Minister

FORMAL APPLICATION FOR APPROVAL IN TERMS OF SECTION 54(1) AND 54 (2) OF THE PUBLIC FINANCE MANAGEMENT ACT 1 OF 1999
RE PROPOSED ESTABLISHMENT OF DENEL ASIA SOC LIMITED

We refer to the pre-notification letter dated 29 October 2015, addressed to the Honourable Minister, which pre-notification served to inform the Department of Public Enterprises in terms of Section 54 (2) of the Public Finance Management Act 1 of 1999 ("**PFMA**") of the proposed establishment of a joint venture company in Hong Kong.

We hereby submit the formal application required in terms of the PFMA, more particularly sections 54(1), 54(2)(a), 54(2)(b) and 54(2)(e). In this regard, we shall simultaneously address the queries raised by the Honourable Minister re: the pre-notification letter. We shall equally inform National Treasury of the proposed establishment of a joint venture company in Hong Kong and its limited financial impact on Denel SOC Limited.

Should any further information be required, please do not hesitate to contact either the Denel Executive Management or myself.

Yours faithfully

Mr L. D. Mantsha
CHAIRMAN OF THE DENEL BOARD
11/12/2015

cc. Mr Richard Seleke — Director-General Department of Public Enterprises
Mr Zwelakhe Ntshepe — Acting GCEO: Denel

Denel SOC Ltd, Reg No 1992/001337/30, Nellmapius Drive, Irene
P O Box 8322, Centurion, 0046, South Africa. Tel: +27 (0)12 671 2700, Fax: +27 (0)12 671 2751
Directors: Mr L D Mantsha (Chairman), Mr R Saloojee[1] (Group Chief Executive Officer), Ms M Kgomongoe, Mr T D Mahumapelo, Ms P M Mahlangu, Ms N Mandindi, Mr Z Mhlontlo[1], Ms R Mokoena, Mr N J Motseki, Mr T J Msomi, Lt Gen T M Nkabinde (rtd), Ms K P S Ntshavheni,

[1]Executive Director
Group Company Secretary: Ms E M Africa

APPLICATION IN TERMS OF SECTION 54(1), 54(2)(a), 54(2)(b) and 54(2)(e) OF THE PFMA

1. EXECUTIVE SUMMARY

This document has been prepared in terms of Sections 54(1), 54(2)(a), 54(2)(b) and 54(2)(e) of the Public Finance Management Act No. 1 of 1999 ("**PFMA**"), as the intention of Denel SOC Ltd ("**Denel**") is to increase its international footprint and capabilities in line with its growth strategy.

The said application seeks to, inter alia, present a comprehensive business case for the establishment of "Denel Asia SOC Limited" ("**Denel Asia**") which would be a new subsidiary limited liability company in Hong Kong, with a view to exploiting opportunities in the Asia Pacific defence market.

It is intended that Denel Asia itself will, subject to applicable local legal requirements, in the future also establish further subsidiaries and/or joint venture companies in the Asia region.

2. BACKGROUND

Denel's growth strategy is based on, inter alia, making inroads into global target markets. The current Denel strategy, based on the internal strengths and weaknesses as well as a regional analysis, is to actively pursue opportunities in the Asia-Pacific market in which Denel has been active since the early 1990's.

2.1. Reasons why this transaction is not proposed in the 2015/2016 Corporate Plan

The proposed establishment of Denel Asia was not included in the 2015-2016 Corporate Plan, for inter alia, the following reasons:

(i) The Asia Pacific market did not play a significant role in Denel's order cover for the 2015/2016 financial year because Denel was excluded from business in India, one of Asia Pacific's largest markets. The reasons for Denel's exclusion from India are fully detailed in **paragraph 5.4** below. The opportunity to re-enter Asia-Pacific presented itself when the Indian Ministry of Defence (MOD) lifted its blacklisting against Denel as prior to the upliftment of the blacklisting, Denel could not contemplate the opportunity for doing business in India.

(ii) Further, the new Board of Directors of Denel, which was appointed only in July 2015, sought to extend Denel's participation in the Asia Pacific market as a way of increasing the order book. This emanated from the fact that there are immediate opportunities that Denel can take advantage of.

2.2. Governance Process: Denel Internal Approvals

ACTION	TIMELINE
Approval by Denel Board to explore a suitable equity partner for the Asia Pacific region	10 September 2015
Final approval by the Denel Board of the identified equity partner together with the draft PFMA application subject to, inter alia, Denel obtaining the requisite regulatory approvals and subject to certain conditions, which conditions have been dealt with in **paragraph 10.1** below.	7 December 2015

2.3. The reasons for Continent Specific vs Country Specific Arrangement and preference for Hong Kong

(i) Hong Kong is strategically located for business in Asia and can really be seen as the best gateway for doing business in that jurisdiction.

(ii) Conducting general business in Hong Kong is simple and setting up offices and structures are quick and inexpensive.

(iii) Foreigners can own 100% of a Hong Kong company and are free to be the sole directors and shareholders of a Hong Kong company. There are no local resident requirements and there are no restrictions on nationality.

(iv) A Hong Kong company offers global recognition and is very stable. Hong Kong is one of the world's major trading, finance and service centres.

(v) To open a Hong Kong company, you don't need a physical address in Hong Kong and your physical presence in Hong Kong is not required

(vi) Hong Kong adopts a territorial source principle of taxation meaning that all profits generated outside of Hong Kong are tax free and profits generated inside Hong Kong are taxed at 16.5%.

(vii) The legal system in Hong Kong is still ruled by British law.

3. REGIONAL STRATEGY

3.1. Studies Undertaken

Rapid and uneven economic development across 25 countries and regions of the Asia-Pacific region both enables and demands new approaches to national defence. By 2018, as global defence spending increases by 5.5 percent, defence budgets across the Asia-Pacific (excluding the US) are expected to grow by over 19 percent (Asia Pacific Defence Outlook 2015 – Deloitte report).

Rapid economic development has also created new sources of vulnerability. While the advancements are essential for developed economies, they require governments to plan for their defence, driving defence budgets and technical requirements upwards and increasing security threats have led to substantial increases in defence spending.

Increasing Global terrorism is also playing a major role in this region. Five Asia-Pacific countries – Pakistan, Philippines, India, Thailand and Bangladesh – accounted for 36 percent of the rise in global terrorist incidents between 2004 and 2013, and 97 percent of the increase within Asia-Pacific. While actual incidents of terrorism remain concentrated in a few nations, regional concerns about terrorism are increasing as Islamic State-related attacks and propaganda proliferate. This also leads to increased defence spending.

Asia-Pacific defence budgets increasingly emphasize procurement and research and development, as nations develop indigenous defence industrial bases and pursue advanced defence technology. Procurement and R&D are projected to grow by 29 and 28 percent respectively from 2014 to 2018, reflecting plans for major new acquisitions in most countries in the region.

Procurement Budget Increases by country

Country	% Increase (2014-2018)	Growth Focus
India	25	Develop Industrial base. Land Based systems Artillery and Infantry weapon systems. Air Defence programs
Singapore	18+	Technology Partners
Cambodia	18+	R&D and Industry development focus.
Indonesia	18+	R&D and Industry development focus. Land Based systems
Pakistan	11	Not Publicly published. Based on current requests. Air Defence and Artillery focus
Vietnam	18+	R&D and Industry development focus. Land Based systems and Air Defence
Philippines	85	R&D and Industry development focus. Land Based systems and Air Defence.

By 2018, rapidly-developing Asia-Pacific nations will command more than half of non-US global defence procurement and two-thirds of non-US defence research and development, making the region a key defence market, and a potent force in defence technology innovation and advancement. Therefore, Denel needs to be in this space.

3.2. Strategic Relevance of Asia

Countries such as India, Indonesia, Singapore, Thailand, Vietnam and China are considered to be primary target markets for Denel whilst markets such as the Philippines, Myanmar, Sri Lanka and Bangladesh form secondary target markets.

In analysing the Denel business in the Asia Pacific region, the following emerged to Denel management as barriers to entry into this fast growing market:

- lack of multilateral defence relationships;
- inability to provide funding solutions;
- inability to source local production and development partners (particularly in India);
- frequent engagement with end user and industry from a distance not feasible;
- company visibility in the market place/region from a distance not possible;
- need for a lawful conduit for developing/Aligning with local business networks; and
- active participation in regional initiatives from a distance are not feasible.

3.3. Hong Kong as the Country of Incorporation for a Private Limited Company

The salient business requirements for Hong Kong particularly with respect to undertaking business in this jurisdiction is set out in **paragraph 4** below. In essence, the financial, regulatory and legal requirements are substantially similar to that applicable to companies in South Africa.

4. COMPREHENSIVE DUE DILIGENCE REPORT ON THE FINANCIAL REGULATORY LEGAL REQUIREMENTS AND REGULATORY LAWS GOVERNING FOREIGN OWNED ENTITIES IN HONG KONG

Denel has been advised that:

- Hong Kong is situated in the south-eastern coast of China. With a total area of 1104km^2. The territory comprises Hong Kong Island, Kowloon Peninsula, and the New Territories, which also includes 262 outlying islands.

- Hong Kong became a Special Administration Region of the People's Republic of China on 1 July 1997, after a century and a half of British colonial administration. Under the "one country, two system" policy and constitutional documents, the Basic Law, Hong Kong's existing economic, legal and social systems will be maintained for at least 50 years. Hong Kong does however enjoy a high degree of autonomy except in defence and foreign affairs.

- While the People's Republic of China follows a civil law system, Hong Kong's legal system is based on the traditions of its former colonial master, England. As such, English common law continues to have sway. As in the British system, lawyers are either solicitors (handling paperwork, negotiations, and settlements) or barristers (who can appear in court). The Hong Kong "Basic Law" functions as Hong Kong's constitution, subject to interpretation by the Standing Committee of the National People's Congress.

- The Basic Law of Hong Kong ensures Hong Kong's autonomy in its executive, legislative, and judicial systems, as well as certain foreign relations. It protects freedom of expression, assembly, and religion, forbids torture and unwarranted searches, seizures, and arrest. Furthermore, Hong Kong is ardently capitalist, in spite of Mainland China's (nominal) adherence to socialism.

- Every year since 1995 to about 2013, Hong Kong was voted the world's most free economy by the Heritage Foundation and the Wall Street Journal's Index of Economic Freedom. It also has one of the lowest tax rates in the world. According to studies conducted by PricewaterhouseCoopers and the World Bank Group, Hong Kong is the fourth-easiest place in the world to pay taxes, just behind three countries in the Middle East.

- Hong Kong is ideally located in the heart of Asia and serves as a gateway to and from Mainland China amongst others. These advantages make Hong Kong an attractive place for foreign investors.

- The Companies Ordinance (the **"CO"**) is the main piece of legislation governing companies in Hong Kong.

- Types of Permitted Operations in Hong Kong

  Depending on the scope of operations, foreign companies seeking to operate in Hong Kong have **three** alternative permitted forms of business presence:

  - Representative Office
    A representative office is suitable for a foreign company that intends to conduct only minimal activities in Hong Kong. A representative office cannot conduct any trade, professional, or business activities or transactions in Hong Kong and cannot enter into any contracts in Hong Kong. A representative office is appropriate, for example, for acting as a liaison office without creating any binding business obligations.

  - Branch Office
    If a foreign company establishes a place of business in Hong Kong, it will require registration as a foreign company under the CO. A "place of business" includes a place used by a company to transact any business that creates legal obligations. The foreign company is liable for the debts and liabilities of its Hong Kong branch, and a branch office cannot take full advantage of Hong Kong's tax benefits.

  - Hong Kong Subsidiary
    Due to the limitations of a representative office and branch office as described above, foreign companies usually favour establishing a Hong Kong–incorporated company as a subsidiary to operate in Hong Kong. **This is generally the preferred type of business structure because the entity may be sued only to the extent of the limited assets of the Hong Kong subsidiary**.

- Classification of a Company

  - Under the CO, a "private company" is a company that restricts the right to transfer its shares, prohibits public subscription for its shares or debentures, and limits the number of shareholders to 50. Any company which cannot satisfy all three requirements is a public company. A public company can be listed on a stock exchange or unlisted.

  - A company can also be classified by whether it is limited by shares or by guarantee, or is an unlimited company. We have limited our discussion to a company limited by shares, which is the most common type and is usually referred to as a "limited company." A company limited by guarantee in Hong Kong is usually a non-profit organization.

- The CO makes it clear that there are five types of companies that can be set up under the CO:
  - a public company limited by shares;
  - a private company limited by shares;
  - a public unlimited company with a share capital;
  - a private unlimited company with a share capital; and
  - a company limited by guarantee without a share capital.

- Requirements for a Hong Kong Private Company

  At a minimum, a Hong Kong private limited company must have the following:
  - one shareholder;
  - one director;
  - a company secretary;
  - a registered office address in Hong Kong;
  - an auditor; and
  - a business registration certificate.

- Director
  - A director must be at least 18 years of age, must not be an undischarged bankrupt, must not be subject to a disqualification order, must comply with any share qualification requirement, and must consent to act. There is no restriction on the nationality of a director.
  - A private company can have a director that is a corporation but at least one director must be a natural person.

- Company Secretary

  A company secretary must either be an individual resident in Hong Kong or a company with a registered office or place of business in Hong Kong.

  - Business Registration Certificate
    - A one-stop Company and Business Registration Service has been launched by the Companies Registry and the Inland Revenue Department. Applications for both incorporation and business registration are undertaken simultaneously.
    - In addition to the business registration certificate, certain types of businesses may need additional forms of licensing. For example, a company conducting regulated financial services activity (such as asset management, dealing in securities, or advising on securities) in Hong Kong requires licenses from the Securities and Futures Commission.

  - Generally
    - There is no prescribed minimum paid-up capital. Under the CO, the concept of nominal or authorized share capital and nominal or par value was abolished. Instead, the articles of the company with a share capital must include a statement of capital containing some prescribed information and the initial shareholdings.
    - The same person can be the secretary, director, and shareholder of a company, except that the sole director of a company cannot also be the secretary of the company.

- A company's statutory records must be kept at its registered office. If they are kept at a different place, a notice must be filed with the Companies Registry.
- Under the CO, the articles of association are the sole constitutional document of the company.

- Information Available to the Public
  Compared to other jurisdictions (e.g., the British Virgin Islands and the Cayman Islands), Hong Kong companies are much more transparent in terms of information that is available to the public. In addition to basic information, one can search for all the documents filed with the Companies Registry in relation to a particular company. One can also search for the registered charges (securities in favour of third parties) of a company and disqualification orders made. Moreover, one can search for all the companies in which an individual has directorships and the particulars of that director, such as his or her identity number and residential address.

- Establishing a Private Company

  There are two ways of establishing a private company in Hong Kong which is either by incorporating a new company or buying a shelf (or existing) company.
  - Incorporation involves applying to the Companies Registry, which then issues a certificate of incorporation within four working days after submission of the application by post (online applications may be processed within an hour). The newly incorporated company then needs to be activated by holding its first board meeting and a shareholders' meeting, if necessary.
  - Buying a shelf company is useful when a company is urgently needed. One just needs to acquire a shelf company and then activate it by effecting a change of shareholders and directors and holding a board meeting (and a shareholders' meeting, if necessary).

- Continuing Compliance Requirements
  - A company should hold an annual general meeting (AGM) each year, and not more than 15 months from the previous AGM, unless everything that is required to be done at the meeting is done by written resolution and the relevant documents are provided to each member.
  - The following matters are usually dealt with at the AGM:
    - adoption of audited accounts comprised of the balance sheets, directors' report, and auditors' report;
    - declaration of dividends;
    - election of directors; and
    - appointment of auditors.

  - The CO provides that a company is not required to hold an AGM if it has only one member or the AGM is dispensed with by unanimous members' consent.

  - Other compliance requirements include, among others, the following:
    - a company should keep a register of members and a register of directors and secretaries;
    - various returns have to be filed with the Companies Registry within stipulated deadlines for changes in relation to the company, such as changes in directorship and secretary, registered office, share capital, etc.;
    - a company must file an annual return;
    - a company must have annual audited accounts. The CO prescribes detailed requirements regarding the types of accounts to be prepared. A directors' report must also be prepared in conjunction with the annual accounts;

- shareholders' or board meetings should be held as may be necessary or required under the CO. The minutes or written resolutions should be filed in a minute book and resolutions or notices should be filed with the Companies Registry as required under the CO; and
- a company also needs to renew its business registration certificate before it expires and file profit tax returns for the company and the employer's return for its employees with the Inland Revenue Department.
- If a company fails to comply with these requirements, the company and every officer of the company who is in default may be liable for a fine and/or imprisonment.

- Tax Issues
  - Profits Tax
    - Hong Kong adopts a territorial corporate tax system. Corporations are taxed on profits at a rate of 16.5% percent. Profits tax is charged on Hong Kong–sourced profits and is collected by the Inland Revenue Department. The tax rate on profit derived in Hong Kong is the same for Hong Kong and foreign companies.
    - Specifically, domestic and foreign entities meeting the following three criteria are subject to profits tax:
      - the entity carries on a trade, profession, or business in Hong Kong;
      - the profits are from such trade, profession, or business carried on by the entity in Hong Kong; and
      - the profits arose in, or were derived from, Hong Kong.
    - A Hong Kong resident may derive profits from abroad that are not subject to Hong Kong profits tax; conversely, a non-resident may be liable for tax on profits arising in Hong Kong. The question of whether a business is carried on in Hong Kong and whether profits are derived from Hong Kong is largely one of fact. Profits arising from activities conducted abroad, even if they are remitted into Hong Kong, are not subject to profits tax.
  - General Tax Benefits
    - Dividends or overseas branch profits repatriated to Hong Kong are not subject to Hong Kong tax. In addition, dividends paid by a Hong Kong company to its shareholders are not subject to Hong Kong tax in the hands of shareholders (tax already having been paid by the company on the profits underlying those dividends), nor is there any withholding tax on dividends paid to shareholders outside Hong Kong.
    - Capital gains are also tax-exempt. A stamp duty is imposed on certain documents such as share transfers, leases of real property, and sale of real property. There is no sales tax, value-added tax, or estate tax in Hong Kong.

5. SELECTION OF PARTNERS

With a focus on Asia, Denel's approach is to immediately re-enter the India market through Denel Asia as a way of building a business profile in the region. The details of the India strategy and its rationale are discussed below. The choice of partner has mainly been influenced by the plan to use India as an entry point into the Asia market.

5.1. Denel's History in India

Denel entered the India market during 1994 with a wide range of products. During the period 1998 and 2005, Denel participated in tenders issued by the Indian MOD and was

successfully awarded contracts for various products including ammunition and land systems products.

These contracts were for the supply of ammunition, explosives, anti-materiel rifles, fuses and other munitions components such as base bleeds and modular charge systems totaling circa US$ 282 623 768.00.

Some of these transactions included the transfer of technology for the relevant products sold to the Government of India.

A contract for a significant artillery program for a tracked self-propelled gun resulted in a successful trial being concluded during July 1999 to February 2000 which included the introduction of the G6. The costs of these trials exceeded R500 million. Contract negotiations commenced in February 2003 and were concluded in December 2003 with a contract value of US$ 1,180,744,682.

On 17 April 2005, an article appeared in the Cape Argus newspaper alleging that Denel had contravened specific Indian legislation. Notwithstanding the lack of proof thereof and Denel's denial that it was in breach of the MOD contracts, the MOD issued a notice of termination of the defence programs and instituted legal proceedings against Denel which resulted in, inter alia, protracted arbitrations. Contracts to the value of US$ 77,3 million were adversely affected by these actions. Denel was effectively treated in India as if it were blacklisted notwithstanding no formal blacklisting being in force.

In 2007 Denel sought to re-enter the India market as a subcontractor on a tracked gun program where Rheinmetall was the prime contractor. Successful trials for the gun took place during July 2010 and March 2011. However, in 2012, Rheinmetall was recommended for blacklisting which resulted in a termination of the said program. Denel incurred a further loss of a R11 million as a result of this termination.

This confirmed that Denel competing on its own in India on major programs is very high risk.

Since Denel's absence from the market, the procurement rules changed significantly on major programs. In particular, it introduced the requirement for a local Indian Industry partner/s based on the "Buy Make India" procurement program. This mandatory requirement combined with Denel's previous unsuccessful attempts to access and remain successful in the Indian market reconfirmed the need for Denel to identify and rather proceed with a local partner in India as opposed to its own.

5.2. Buy Make India

The India "Buy Make Program" requires that local content should be more than 50% as well as inclusion of technology transfer from the foreign Original Equipment Manufacturer (OEM).

Denel is positioning itself for major programs in India which programs are premised on the 'Buy Make India' concept. This means that only Indian Companies that can prove that they have partnered with "foreign technology companies" are allowed to bid as prime contractors.

The Indian procurement process demands a strenuous and protracted product evaluation process which can become extremely costly (as detailed in **paragraph 5.1** above and experienced first-hand by Denel).

5.3. India Remains a Lucrative Market

Despite Denel's previous lack of success in the India market, due largely to circumstances outside its control, the Asia Pacific region and specifically the Indian market remains a lucrative market as more fully set out in **paragraph 3.1** above.

5.4. Possible Partners Explored

As detailed in **paragraph 5.1** above, Denel was inactive in the India market for a significant length of time until verbal notification was received late in 2014 from the Indian Embassy in South Africa informing Denel that the investigation was completed and that we may proceed to conduct business in India.

It must be pointed out that the defence industry is a niche market and the norm in this industry is that a competitor can easily become a strategic partner and vice versa depending on the type of opportunity being explored by the parties.

As Denel needed to finalise a partner in light of a Request for Information (RFI) to be issued on the mounted artillery gun program, an industry visit took place during February 2015 wherein Denel visited the following potential business partners. Securing a suitable partner proved to be unsuccessful as most of the potential business partners that Denel considered were already aligned to other companies. For example, Denel considered the following companies:

a) *Bharat Forge*
They have a large forging capability and are a well-established defence contractor. They were however already committed to ELBIT (Israel Company) on artillery programs.

b) *Larsen and Toubro*
They are a well-established defence contractor but were already committed to NEXTER (French company) on artillery programs.

Given the significant changes in the procurement process as well as Denel's previous unsuccessful experiences coupled with our own internal strengths and weaknesses, a decision was taken not to participate in major programs in India unless there was a distinct advantage that presented itself and which would increase the possibility of us successfully participating in the Indian market.

VR Laser presented to Denel, on an unsolicited basis, a value proposition that was worth considering. The value proposition, more fully set out in **paragraph 5.2** below, was attractive to Denel as it was based on VR Laser Asias' experience as well as market studies conducted during the planning phase of re-entry into India. VR Laser Asia's value proposition allows for Denel to enter into the India market as well as the wider Asia Pacific market.

In the past, Denel has incorporated similar joint venture companies in other countries with some of its suppliers as in the case of Tawuzan Dynamics, a joint venture company incorporated in the UAE. Denel has seen and continues to see significant benefits in the incorporation of this joint venture.

Key aspects of the Tawazun Dynamics Joint Venture are, inter alia:

- It is a risk sharing model; and
- Intellectual Property (IP) is licenced in Tawazun Dynamics in order to discharge offset obligations.

5.5. Value proposition of VR Asia

As previously indicated, a decision was initially taken (prior to VR Laser Asias approach) not to re-enter the India market given the informal blacklisting and having not been in the market for a significant length of time.

It is evident that, in order to be successful on any major defence program in the world, there needs to be a balanced strategy which encompasses, inter alia, the following:

(i) A defence solution that supports national objectives
The VR Asia proposition brought an understanding on national objectives at an industry level and industry knowledge in the form of a well-established, highly respected and highly successful India partners being PIPAVAV and the Adani Group. The Adani Group is an Indian multinational conglomerate company. It has a diversified business portfolio covering resources, logistics, agribusiness and energy supply. The company was founded in 1988 as a commodity trading business. The founder and Chairman, Mr Gautam Adani is a well established business man and has vast knowledge of setting up significant programs. Similarly, PIPAVAV is a reputable Indian company which operates in the armament industry with knowledge of the Indian market.

(ii) Compliance to the user specification with a competitive value proposition
The VR Asia proposition at this level is again Industry knowledge, setting up the not so obvious contenders in a business venture. As indicated above, Denel's initial evaluation of possible partners was unsuccessful as the main contenders were already committed or not willing to share the risk. Through, for example, the Adani business partners in India as well as risk sharing by Indian partners such as PIPAVAV during the pre-contracting phase of the program, participation will be possible. The value proposition in the bidding process will be an Indian solution with local content growing new contenders and establishing new technologies as directed by policy.

(iii) A competitive technical solution
The VR Asia proposition at this level is technical skills in VR South Africa as well as operational funding.

5.6. VR Laser Asia as a partner of choice

Denel has thus concluded that VR Laser Asia Limited, a company incorporated in Hong Kong ("**VR Asia**"), and aligned with one of Denel's local fabrication specialists (VR Laser South Africa Proprietary Limited ("**VR RSA**")), as a suitable partner to form a joint venture company. VR RSA, on behalf of VR Asia has presented a suitable business model to Denel for consideration. VR RSA has also undertaken to fund VR Asia in order to enable VR Asia to meet its funding commitments to Denel Asia.

Denel's traditional strength lies in the areas of concept, design, prototyping and weapons integration. In partnering with VR Asia, Denel obtains access to VR RSA's strong capability in industrialisation, production and support of armoured and specialised vehicles.

The advantages of Denel entering the Asia market with VR Asia includes:

- the provision of design, manufacturing and fabrication skills
- a deeper understanding of the local market and industrial landscape
- the ability to align with local business networks
- the provision of quick access to local potential production and development partners
- the ability to increase visibility in the market/region
- access to operational funding

- the ability to grow the business in a sustainable manner
- the ability to share all demonstration costs proportionately to its shareholding

For the above reasons the partnership with VR Asia, who has satisfied Denel that it is familiar with the landscape of Denel's primary and secondary target markets, makes commercial sense.

Further, it makes commercial sense for Denel to establish a footprint in the market. In order to mitigate the costs and risk of a new market entry, Denel management are of the view that a risk sharing model be adopted. This entails that Denel enter into a joint venture with VR Asia to form Denel Asia.

It is reiterated that VR Asia is a partner of choice for Denel for reasons, which include, details as set out in this **paragraph 5**, the unsolicited approach made by VR Asia together with, inter alia, its value proposition and the commercial relationship enjoyed between VR Laser RSA and Denel Land Systems (a Denel entity) which has resulted in mutual trust and recognition between the respective parties.

6. ADVANTAGES OF PARTNERING WITH VR LASER ASIA

6.1. Registration Details and shareholding of VR Laser Asia

The registration details of VR Laser Asia are: **VR LASER ASIA LIMITED**, (Company No. 2111273) whose registered office is at Block A, 15/F, Hillier Comm Building, 65-67 Bonham Strand East, Sheung Wan, Hong Kong.

The sole shareholder of VR Laser Asia Limited is Mr Salim Aziz Essa, a South African national with passport no. M00073786. Mr Essa is via the entity Elgasolve Proprietary Limited, the controlling shareholder of VR Laser South Africa Proprietary Limited.

6.2. Networking Capability Expanded

As mentioned in **paragraph 5.2** above, VR Laser Asia's network includes, but is not limited to, the following reputable Indian businesses:

6.2.1 Adani's Profile

Mr Gautam Adani, the Chairman and Founder of the Adani Group, has more than 33 years of business experience. Under his leadership, Adani Group has emerged as a global integrated infrastructure player with interests across Resources, Logistics and Energy verticals.

Mr Adani's success story is extraordinary in many ways. His journey has been marked by his ambitious and entrepreneurial vision, coupled with great vigour and hard work. This has not only enabled the Group to achieve numerous milestones but also resulted in creation of a robust business model which is contributing towards building sound infrastructure in India.

Quoted from the Chairman message:

"The government's call for 'Make in India' shall get a fillip with a robust infrastructure that is world class and facilitates the manufacturing industry. It is our endeavour to narrow the energy demand and supply gap, build world class ports so that India becomes a shipping hub and operates mines across the globe with environmental concerns addressed most optimally.

We look forward to make inroads into new sectors of infrastructure and aim to excel in all our initiatives."

Adani's Vision

As part of preparing the Group for the next phase of our growth, we have re-formulated our 2020 vision:
"To be a globally admired leader in integrated infrastructure businesses with a deep commitment to nation building. We shall be known for the scale of our ambition, speed of execution and quality of operation."

(Source: Adani website)

6.2.2 PIPAVAV's Profile

Reliance Infrastructure, together with its wholly owned subsidiary Reliance Defence Systems Private Limited, acquired in March 2015, a controlling share from the promoters of Pipavav Defence.

Reliance Infrastructure Limited (RInfra) is amongst the largest Infrastructure Companies in India, developing Special Purpose Vehicles (SPVs) in several high growth sectors within the Infrastructure space.

PIPAVAV Defence is India's first world class company integrated Defence production company. PIPAVAV was the first private sector company to get a license and contracts to build frontline warships for the Indian Navy.

PIPAVAV has strong partnerships with Global players such as:
- SAAB Technology AG, Sweden on technology transfer for the manufacturing of missiles, underwater systems and Aero-structures for fighter jets
- DCNS (France) Government owned company on Naval programs
- Rosoboron Export Russia on Naval programs
- Atlas Electronica on torpedoes and Sonars for the Indian Navy
- Sagem Defence Securite, part of the Sagem Group on long range air borne multi sensor multi spectral electro optical systems

PIPAVAV has been participating in several land system projects such as:
- Upgrade of several vehicle programs such as BMP2 and tank projects
- Manufacturing and supply of Armour Personnel Carriers
- Several UAV programs

Having regard to the fact that Denel has come in as a late entry competitor on the main programs in India, our partnering options were very limited as the traditional partners that Denel could have considered were in most instances already paired with other major industry players (See **paragraph 5.1** above).

In support of Indias' national objective of developing local privately owned defence companies, partnering with (either one or both) Adani and PIPAVAV will bring major advantages in terms of Industry knowledge, manufacturing capability, setting up manufacturing partners, business knowledge and investment capital on major programs. Expanding into the Defence Business forms part of both companies growth vision and both have a history of success.

6.3. Financial Commitment

VR Laser Asia via VR Laser RSA has committed R100 million in terms of a shareholder loan on an arms-length basis with interest (being at normal market rates).

Denel intends to negotiate a higher amount to be paid at the outset and should this be unsuccessful, it will be referred back to the Denel Board.

Should the joint venture be unsuccessful within the first 5 years of incorporation of the company, VR Asia will not have recourse to Denel to repay the loan but shall bear this risk in totality. This is articulated in the Shareholders Agreement.

7. BUSINESS MODELS

As indicated in **paragraph 5,2** above, Denel can best position itself for programs based on the 'Buy Make India' concept. In addition, if there are any similar requirements within the Asia Pacific region, it will be easier to leverage on these opportunities from the India base.

Set out in **paragraph 8** below are the 2 main business / contracting models that may arise from identified opportunities in the Asia Pacific region hereafter referred to as Scenario 1 (No Production Scenario) and Scenario 2 (Production Scenario) respectively.

8. CONTRACTING MODEL

8.1. Joint Venture Governance

In order to implement Denel's chosen risk mitigation strategy, Denel has elected that a new limited liability company be registered in Hong Kong (Denel Asia). This ensures that Denel does not inherit any legacy concerns and ensures a speedier due diligence process.

Notwithstanding the fact that Denel Asia will be incorporated in Hong Kong, Denel has to ensure that Denel Asia will be established and managed in line with its status as a state owned company, reflecting Denel's own corporate governance best practices and standards. In this regard, Denel has negotiated a favourable shareholders' agreement entrenching its rights and providing a contractual framework which will ensure Denel Asia's effective governance.

8.2. Contributions by the Parties

Denel management have recognised that the intended shareholders of Denel Asia have differing strengths and capabilities. In this regard, it is envisaged (and the Denel Asia shareholders' agreement provides) that:

- Denel, will be the technology partner and will hold 51% of the issued share capital and control of Denel Asia. The remaining 49% minority is to be held by VR Asia who will be the networking and industrial partner.
- Other than standard minority protections, Denel as majority shareholder will be able to influence the strategic direction of Denel Asia at a shareholder level as shareholder matters require approval by a simple majority.
- Denel Asia will pursue opportunities in Asia, and, specifically in India using the network of VR Asia. Once an opportunity translates into a firm order:

- Denel Asia may establish a subsidiary in India in order to satisfy Indian legal requirements;
- Denel Asia will pursuant to a preferential supply agreement with Denel, procure product for delivery to an Indian end-consumer; and
- If and to the extent required, VR RSA will contract, manufacture, and produce for Denel Asia for delivery to an Indian end-user.

Subject to relevant approvals, a Shareholders agreement in relation to Denel Asia has been negotiated. The current draft of the shareholders' agreement is attached hereto as **Appendix A**. The Denel Board has considered the same and taken advice thereon. They are satisfied that Denel has adequately protected itself in relation to Denel Asia.

8.3. Transaction Structure

The cooperation agreement referenced in the pre-notification letter to Minister Brown dated 29 October 2015 is to be superseded by the shareholders' agreement. In addition, Denel, VR RSA and VR Asia are to conclude:

- A standard form Denel supply agreement in relation to the supply of product by Denel to Denel Asia, which will entitle Denel Asia (as a subsidiary of Denel) to preferential pricing and procurement status; and
- A contract manufacturing agreement between Denel Asia (as customer) and VR RSA (as supplier) in terms whereof, amongst other things:
  - Denel Asia will appoint VR RSA as its preferred contract manufacturer for specialized vehicles and related products in India;
  - VR RSA will supply specialized vehicles and related products at a preferential price, given its indirect interest via VR Asia; and
  - Denel will make available to VR RSA, certain IP on a limited licensed use basis, to enable VR RSA to manufacture/fabricate product.

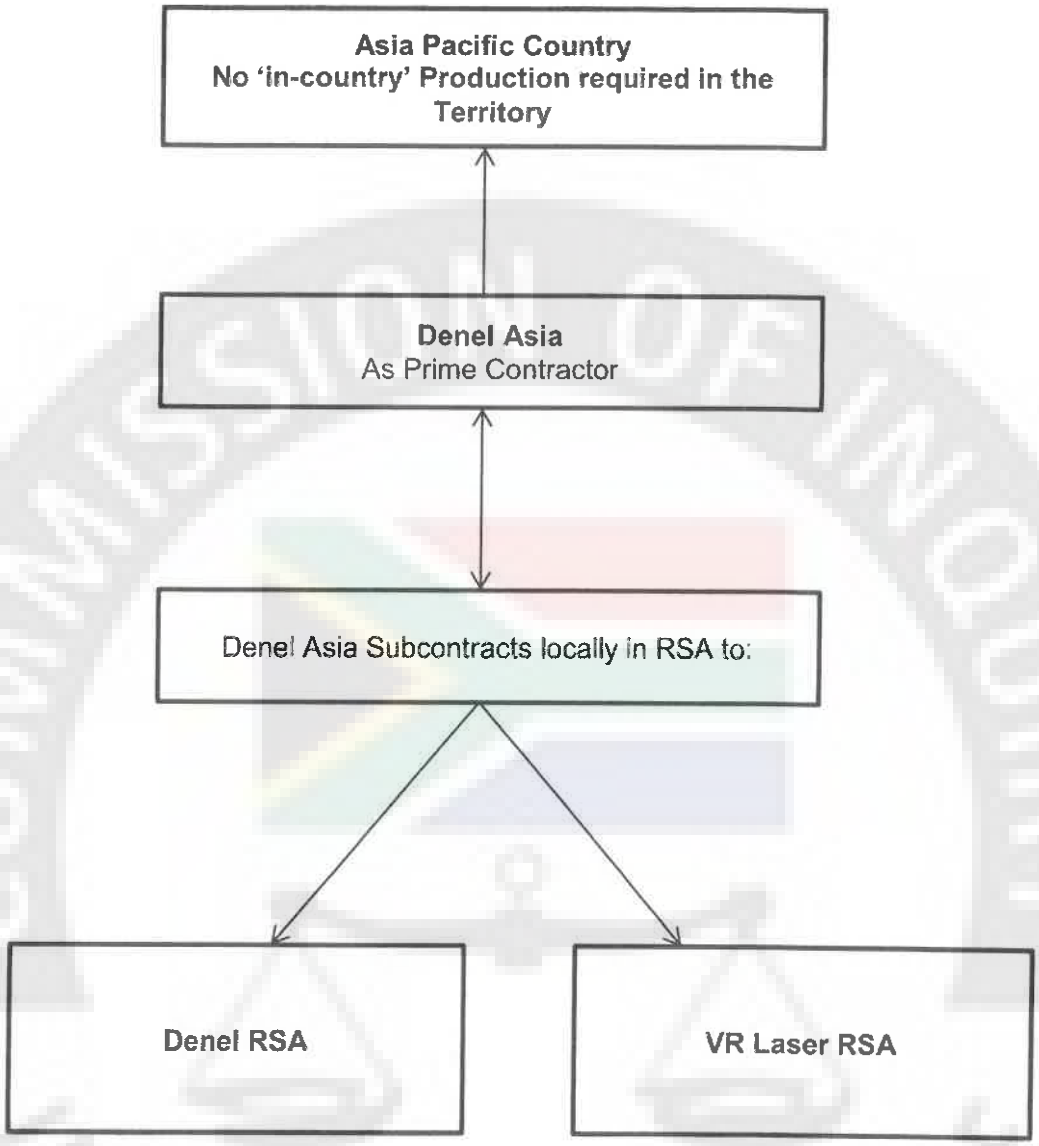
  See **paragraph 12.7** below.

8.4. Schematic representation of the contracting models

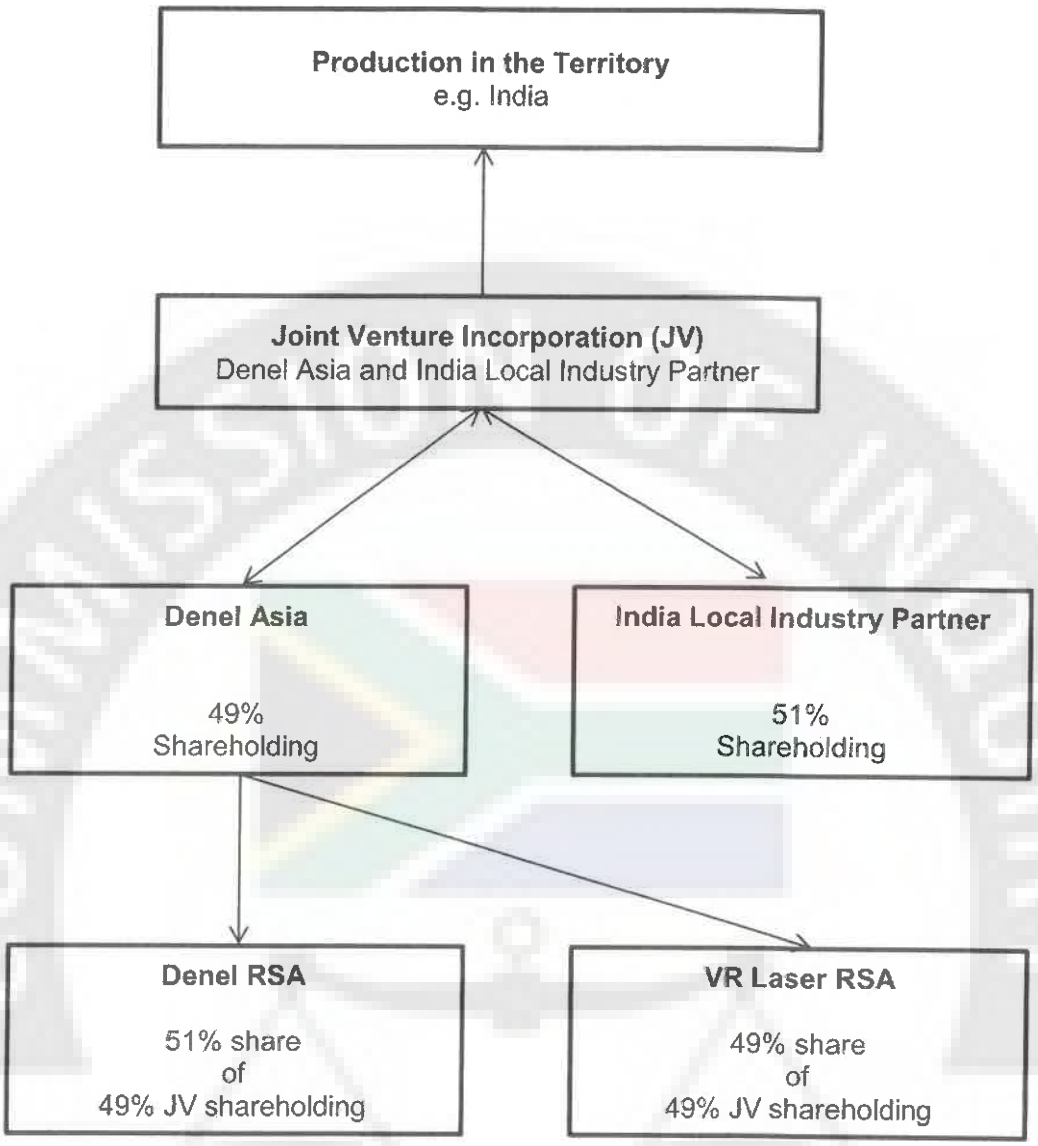
8.4.1 Scenario 1 – No Production envisaged in country

8.4.2 Scenario 2 – In country Production is envisaged

Scenario 1:


Asia Pacific Country
No 'in-country' Production required in the Territory
Denel Asia
As Prime Contractor
Denel Asia Subcontracts locally in RSA to:
Denel RSA
VR Laser RSA

Scenario 2:



(i) It is not envisaged that any production will take place in Hong Kong as this office is essentially a marketing office.

(ii) Tawazun Dynamics conducts business in accordance with Scenario 2 above.

8.5. Financing

One of the key supporting drivers for the formation of Denel Asia, is Denel's limited finance obligations. VR Asia has undertaken to invest an amount of R100 million (One Hundred Million Rand) into Denel Asia for operational costs, payable in amounts of R20 million a year for a period of five years.

Thereafter, Denel Asia will, to the extent that external funding is required, source such funding from third party funders. The shareholders (Denel and VR Asia) will also be able to provide funding by way of shareholder loans pro-rated according to their respective shareholding but they are not obliged to provide funding. Denel does not have any definitive finance obligations or exposure to Denel Asia (save for ordinary supply arrangements).

9. INTELLECTUAL PROPERTY (IP) AND LICENCING

9.1. Technology transfer and protection of Denel's IP

(i) Denel will not alienate its Intellectual Property and technology transfer will be done by way of an applicable licencing agreement between relevant parties.

(ii) Requisite approvals from Armscor and/or a third party will be obtained prior to licencing this IP.

(iii) To the extent that royalties are payable to Armscor and/or any third party, Denel Asia will be required to effect such payment.

(iv) Where Denel is the owner of the IP, there will be no royalty payable by Denel Asia as Denel is the technology partner bringing with it the technology to the joint venture subject to **paragraph 9.1 (i)** above. This is consistent with the Tawazun Dynamics joint venture model referred to in **paragraph 5.7** above.

(v) In instances where Denel cannot be subcontracted by Denel Asia for technology transfer to a local industry company in a specific jurisdiction, Denel Asia will instead be licenced with a right to extend such licence to an identified local industry company.

10. RISKS AND MITIGATION

Key risks were considered during the assessment of the business and relevant risks taken into account in the negotiation process and contractual framework. Appropriate financial and legal due diligence reviews were performed to identify and mitigate any further risks and the recommendations emanating therefrom have and/or will be adopted and implemented. **Appendix B**, **Appendix C** and **Appendix D** refers.

10.1. Transaction risks and its mitigation

	Risks	Mitigation/Remarks
1.	Reputational	• Denel has undertaken a due diligence investigation and the recommendations thereof will be implemented. • No agents will be involved. • Denel has a controlling share and thus can

Risks		Mitigation/Remarks
		control the direction of Denel Asia.
2.	Guarantees/ Finance Risk	• VR Asia is funding Denel Asia in the amount of R100 Million (R20 million a year for 5 years). Denel is to engage with VR Asia to secure a greater cash injection in the first 2 years. Denel previously unsuccessfully engaged with VR Asia on this issue. The Board has requested that a re-engagement with VR Asia on this issue is to take place. • Reduced balance sheet exposure due to partnering. • Denel has limited credit exposure to its subsidiary for normal supply arrangements on preferential terms.
3.	Penalties	• Both Denel and VR Asia, have the skill, expertise and experience to minimise the possibility of penalties being incurred.
4.	Legal Exposure	• Denel exposure is seen by the Denel board as limited.
5.	PFMA Conditions	• Denel will ensure that Denel Asia abides, to the extent applicable to the PFMA, the Denel Shareholder Compact and the Denel Risk and Compliance Frameworks. • Adherence to all shareholder conditions prior to Shareholders Agreement and ancillary agreements.
6.	Cooperation Agreement	• The Shareholders Agreement, once signed, will supersede the Cooperation Agreement (**Appendix E**).
7.	Protection afforded in terms of the Shareholder Agreement	• The agreement only becomes effective upon the fulfilment of the suspensive conditions (Clause 4). • Control vests in Denel which has a 51% shareholding (Clause 5). • There are certain reserved matters which require a 75% majority vote with other

Risks		Mitigation/Remarks
		matters requiring a simple majority of 51% in order for the resolution to be passed (Annexure B for reserved matters). • There is specific provision for the implementation of anti-bribery, anti-money laundering and anti-corruption policies in the joint venture (Clause 6). • In the event of the joint venture being wound up/dissolved prior to full repayment of the shareholders loan, no liability will accrue to Denel to settle the loan (Clause 16.2). • Denel has the right to investigate the directors and ultimate beneficiaries and shareholders of VR Asia to ensure that such persons have sufficient standing and if not satisfied, Denel has the right to demand that VR Asia repurchases the shares from that person thereby removing the person from being a shareholder of VR Asia (Clause 18.3). • The termination clause (Clause 21) relates to termination on material breach (as opposed to termination for convenience). • Provision is made for termination in circumstances where the Government directs that Denel ceases to be a shareholder for reasons of national security or otherwise (Clause 25.1) • Termination can take place by mutual agreement (Clause 25.1.3). • Termination can also take place where a party frustrates the performance of the other party by making performance impossible or unreasonably expensive or difficult, materially alters the rights and obligations of the parties or materially interferes with the benefits (Clause 25.1.4).
8.	Exit Clause: Termination for convenience	• Initial discussions with VR Asia resulted in a rejection of a clause for termination for convenience. • Denel is to engage with VR Asia and address the Board's requirement that such a clause is to be included in the agreement.
9.	Due Diligence	• The key risk identified is the potential for bribery and corruption. This is alleviated in the shareholders agreement by the obligation to abide by anti-money laundering (AML) and anti-bribery and anti-corruption (ABC) policies. • Financial viability of VR Laser Asia raising the loan – in the absence of the loan being furnished by VR Asia to the joint venture, it

Risks		Mitigation/Remarks
		will constitute a material breach and is a ground for termination. • Denel is satisfied that the loan can be legitimately be raised by VR Laser Asia via its shareholders.
10.	Double Taxation Agreement	• There are currently discussions between India and Hong Kong re a double tax agreement. • The risk of the lack of a double taxation agreement is outweighed by the lucrative opportunities that can be realised in India.

11. DUE DILIGENCE

Denel had procured that a due diligence investigation be undertaken in respect of each of the following areas, which due diligence reports are attached hereto as follows:

1. Regulatory Due Diligence – **Appendix B**
2. Legal Due Diligence – **Appendix B and Appendix C**
3. Financial Due Diligence – **Appendix D**

There were some findings of concern that was raised by the due diligence which are acknowledged. Denel management is however confident that it is able to incorporate the recommendations of the report and will adopt corrective measures in particular related to an anti-corruption policy and compliance framework coupled with rigorous monitoring thereto. See **paragraph 10.1** above.

In addition, Denel is satisfied that the shareholder loan can be legitimately raised by VR Laser Asia via its shareholders failing which the breach provision in the Shareholder Agreement will be invoked.

12. FINANCIALS

12.1. Capital Contribution

There will be a capital contribution of 1000 shares issued at USD 1 with Denel taking up 590 shares and VR Laser Asia taking up 490 shares.

12.2. Financial viability

The formation of Denel Asia in the region is opportune as it resolves many challenges that prevent Denel taking advantage of the current regional opportunities. It will also provide solutions to challenges that Denel faces at the moment i.e. to provide funding solutions.

Initially potential business amounting to USD 9,2 billion was identified. This has been tested and evaluated again and based on a realistic probability matrix on the latest marketing intelligence, the potential business is approximately USD 5.8 billion over the next 5 years which Denel could take advantage of (See **paragraph 12.3** below).

12.3. Markets and Opportunities

Denel Asia's forecasted capabilities and market interests are promising.

The business opportunity at a reduced risk via partnering constitutes a logical next step by Denel for entry into a new market. See **Appendix F** which sets out markets and opportunities.

12.4. Income Statement

R'm	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25
Sales	0	587	900	1,543	3,087	4,372	6,013	7,025	7,500
Gross Profit	0	117	180	309	617	874	1,203	1,405	1,500
Gross Profit %	0	20	20	20	20	20	20	20	20
Operational Cost	11	14	19	22	27	35	35	35	35
Labour	6	8	12	15	20	25	25	25	25
Marketing	3	4	4	4	4	5	5	5	5
Overheads	2	2	3	3	3	5	5	5	5
Additional Operating Cost to Cover Business Growth	50	46	54	55	127	184	266	316	340
Profit before Interest / Tax / Dividends	(61)	57	107	232	463	655	902	1,054	1,125

Notes

[1] The rate of exchange used was R12.50/USD.

[2] The normal yearly operational costs consist mainly of salaries for the office personnel and will increase as more resources are needed to do project management and marketing.

The marketing costs would mainly be for travel and accommodation and direct marketing in the different countries where the opportunities lies.

The operational overheads will be to rent space and equipped the office with the necessary resources to operate effectively. The IT costs will be typically be part of this.

This calculation is based on foreign offices cost structures that are managed by Denel over a very long term.

[3] The additional operating costs would mainly be used to do big system demonstrations to the potential clients. Any one big full in client country demonstrations could cost between R10m – R20m. This is based on various system demonstrations done in foreign countries.

12.5. Business Funding

Denel is satisfied that it has limited financial exposure in terms of Denel Asia due to the fact that VR Asia will be assuming the primary finance obligations of Denel Asia. Forecasted cash flows are in the view of Denel management sufficient to meet Denel Asia's obligation to VR Asia, which is without recourse to Denel.

(i) The R100m investment from the Denel partner will fund the basic office operational costs for the first few years until sales are realised. The sales from operations will cover the direct cost and increased operational costs associated with the business case.

(ii) The R100m investment will be a preferential and secured loan, which will be re-paid to the partner before any future profit sharing takes place.

(iii) No substantial capital spend will be incurred before an order is obtained and the capital investment will be recovered on the orders obtained.

12.6. Cash Flow Impact

(i) The cash shortfall in the first year would have to be financed from either a 12 month short term loan at reasonable international rates negotiate with the partner. Subsequently, the business would be self-funding and sustainable over the medium to long term.

R'm	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25
Nett Operating Cash	(61)	57	107	232	463	655	902	1,054	1,125
Investment Capital	20	20	20	20	20				
Nett	(41)	77	127	252	483	655	902	1,054	1,125

12.7. Pricing Policy

(i) There is currently a Memorandum of Agreement that specifies rates which were negotiated and agreed between VR Laser RSA and Denel Land Systems (a trading division of Denel) which provides a basis to the pricing.

(ii) **Paragraph 8.3** above refers.

13. BENEFITS

13.1. Local Manufacturing Development

By concluding a contract manufacturing agreement with VR RSA (an established provider to Denel), Denel Asia ensures the sustainability of local manufacturing expertise.

13.2. Skills Development

Due to the technological partnering between Denel, Denel Asia and VR RSA, Denel serves its obligation and desire of fostering the development of core skills and technology competencies with black owned and/or black controlled South African entities. A proposition that satisfies a number of key Denel policies.

13.3. Job Creation

By facilitating a black owned and/or controlled South African company (VR RSA), Denel Asia seeks to maintain South African jobs in the skilled and semi-skilled industry sectors. In addition, based on the projected income, significant work will result from Denel Asia contracting with both Denel and VR RSA.

13.4. Human Capital Development / Transformation

We refer the Honourable Minister to our comments contained in **paragraphs 13.1**13.1 and **13.2** above.

14. CONCLUSION

Asia is one of the fastest growing defence markets. Of the top ten worldwide defence importers in 2014, four were from Asia (India, China, Indonesia and Vietnam) with Singapore and Pakistan making 11 and 12 slots respectively. (Stockholm International Peace Research).

The formation of Denel Asia in the region is opportune as it resolves many challenges that prevent Denel taking advantage of the current regional opportunities. It will also provide solutions to challenges that Denel faces at the moment i.e. provide funding solutions.

15. IMPLEMENTATION PLAN

The following activities will take place towards contract implementation and the establishment of Denel Asia:

Action	Timeline
Negotiation and conclusion of the shareholders agreement	Draft shareholder agreement has been agreed to in principle and awaits Ministerial approval.
Establishment of the Joint Venture Company • PFMA pre-notification	Delivered on 30 October 2015
• Draft Shareholders Agreement • Regulatory due diligence, Legal and Financial due diligence • Denel Board Approval • PFMA submission • PFMA Approval expected	Circulated herewith Completed as at 27 November 2015 7 December 2015 10 December 2015 January 2016
Approval from the financial surveillance department of the RSA Reserve Bank for establishing a subsidiary outside the common monetary jurisdiction	January 2016
Conclusion of final shareholders agreement and adoption of memorandum of incorporation.	January 2016
Joint Venture Company business activation and procuring all relevant approvals and/or registrations	January / February 2016

RECOMMENDATION

It is requested that the Honourable Minister notes and approves of Denel's intention to:

1. establish Denel Asia as joint venture company in Hong Kong which company will facilitate the legitimate securing of contracts in the Asia-Pacific region; and

2. establish any further joint ventures, particularly within the India market, to ensure the successful execution of the contracts placed on Denel Asia.

The Denel Board has approved of such establishment subject to the receipt of Ministerial approval in terms of section 51(1)(g), section 54(1) and 54 (2) of the PFMA.

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COMMISSION OF INQUIRY INTO STATE CAPTURE

LIST OF QUERIES RE PRE-NOTIFICATION LETTER

Denel's responses to the specific queries raised by the Honourable Minister has been addressed in the preceding business case. For the sake of completeness, the queries and the paragraph references in the business case to our responses are set out below.

RESPONSES TO SPECIFIC QUERIES

In response to the Honourable Minister Brown's specific queries as contained in her letter to Denel SOC Limited ("**Denel**"), dated 23 November 2015, we advise as follows:

1. **Comprehensive detailed business case:**
   Paragraphs 1 to 14 refers.

2. **Comprehensive due diligence report on the financial regulatory legal requirements and regulatory laws governing foreign owned entities in Hong Kong:**
   Paragraph 4 refers.

3. **Funding Plans and Transaction Documents:**
   Paragraph 12 refers.

4. **Process followed to select VR Laser as partner of choice:**
   Paragraph 5 refers.

5. **Proposed structure of new subsidiary limited liability company in Hong Kong, to be known as "Denel Asia SOC Limited" ("Denel Asia"):**
   Paragraph 8.2 above refers.

6. **Comprehensive Due Diligence of VR Laser:**
   Paragraph 11 refers.

7. **Registration Details of the company and shareholding of VR Laser Asia:**
   Paragraph 6.1 refers.

8. **The reasons for Continent Specific vs Country Specific Arrangement and preference for Hong Kong:**
   Paragraph 2.3 refers.

9. **Studies undertaken by Denel to establish VR Laser as a suitable Partner:**
   Paragraphs 5 and 6 refers.

10. **Reasons why this transaction is not proposed in the 2015/2016 Corporate Plan:**
    Paragraph 2.1 refers.

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DENEL

APPENDICES TO APPLICATION IN TERMS OF SECTION 54 (2) OF THE PFMA

RE FORMATION OF OFFSHORE JOINT VENTURE COMPANY: DENEL ASIA

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DENEL SOC LTD

and

VR LASER ASIA LIMITED

SUBSCRIPTION AND SHAREHOLDERS' AGREEMENT

with and relating to

DENEL ASIA CO. LTD.

Deacons

5th Floor

Alexandra House

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Hong Kong

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COMMISSION OF INQUIRY INTO STATE CAPTURE

SUBSCRIPTION AND SHAREHOLDERS' AGREEMENT dated 2015

1. **PARTIES**

1.1. **DENEL SOC LTD**, a state-owned company incorporated under the laws of RSA (Registration No. 1992/01337/30) whose registered office is at Nellmapius Drive, Irene, Centurion, 0046, Gauteng Province, RSA ("**Denel**"); and

1.2. **VR LASER ASIA LIMITED**, a private company incorporated under the laws of Hong Kong (Company No. 2111273) whose registered office is at Block A, 15/F, Hillier Comm Building, 65-67 Bonham Strand East, Sheung Wan, Hong Kong ("**VR Asia**"); and

1.3. **DENEL ASIA SOC CO. LTD.**, a private company intended to be incorporated under the laws of Hong Kong whose registered office is intended to be at [5th Floor, Alexandra House, 18 Chater Road, Hong Kong], Hong Kong ("**Company**").

The Company, Denel and VR Asia shall be collectively referred to as "**Parties**", and individually as a "**Party**" as the context may require.

2. **INTRODUCTION**

2.1. Denel is a state-owned company incorporated to carry on the business of supplying the RSA defence and security environment, with strategic technology capability, products, services and support, including exporting to key international markets. It offers turn-key solutions for defence equipment to its clients by designing, developing, integrating and supporting, *inter alia*, artillery, munitions, missiles, aerostructures, aircraft maintenance, unmanned aerial vehicle systems and optical payloads based on high-end technology.

2.2. VR Asia has the capability of procuring skills and know-how in steel processing via its associate entity VR RSA. VR RSA provides unique solutions for the defence industry and vehicle protection which includes, inter alia, laser cutting, armour works, fabrication, machining related to such fabrication and integration which services are supported by the latest technology. VR Asia understands the international fabrication market and industrial landscape well. VR Asia has an established network of potential business sources in Asia and in India in particular, which continues to expand. VR Asia shall procure that VR RSA assists the Company in relation to the Business (as defined below).

2.3. The Parties have identified Asia (in particular India) as a key strategic region for cooperation between the Parties and are interested in co-operating with each other

to, *inter alia*, support the requirements of key local and/or international clients and prospective clients in this region.

2.4. For that purpose, the Parties wish to establish the Company as a joint venture offshore private company in Hong Kong in accordance with the provisions of this Agreement and the laws of Hong Kong for undertaking the Business (as defined herein). In this regard, as soon as possible after the Signature Date, the Parties shall using their respective commercial efforts procure the incorporation of the Company and once so incorporated, the Company undertaking to be bound by the provisions of this Agreement.

2.5. This Agreement is entered into amongst the Parties for the purpose of recording the terms and conditions upon which the Parties are to procure the incorporation of the Company (to the extent not already done), investing in the Company and regulating the relationship between the Parties as amongst themselves and their interests in the Company and the conduct of the Business.

3. DEFINITIONS AND INTERPRETATION

3.1. **Definitions:** In this Agreement, the following expressions shall have the following meanings unless the context otherwise requires:

3.1.1. "**Affiliate**" means (i) with respect to any legal entity, another entity that, directly or indirectly through one or more intermediaries, Controls, is Controlled by or is under common Control with such entity, and (ii) with respect to any natural person, any of his Associates;

3.1.2. "**Agreed Proportion(s)**" means the following proportion in respect of the respective shareholdings of each Shareholder in the capital of the Company expressed as a percentage of the total issued share capital of the Company, initially being:

3.1.2.1. Denel: 51%; and

3.1.2.2. VR Asia: 49%;

3.1.3. "**Agreement**" means this Subscription and Shareholders Agreement (as it may be amended in writing from time to time);

3.1.4. "**Applicable Law**" means the common-law, any state enactment or law, by-laws, statutes, rules, regulations, subordinate legislation, orders, ordinances, notices, notifications, directions, restrictions, judgments, decrees, circulars, decisions or other requirements or directives of any

governmental authority in Hong Kong, including (without limitation) the Companies Ordinance as well as any international, federal or state protocols, policies, codes, standards and/or resolutions which have the force of law whether in Hong Kong or the RSA, or such other jurisdiction in which the Company undertakes its Business;

3.1.5. **"Approval(s) Framework"** means an approval framework established by the Shareholders from time to time for purposes of determining the powers and authority of the Board in relation to the management of the Company. The initial such framework is attached hereto marked **Annexure D**;

3.1.6. **"Articles"** means the articles of association of the Company in effect from time to time;

3.1.7. **"Associates"** in relation to an individual means his spouse and children and any of his parents and grandparents, his brothers and sisters, and the spouses and children of his brothers and sisters (collectively **"relatives"**) and any company or trust (wheresoever registered and/or incorporated) which is directly or indirectly Controlled by such individual or any of his relatives and for the purpose of this definition a trust is Controlled by one or more persons if his or their wishes shall generally be adhered to by the relevant trustees and **"children"** (when used above) shall include the spouses and children (natural or adopted) of such children;

3.1.8. **"Anti-Bribery Laws"**: means in respect of each jurisdiction in which the Company conducts its business and/or has a registered office, any and all Applicable Laws which relate to and/or regulate anti-bribery and/or anti-corruption, and to the extent applicable also means without limitation, the:

3.1.8.1. United States' Foreign Corrupt Practices Act of 1977, as amended;

3.1.8.2. United Kingdom's Bribery Act, 2010 (Chapter 23), as amended;

3.1.8.3. the Prevention of Bribery Ordinance (Ch. 201); and

3.1.8.4. India's Prevention of Corruption Act, 1988 (Act No. 49 of 1988),

applying concurrently;

3.1.9. "**Auditors**" means such auditors of the Company as the Company may appoint from time to time pursuant to and in accordance with the Companies Ordinance;

3.1.10. "**Board**" means the board of Directors as constituted from time to time;

3.1.11. "**Budget**" means the budget adopted under Clause 14.1;

3.1.12. "**Business**" means the business of the Company (including that of any subsidiary) as described in clause 5.9 and **Annexure A**;

3.1.13. "**Business Day**" means a day, other than a Saturday or Sunday, on which banks are generally open for banking business in Hong Kong;

3.1.14. "**Business Plan**" means a detailed business plan of the Company for carrying on the Business that is adopted from time to time in accordance with Clause 14.2;

3.1.15. "**Commercially Reasonable Efforts**" means at the relevant time in question, and from time to time, during the term hereof, taking such reasonable steps and performing such conduct in good faith and such a manner as a well-managed for-profit company would undertake or perform implementing good industry practice where such company was acting in a determined, prudent and reasonable manner that will probably achieve the particular result for its own benefit; provided that this obligation shall not be construed to require a Party to:

3.1.15.1. undertake any conduct other than that which a prudent, determined and reasonable person, acting in his own interests and desiring to achieve that result, would take;

3.1.15.2. undertake any litigation or appeal against a decision;

3.1.15.3. breach any fiduciary duty or contravene any Applicable Law; and

3.1.15.4. undertake conduct that would be objectively unreasonable in all the circumstances then present,

and shall be limited to take into account the respective financial and/or commercial benefits contained in and risk herein undertaken;

3.1.16. **"Companies Ordinance"** means the Companies Ordinance (Chapter 622 of the Laws of Hong Kong);

3.1.17. "**Control**" means:

3.1.17.1. the power (whether directly or indirectly and whether by the ownership of share capital, the possession of voting power, contractually or otherwise) to appoint and/or remove all or such of the members of the board of directors or other governing body of an entity or partnership as are able to cast a majority of the votes capable of being cast by the members of that board or body on all, or substantially all, matters, or otherwise to control or have the power to control the policies and affairs of that person; and/or

3.1.17.2. the holding and/or the possession of the beneficial interest in and/or the ability to exercise the voting rights applicable to shares or other securities in any person which confer in aggregate on the holders thereof more than 50% of the total voting rights exercisable at general meetings of that person on all, or substantially all, matters;

3.1.18. "**Conflict of Interest**" means a set of circumstances that creates a risk that professional judgment or actions regarding a primary interest of the Company will be influenced by a secondary interest of a Director;

3.1.19. "**Deed of Adherence**" means the deed of adherence substantially in the form set out in **Annexure C**;

3.1.20. **"Directors"** means directors of the Company as contemplated in the Companies Ordinance and **"Director"** shall be construed accordingly;

3.1.21. "**Dispose**" includes, in relation to any asset, sell, transfer, assign, create a trust or option over, or alienate the right to exercise the vote attached to, pledge, hypothecate, or otherwise Encumber, the legal or beneficial ownership of such asset and "**Disposal**" shall be construed accordingly;

3.1.22. **"Encumbrance"** means a debenture, mortgage, charge, pledge, lien, option, restriction, hypothecation, assignment, right to acquire or of pre-emption, third-party right or interest, other encumbrance, priority or security interest of any kind, or any other type of preferential arrangement (including, without limitation, a title transfer or retention

arrangement) having similar effect, and any agreement or obligation to create or grant any of the aforesaid and **"Encumber"** shall be construed accordingly;

3.1.23. **"Financial Statements"** means the financial statements referred to in Clause 15;

3.1.24. **"Financial Year"** means each period of twelve (12) months commencing on 1 April and ending on 31 March of a calendar year or such other period as the Directors may determine;

3.1.25. **"HK dollars"** or **"HK$"** means the lawful currency of Hong Kong.

3.1.26. **"Hong Kong"** means the Hong Kong Special Administrative Region of the People's Republic of China;

3.1.27. **"HK IFRS"** means International Financial Reporting Standards as published from time to time by the International Accounting Standards Board as practiced and applied in Hong Kong, also known as Hong Kong Financial Reporting Standards as applied by the Hong Kong Institute of Certified Public Accountants;

3.1.28. **"Interest(ed)"** for the purposes hereof, means where a Director is interested in a transaction to which the Company is a party, being where that Director (directly or indirectly) -

3.1.28.1. is a party to, or shall or may derive a material financial benefit from, the transaction;

3.1.28.2. has a material financial interest in or with an Affiliate or another party to the transaction;

3.1.28.3. is a director, officer, or trustee of and Affiliate or another party to, or person who shall or may derive a material financial benefit from, the transaction, not being a party or person that is -

3.1.28.3.1. the Company's holding company;

3.1.28.3.2. a subsidiary of the Company; or

3.1.28.3.3. a wholly-owned subsidiary of a holding company of which the Company is also a subsidiary;

3.1.28.4. is the relative of another party to, or person who shall or may derive a material financial benefit from, the transaction; or

3.1.28.5. is otherwise directly or indirectly materially interested in the transaction in question;

3.1.29. "**material**" for the purposes of this Agreement means with respect to a given Party, a level of significance that would have affected any decision of a reasonable person in such Party's position regarding whether or not to enter into this Agreement, or to implement the terms hereof, being in particular:

3.1.29.1. a matter, cost, obligation or liability of more than a gross amount of $100,000.00 (one hundred thousand United States Dollars); or

3.1.29.2. any series of events that, in aggregate, exceed the materiality quantum referred to in clause 3.1.29.1;

3.1.30. "**OFAC**" means the United States of America's national department of treasury, acting via its Office of Foreign Assets Control;

3.1.31. "**PEP**" means a politically exposed person being an individual (or a relative of such an individual) who is or has, at any time in the preceding Financial Year in question, been charged or entrusted with a prominent public function by either (i) the Government of the country in which any member of the Denel group of companies conducts business, (ii) a political party or public body in the jurisdiction in which the Company or its subsidiary conducts the Business, or (iii) an international body;

3.1.32. "**RSA**" means the Republic of South Africa;

3.1.33. "**Reserved Matter Approval(s)**" means a decision in relation to a reserved matter (as contemplated in the Articles and/or this Agreement in **Annexure B**) which requires the prior written affirmative approval of 75% (seventy five percent) of the Shareholders, prior to the Company undertaking the same, whether obtained in general meeting by the Shareholders represented in person or by proxy or by way of approval of all Shareholders entitled to vote by way of written resolutions;

3.1.34. "**Sanctioned Entity**" means any person, entity or country that:

3.1.34.1. is listed in the OFAC list; or

3.1.34.2. is listed on the SDN List; or

3.1.34.3. is subject to OFAC sanctions; or

3.1.34.4. is listed on the World Bank List; or

3.1.34.5. is a PEP; or

3.1.34.6. is listed on the United Nations sanctions list, which list can be found at www.un.org/terrorism, or any successor website, domain or location. It is recorded that such sanctions programs include as at the Signature Date, but are not limited to, Security Council Resolutions 751 (1992), 1267 (1999), 1518 (2003), 1521 (2003), 1533 (2004), 1572 (2004), 1591 (2005), 1718 (2006), 1737 (2006), 1970 (2011), 1988 (2011); or

3.1.34.7. is listed on the European Union's sanctions list which would include but are not limited to Common Positions 2001/931/CFSP and/or 2002/402/CSFP as found at the domain http://eeas.europa.eu/cfsp/sanctions/consol-list_en.htm or any successor website, domain or location;

3.1.34.8. is listed as being subject to sanctions issued by the United Kingdom (as currently set forth in the list situated at the domain https://www.gov.uk/publications/financial-sanctions-consolidated-list-of-targets), or any successor website, domain or location;

3.1.35. **"Signature Date"** means the date on which this Agreement is signed by the last Party to do so;

3.1.36. **"Secretary"** means the company secretary of the Company as the Company may appoint from time to time;

3.1.37. **"Shareholder"** means Denel and VR Asia (for so long as they shall respectively hold any Shares) and any other person from time to time holding any Shares as a consequence of a transfer or issue thereof and **"Shareholder"** shall be construed accordingly;

3.1.38. **"Shareholders' Loan(s)"** means loans made to the Company by the Shareholders (including the VR Asia Loans) and, where the context shall so require, the outstanding amount thereof;

3.1.39. **"Shares"** means ordinary shares in the capital of the Company and **"Share"** shall be construed accordingly;

3.1.40. **"South African Rand"** or **"ZAR"** means the lawful currency of the RSA;

3.1.41. **"SDN List"** means collectively (i) the Specially Designated Nationals (SDN) and Blocked Persons List, (ii) the Control List, and (iii) the List of Sanctions Programs and Country Information, being lists administered and published, from time to time, by OFAC which lists individuals and entities with whom United States' citizens and permanent residents of the United States of America are prohibited from doing business;

3.1.42. **"Territory"** means those territories which are unanimously agreed to in writing by the Shareholders where the Company (or its subsdiary/ies) shall conduct the Business, which shall initially include India and such other countries and opportunities as may be agreed in writing;

3.1.43. **"VR Asia Loans"** means the loans made to the Company (as debtor) in accordance with Clause 17; and

3.1.44. **"World Bank List"** means the World Bank's listing of ineligible firms, being a list, as updated from time to time, of persons or entities ineligible to be awarded a World Bank Group-financed contract or otherwise sanctioned by the World Bank Group sanctions board for the periods indicated on that list because they were found to have violated the fraud and corruption provisions of the World Bank Group anti-corruption guidelines and policies. For ease of reference it is recorded that the current list as at the Signature Date may be found at http://www.worldbank.org/debarr or any successor website, domain or location.

3.2. **References:** In this Agreement, unless the context otherwise requires, any reference to:

3.2.1. a Clause, Sub-clause, Annexure or Schedule is a reference to a clause or sub-clause of, annexure or schedule to this Agreement;

3.2.2. any ordinance, regulation or other statutory provision or enactment is a reference to such ordinance, regulation, statutory provision or enactment as amended, modified, consolidated, codified, re-enacted, or extended from time to time and includes subsidiary legislation made thereunder;

3.2.3. a "**company**" is a reference to a body corporate (wherever incorporated);

3.2.4. a "**person**" includes a reference to a company, unincorporated association, partnership, firm, institution and trustee and includes a reference to that person's or party's legal personal representatives and successors;

3.2.5. an "**agreement**" includes any document or deed, an arrangement and any other kind of commitment that is reduced to writing and signed by the Parties, it being agreed that for purposes hereof data messages are excluded;

3.2.6. a "**right**" includes a power, a remedy and discretion; and

3.2.7. a "**holding company**" or "**subsidiary**" shall have the same meaning herein as is ascribed thereto and defined in section 13 and section 15 of the Companies Ordinance.

3.3. **Headings and Contents:** The headings and table of contents in this Agreement are for ease of reference only and shall not affect the interpretation or construction of this Agreement.

3.4. **Schedules:** The Annexures and Schedules form part of this Agreement.

3.5. **Construction:** In construing this Agreement:

3.5.1. general words shall not be given a restrictive meaning by particular examples intended to be embraced by the general words, and where the word "including" appears in any statement, it shall be deemed to be immediately followed by the words "without limitation";

3.5.2. words denoting the singular include the plural and vice versa;

3.5.3. words denoting one gender include all genders;

3.5.4. when any number of days is prescribed in this Agreement, same shall be reckoned exclusively of the first and inclusively of the last day unless the last day falls on a day which is not a Business Day, in which case the last day shall be the next succeeding day which is a Business Day;

3.5.5. if figures are referred to in numerals and in words and if there is any conflict between the two, the numerals shall prevail;

3.5.6. words and expressions defined:

3.5.6.1. in this Agreement shall bear the same meanings in schedules or annexures to this Agreement which do not themselves contain their own conflicting definitions; and

3.5.6.2. in the Companies Ordinance shall bear the same meanings herein save as otherwise defined in this Agreement;

3.5.7. the use of any expression in this Agreement covering a process available under Hong Kong law such as a winding-up shall, if any of the Parties is subject to the law of any other jurisdiction, be construed as including any equivalent or analogous proceedings under the law of such defined jurisdiction;

3.5.8. if any term is defined within the context of any particular Clause in this Agreement, the term so defined, unless it is clear from the Clause in question that the term so defined has limited application to the relevant Clause, shall bear the meaning ascribed to it for all purposes in terms of this Agreement, notwithstanding that that term has not been defined in this interpretation clause;

3.5.9. the expiration or termination of this Agreement shall not affect such of the provisions of this Agreement as expressly provide that they will operate after any such expiration or termination or which of necessity must continue to have effect after such expiration or termination, notwithstanding that the clauses themselves do not expressly provide for this;

3.5.10. the rule of construction that a contract shall be interpreted against the party responsible for the drafting or preparation of the contract, shall not apply; and

3.5.11. any reference in this Agreement to a Party shall include a reference to that Party's assigns expressly permitted under this Agreement and, if such Party is liquidated or sequestrated, be applicable also to and binding upon that Party's liquidator or trustee, as the case may be.

4. SUSPENSIVE CONDITIONS

4.1. This entire Agreement save for Clause 1, 2, this Clause 4, and Clauses 28 to 32 (both inclusive) ("**Immediately Operative Provisions**") which are binding on the Parties with effect from the Signature Date, is subject to the fulfilment of the following suspensive

conditions on or before 1 June 2016 after the Signature Date, (or such later date as may be agreed by Denel and VR Asia in writing) that:

4.1.1. VR Asia's board of directors authorise(ing) the execution and implementation of this Agreement;

4.1.2. Denel's board of directors authorise(ing) the execution and implementation of this Agreement;

4.1.3. Denel obtaining the relevant approvals required of it in terms of sections 51(1)(g), 54(2) and 66 of the RSA Public Finance Management Act, 1999 (Act No. 1 of 1999) ("**PFMA**");

4.1.4. Denel obtaining the relevant approvals required of it from the RSA National Treasury for the execution and implementation of this Agreement;

4.1.5. Denel obtaining the relevant approval/s from the Financial Surveillance department of the South African Reserve Bank authorising Denel to acquire an equity interest in the Company; and

4.1.6. the Company obtaining all such approvals as it may require in terms of the RSA National Conventional Arms Control Act, 2002 (Act No. 41 of 2002) in order to conduct the Business.

4.2. The suspensive conditions referred to in Sub-Clause 4.1 above ("**Suspensive Condition(s)**") may not be waived nor may they be deemed to be fictionally fulfilled.

4.3. Denel and VR Asia shall use their respective Commercially Reasonable Efforts to procure the fulfilment of the Suspensive Conditions and each Party undertakes not to frustrate the fulfilment of the said Suspensive Conditions.

4.4. Should this Agreement (save for the Immediately Operative Provisions) cease to be of any force or effect by reason of clause 4.1 above then:

4.4.1. the Parties shall be restored as near as may be possible to the position in which they would have been had this Agreement not been entered into; and

4.4.2. no Party shall have any claim against the other as a result of the said Suspensive Condition precedent not having been fulfilled or waived, as the case may be.

5. INCORPORATION, ORGANISATION AND BUSINESS OF THE COMPANY

5.1. Subject to Clause 4, immediately after the Signature Date, the Parties agree to establish and incorporate the Company in Hong Kong as a private company with limited liability limited by shares in accordance with the Companies Ordinance and generally the Applicable Laws of Hong Kong for the purpose of undertaking the Business.

5.2. The name of the Company shall be "**Denel Asia Co. Ltd.**" or such other similar name as Denel may direct.

5.3. The registered office address of the Company shall initially be at [5th Floor, Alexandra House, 18 Chater Road], Hong Kong.

5.4. The Company shall have one class of Shares (being 10,000 Shares) in its capital, and shall issue [1,000 Shares] upon incorporation. Denel and VR Asia shall, immediately upon the formation of the Company, subscribe for Shares in accordance with the Agreed Proportions for cash in an amount of USD1 (one United States Dollar) per Share as set out in the table below.

Applicant	Number of Shares	Total Consideration
Denel	510 Shares	USD$510 in cash
VR Asia	490 Shares	USD$490 in cash

5.5. The payment by Denel and VR Asia in respect of the Shares that they subscribe for pursuant to Clause 5.4 above shall be made, within three (3) days of the issuance of a Certificate of Incorporation of the Company, in US dollars or HK Dollars by telegraphic transfer or electronic funds transfer to a bank account notified by or on behalf of the Company to each of Denel and VR Asia.

5.6. The Shareholders shall procure that the Company pass the necessary resolutions to issue and allot the Shares for cash to Denel and VR Asia respectively in accordance with the table in Sub-Clause 5.4, the entry of their respective names into the register of members of the Company and the issue of appropriate share certificates to each of them.

5.7. The number of Shares to be respectively held by Denel and VR Asia pursuant to this Agreement shall, except in consequence of the operation of this Agreement or the Articles or by Applicable Law or otherwise agreed in writing between the Parties, be maintained at all times in the Agreed Proportions.

5.8. As soon as reasonably practicable from the date of incorporation of the Company, each of the Shareholders shall use all Commercially Reasonable Efforts to:

5.8.1. procure the Company to pass the necessary resolutions to:

5.8.1.1. appoint the persons nominated by the Shareholders pursuant to Clause 9.2 as Directors;

5.8.1.2. appoint KPMG as the Secretary with the power of delegation to an independent corporate service provider, it being agreed that the Shareholders in general meeting may resolve to appoint another certified independent corporate service provider to act as the Secretary of the Company;

5.8.1.3. appoint KPMG as the initial Auditors for the first Financial Year, it being agreed that the Shareholders in general meeting may resolve to appoint another certified public accountant to act as auditor of the Company;

5.8.1.4. fix the Financial Year end of the Company as the last day of March of each year; and

5.8.1.5. appoint the authorised signatories to all the Company's bankers, subject to the provisions of the Approvals Framework (**Annexure D**); and

5.8.2. procure the Company to apply for and obtain, in accordance with Applicable Laws, all approvals, consents and/or licences necessary and required to operate the Business from the relevant authorities and/or regulatory bodies (including but not limited to business registration certificate) as soon as reasonably practicable.

5.9. Unless otherwise unanimously agreed between the Shareholders in writing, the business of the Company shall be to:

5.9.1. conduct trading in various defence products, amongst others the marketing, selling, merchandising and delivery of any products listed in **Annexure A** as is manufactured and/or sold by Denel

5.9.2. bid or otherwise participate or become involved in special projects for the provision of defence products and expertise as and when such opportunities arise.

within the Territory as more fully indicated in **Annexure A**. The Company may also conduct business in Hong Kong and/or any other jurisdiction as unanimously agreed between the Shareholders in writing.

5.10. Each of the Shareholders shall use its Commercially Reasonable Efforts to ensure that the Business shall be conducted in the best interests of the Company, on sound commercial profit making principles and in all material respects in accordance with all Applicable Laws and regulations. It is specifically acknowledged and agreed that the Company as a subsidiary of Denel shall be subject to the provisions of the PFMA and consequently, the Parties acknowledge that in undertaking its Business and operations the Company shall, as applicable, adhere to and pro-actively implement the principles and/or requirements of the PFMA, as directed by Denel from time to time.

5.11. In order to develop the Business, each Shareholder shall use its Commercially Reasonable Efforts to refer and/or introduce business opportunities to the Company.

5.12. The Shareholders acknowledge and confirm that they will perform this Agreement in good faith and in a spirit of mutual co-operation, trust and confidence.

5.13. Responsibilities of Denel:

5.13.1. Subject to Sub-Clause 5.13.2, Denel shall via a separate written agreement on its standard terms and conditions of trade, supply, sell and make available to the Company agreed products as manufactured by Denel in RSA, in such quantity as from time to time requested by the Board and on terms agreed to between Denel and the Company, for the purpose of the conduct of the Business in the Territory (including but not limited to the processing, selling and marketing of such products by the Company).

5.13.2. Denel shall, free of charge and/or costs (other than in respect of third party charges or costs):

5.13.2.1. provide and make available to the Company all information in relation to the products supplied by Denel in accordance with Sub-Clause 5.13.1 which is reasonably necessary for the conduct of the Business; and

5.13.2.2. provide and make available to the Company all such technical assistance and/or "data-packs" required by the Company and/or its contractor, VR RSA in order to further the Business,

all on terms and conditions as the parties thereto may agree in writing.

5.14. Responsibilities of VR Asia:

5.14.1. VR Asia shall procure, upon the request of the Board and on terms agreed between VR RSA and the Company, that VR RSA provide to the Company the services of attending to, advising on and executing certain fabrication, manufacturing and operational services and/or related aspects of the Business and/or of the Company, all on terms as shall be agreed to in a written agreement between the parties thereto. In consideration of such provision of services, the Shareholders shall procure that the Company pay to VR RSA, or such other party as nominated by VR RSA an agreed arms-length and marked related fee and/or rate. For the sake of clarity, it is recorded that the rates and/or the fee which may be agreed upon, may be agreed either on a project by project basis, or at a rate/fee/cost per unit or otherwise based on reasonable manufacturing rates applicable in the market unless the parties agree otherwise to preferential rates.

5.14.2. VR Asia shall, using its Commercially Reasonable Efforts, be obliged to utilize all its resources, including but not limited to its established network of potential business sources, in performing the marketing activities on behalf of the Company and in general ensuring that potential business opportunities shall be fully exploited by the Company in the Territory.

5.14.3. VR Asia shall make available to the Company the VR Asia Loan, in an amount of ZAR100,000,000.00 over a period of 5 (five) Financial Years, advanced as to ZAR20,000,000,00 per annum, with the first such advanced being effected as and when required and on a date to be determined by the Board and annually thereafter on each anniversary thereof.

5.15. Responsibilities of both Denel and VR Asia

The Parties hereby undertake to use their respective Commercially Reasonable Efforts to procure that the relevant supply and contract manufacturing arrangements

contemplated in clauses 5.13 and 5.14 are concluded within a period of 6 (six) months after the date of satisfaction of the last of the suspensive conditions referred to in clause 4, or such later date as the Parties may agree in writing.

5.16. Responsibilities of the Company

5.16.1. The Shareholders acknowledge that if and to the extent that the Company, pursuant to it conducting the Business, is liable to any governmental authority to re-invest funds and/or value in that Territory and/or in settlement of any off-set obligations (created and/or arising therefrom), they shall procure that the Company shall be solely liable for any such off-set obligations and/or other similar obligations that may arise in the Territories in which it has secured opportunities.

5.16.2. The Shareholders shall procure the Company will establish its own information organisation systems that shall be responsible for procuring and/or providing all of the information systems and technology required for the operation of the Business. Such organization shall be responsible for establishing and operating the Company's IT infrastructure, including but not limited to information systems and all supporting services.

6. CONDUCT OF BUSINESS OF THE COMPANY

The Parties hereby agree that the Company shall (and procure that its subsidiaries shall):

6.1. comply in all respects with the PFMA and other Applicable Laws;

6.2. not engage directly or indirectly in any prohibited activities, as contemplated in the Anti-Bribery Laws or do business with or issue Shares to any Sanctioned Entity;

6.3. implement anti-money laundering and anti-bribery and anti-corruption policies ("**AML and ABC Policies**") in compliance with Anti-Bribery Laws, and otherwise substantially similar to those AML and ABC Policies implemented by Denel with respect to its own operations. To the extent not already undertaken as at the Signature Date, Denel shall provide to the Company with its own AML and ABC Policies, for purposes of implementing the same in accordance herewith;

6.4. implement the environmental, social and governance policies and principles adopted by Denel. To the extent not already undertaken as at the Signature Date, Denel shall provide to the Company with copies of such policies and/or principles, for purposes of the Company implementing the same in accordance with the provisions hereof;

6.5. comply with all of the applicable requirements contained in Denel's policies and procedures and to the extent those requirements are not fully complied with at the date on which Denel becomes a Shareholder, formulate and implement an action plan for such compliance; and

6.6. not amend the Denel policies and/or principles (including the AML and ABC Policies), once adopted, without consultation with and the consent of Denel (which consent shall not be unreasonably withheld or delayed).

7 **MANAGEMENT OF THE COMPANY, OPERATIONAL AFFAIRS AND ADMINISTRATION**

7.1. **Accounting and Control:** It is hereby recorded and agreed by the Parties that its intended that from a financial reporting and control perspective (from an HK IFRS and accounting perspective) that the Company is reported as being a part of the Denel group of companies, and, consequently that Denel will be able to consolidate (from an accounting perspective) the Company's financial results. In order to ensure the implementation of this intention thereby enabling Denel to report on the financial performance of the Company on a consolidated basis, it is hereby irrevocably acknowledged and/or agreed, notwithstanding anything to the contrary herein contained, that:

7.1.1. from an accounting perspective (in accordance with International Financial Reporting Standards Statement 10 (*Consolidation of Financial Results)* perspective, the Company is Controlled by Denel;

7.1.2. for purposes of this Sub-Clause 7.1, each of VR Asia and the Company hereby agree that Denel is exposed, or has rights, to variable returns from its involvement with the Company and has the ability to affect those returns through its power over the Company (as such powers is contained in this Agreement);

7.1.3. the Company shall be accounted for as a subsidiary of Denel thus:

7.1.3.1. all intra-group transactions between them are to be eliminated in full;

7.1.3.2. the Company shall adopt, implement and maintain uniform accounting policies of Denel as are applied throughout the consolidated Denel group of companies; and

7.1.3.3. the Financial Statements of the Company shall be prepared to the same reporting date of Denel; and

7.1.4. subject to the remaining terms of this Agreement (including the Approvals Framework (**Annexure D**), Denel as a consequence of its contractual entitlements in terms of this Agreement has the ability to direct, in relation to other things:

7.1.4.1. the management of the Company's financial assets during their life (including upon default);

7.1.4.2. the selection, acquisition or disposition of assets of the Company;

7.1.4.3. a funding structure or obtaining funding in relation to the Company;

7.1.4.4. establishing operating and capital decisions of the Company, including budgets; and

7.1.4.5. appointing and remunerating the Company's key management personnel or service providers and terminating their services or employment,

all of which shall align to and/or be comparable to the wider consolidated Denel group of companies policies and procedures.

7.2. The Board undertakes to procure that the Company shall

7.2.1. carry on and conduct its Business and its affairs –

7.2.1.1. in accordance with this Agreement, its Articles and the Business Plan;

7.2.1.2. in a proper and efficient manner for its own benefit;

7.2.1.3. in accordance with the Approvals Framework as read together with the Reserved Matter Approval(s), from time to time; and

7.2.1.4. on arm's length commercial terms (whether with its Shareholders or with third parties);

7.2.2. at all times maintain in connection with its Business –

7.2.2.1. adherence to Applicable Laws, its Articles, and this Agreement; and

7.2.2.2. all necessary RSA or other Territory specific governmental or other consents and approvals in full force and effect;

7.2.1. if so directed by the Board, seek, obtain and maintain with a well-established and reputable insurer –

7.2.1.1. adequate insurance (as determined by the Board) against all risks usually insured against by companies carrying on the same or a similar business to the Business;

7.2.1.2. general liability and Directors and officers professional liability insurance in respect of the Directors, in accordance with the Companies Ordinance; and

7.2.1.3. general liability and public liability insurance in respect of its assets and/or Business; and

7.2.2. maintain accurate and complete accounting and other financial records in accordance with the requirements of this Agreement, all Applicable Laws and make true and complete entries of all its dealings and transactions in relation to the Business in such records. In particular, the Company shall comply with Denel's monthly management accounts, financial forecasts, budgeting and reporting standards, from time to time.

8. RESTRICTIONS AND EXERCISE OF VOTING RIGHTS

8.1. The Shareholders shall procure that no action is taken or resolution is passed by the Company, or any of its subsidiaries (if any) or the Directors of the Company or of any subsidiary of the Company in respect of any of the acts, matters or things specified in Part A of **Annexure B** without the prior Reserved Matter Approval first having been obtained ;provided that this Clause 8.1 shall not apply to acts matters or things required to be, or expressly contemplated as being, done by this Agreement. Should a particular matter not obtain the requisite Reserved Matter Approval, the matter in question shall fail.

8.2. The Shareholders shall procure that no action is taken or resolution is passed by the Company, any of its subsidiaries (if any) or by any of the Directors of the Company or of any subsidiary of the Company in respect of any of the acts, matters or things specified in Part B of **Annexure B** without the prior approval of at least 75% of all the Directors in writing or at a meeting of the Directors (akin to that of a Reserved Matter Approval), provided that this Clause 8.2 shall not apply to acts matters or things required to be, or expressly contemplated as being, done by this Agreement.

9. DIRECTORS AND THEIR MEETINGS

9.1. Without prejudice to Clause 5 and 8, the Directors shall be responsible for the day-to-day operation and management of the Company.

9.2. The minimum number of Directors holding office at any time shall be 2 (two) and there shall be a maximum of 10 (ten), provided that for each complete 10% of Shares held, a Shareholder is entitled but not obliged to appoint a Director. The initial number of Directors shall be four (4) and shall comprise the following persons:

9.2.1. Zwelakhe Ntshepe (nominated by Denel);

9.2.2. Stephan Burger (nominated by Denel);

9.2.3. Pieter van der Merwe (nominated by VR Asia); and

9.2.4. Kamal Singhala (nominated by VR Asia),

or such other persons as the Shareholders may from time to time appoint.

9.3. Any increase or decrease in the number of Directors referred to in Sub-Clause 9.2 shall require the unanimous consent of all the Shareholders.

9.4. The Chairman of the Board shall preside as chairman in meetings of the Directors. The first Chairman shall be a Director nominated and appointed by Denel, and any changes to the Chairman may be made in accordance with Clause 9.2 and item 1 in Part B of **Annexure B**.

9.5. Each of the Shareholders agrees to immediately remove any person nominated by it as a Director who is (i) a Sanctioned Entity, or (ii) convicted of any criminal offence (wherever committed) involving dishonesty, or (iii) who is otherwise disqualified as a Director pursuant to the Articles and/or the Applicable Laws of Hong Kong and/or the AML and ABC Policies and/or Denel's internal governance framework and/or polices and/or procedures. Pending the formal removal of such person, by that fact, such person shall be suspended and need not receive notice of any meetings of the Board for the duration of such suspension until his/her removal from the Board.

9.6. Subject to the proviso to Sub-Clause 9.5 and the provisions of Clause 11, the Directors shall have the right to receive all notices and minutes of meetings of the Directors and all written resolutions and other documents relating to the business and affairs of the Company and shall be entitled to speak and vote at meetings of the Directors.

9.7. The Directors shall have one vote each with the Chairman having a casting vote.

9.8. Any Director may, by giving notice in writing to the other Director(s), appoint an alternate and may, in the same way, remove an alternate so appointed by him. Subject to the proviso to Sub-Clause 9.5 and the provisions of Clause 11, an alternate shall be entitled to receive notice of all meetings of the Directors and attend and vote as such at any meeting at which the Director appointing him is not personally present, and generally in the absence of his appointer, to do all the things which his appointer is authorised or empowered to do.

9.9. The first meeting of the Directors shall be held within thirty (30) days of the date of incorporation of the Company. Meetings of the Directors shall be held at least once every Financial Year or such more frequent time/s as the Chairman of the Board may from time to time decide. All meetings of the Directors shall be held at the registered office of the Company or such other place as may be determined by the Directors from time to time. Unless 75% or more of the Directors resolve otherwise, not less than fifteen (15) days' notice of each meeting of the Directors specifying the date, time and place of the meeting and the agenda of business to be transacted thereat shall be given to all Directors and alternate directors.

9.10. Unless 75% or more of the Directors resolve otherwise, a meeting of the Directors may be convened with less than fifteen (15) days', but no sooner than two (2) Business Days', by notice by the Chairman of the Board if, in the reasonable opinion of the Chairman, there is an important issue which needs to be discussed in emergency in advance of the next scheduled meeting of the Directors.

9.11. An agenda for any meeting of the Directors and copies of any relevant papers to be discussed at such meeting shall be distributed to all Directors together with the notice of such meeting. Any Director who wishes to add a subject matter to the agenda for any meeting of the Directors upon receipt of the notice of such meeting shall notify the other Director(s) in writing at least ten (10) days prior to the date of such meeting.

9.12. The quorum necessary to constitute a meeting of the Directors shall be the majority of Directors present in person or by proxy. If within half an hour from the time appointed for a meeting of the Directors a quorum is not present, the meeting shall be automatically adjourned without notice to the same day of the next week at the same time and place. At any resumed meeting or re-convened adjourned meeting the Directors then present in person or by proxy shall constitute a quorum.

9.13. At any meeting of the Directors, subject to the provisions of Sub-Clause 9.7, each Director shall be entitled to one vote and all day-to-day operational and management matters shall be decided by a 51% majority of the Directors (except where a greater

majority is required by the Articles, this Agreement or the Applicable Laws of Hong Kong).

9.14. In the event of equality of votes, the Chairman of the Board shall have a casting vote.

9.15. The Directors may participate in a meeting of the Directors by means of video conferencing, teleconferencing, or other electronic or digital or similar communications equipment whereby all persons participating in the meeting can speak, hear and/or see each other contemporaneously and such participation shall constitute presence in person. A quorum shall be deemed to be present if such conditions are satisfied in respect of the number and designation of Directors required to form a quorum, and any Director participating in such a manner shall be entitled to vote in the meeting of the Directors.

9.16. A resolution in writing signed by all or the required majority of the Directors forming a quorum of a meeting of Directors (or their respective alternates) shall be as valid and effective for all purposes as a resolution of all or the required majority of Directors duly passed at a meeting of the Directors duly convened, held and constituted provided that when a Director has signed a resolution by facsimile, or scan and email, the original of the signed copy shall be deposited with the Secretary or Company in its registered office or such other office as the Company may designate for this purpose from time to time by such Director as soon as possible thereafter. Any such resolution may consist of several documents, provided that each such document is signed by one or more Directors.

9.17. The Directors shall devote so much of their business time and efforts to the furtherance of the Business and the performance of their responsibilities under this Agreement as is appropriate for the nature of the business of the Company and as they reasonably deem necessary. Each Director shall faithfully and diligently perform such duties in accordance with this Agreement and Applicable Laws and exercise such powers as may from time to time be assigned to or vested in him and shall use his reasonable best endeavours to promote the business and interests of the Company.

9.18. Unless otherwise agreed by 75% of the Shareholders in general meeting, the Directors shall not be entitled to any remuneration from the Company in relation to their respective appointments as Directors or to the reimbursement of any expenses except those properly and reasonably incurred by them in the performance of their duties as Directors.

9.19. The Board shall at all times be entitled to delegate any of its powers and authorities to any committee of the Board.

9.20. The Board shall at all times determine the form and detail of the Business P Plan and shall review and approve the Business Plan (which shall include the budget of the Company) on an annual basis in accordance with the reporting cycles and controlling requirements of the Shareholders in general meeting. The Board shall be responsible for implementing the Business Plan in accordance with (i) its terms and (ii) the Approvals Framework.

9.21. The Board shall be responsible for ensuring compliance by the Company with Applicable Laws and the risk policies of the Company for the time being and from time to time.

10. BOARD COMMITTEES

10.1. The Board may appoint any number of committees and delegate to such committees any authority of the Board in accordance with the Applicable Law, its Articles and as the Board may determine.

10.2. No person shall be appointed as a member of a Committee, if he is in Applicable Law ineligible or disqualified to be appointed as a Director and any such appointment shall be a nullity. A person who is ineligible or disqualified must not consent to be appointed as a member of a committee nor act as such a member. A person placed under probation by a court must not serve as a member of a Committee unless the order of court so permits.

10.3. Subject to the determination of the Board to the contrary, a committee may consult with or receive advice from any person.

10.4. Meetings and other proceedings of a committee consisting of more than 1 (one) member shall be governed by the provisions of this Agreement and the Articles regulating the meetings and proceedings of the Board.

10.5. Where practical, the composition of such committees, a brief description of their mandates, the number of meetings held and other relevant information must be disclosed in the annual report of the Company, which is to be furnished to the Shareholders.

10.6. An Advisory Committee may be constituted after the establishment of the Company, which shall be responsible for providing the Board with advice. The Advisory Committee shall consist of experts and other persons nominated by the Board.

11. INTERESTS AND CONFLICTS OF INTEREST

11.1. A Director who has an Interest in any transaction may attend any meeting of the Board or any Committee thereof at which such transaction is to be discussed, shall declare such Interest and shall not be permitted to vote on any matter relating thereto.

11.2. Each Director must avoid a situation in which s/he has, or can have, a direct or indirect Conflict of Interest. In particular (but without limitation), the Directors shall procure that they avoid a Conflict of Interest between their own personal (direct and indirect) interests, or that of a related party (on the one hand) and that of the Company (on the other) in relation to the exploitation of any property, information or opportunity (and it is immaterial whether the Company could take advantage of the property, information or opportunity concerned).

11.3. The duty contained in Sub-Clause 11.1 and 11.2 does not apply to a Conflict of Interest:

11.3.1. arising in relation to a transaction or arrangement with the Company in their capacity *qua* Director;

11.3.2. arising in relation to a transaction or arrangement with the Company in their capacity *qua* Shareholder;

11.3.3. if the Board determines that the situation cannot reasonably be regarded as likely to give rise to a Conflict of Interest; or

11.3.4. if the matter has been authorised by a disinterested majority of the Board then in office.

12. SHAREHOLDERS AND THEIR MEETINGS

12.1. The Shareholders shall procure that Shareholders' meetings are held regularly, no less than once per Financial Year. Shareholders' meetings will be held in such place as agreed by the Shareholders or failing which, as the Secretary shall decide. At least twenty one (21) days' (for annual general meetings) or at least fifteen (15) days' (for meetings other than annual general meetings) written notice of a Shareholders' meeting must be given to each Shareholder specifying the date, time and place of the meeting and the agenda of business to be transacted provided that if all the Shareholders agree to a shorter period of notice, then such meeting shall be deemed to be properly called.

12.2. An agenda for any meeting of the Shareholders and copies of any relevant papers to be discussed at such meeting shall be distributed to all Shareholders together with

the notice of such meeting. All notices and agenda (if not in English language) shall be accompanied by accurate and complete English language translations thereof.

12.3. The quorum for meetings of the Shareholders shall be such number of Shareholders who together hold more than 60% of the issued share capital of the Company, present in person or by proxy or participating by means of video conferencing teleconferencing, or other electronic or digital or similar communications equipment (whereby all persons participating in the meeting can hear and/or see each other contemporaneously and such participation shall constitute presence in person). If within half an hour from the time appointed for a meeting of the Shareholders a quorum is not present, the meeting shall be adjourned to the same day of the next week at the same time and place. No meeting of the Shareholders shall vote or resolve any matter which is not specified on the agenda for that adjourned meeting unless with the prior consent of each Shareholder.

12.4. For the purposes of decision making at meetings, each Shareholder/s shall vote in accordance with their Agreed Proportions. Questions arising at any Shareholders' meeting shall be decided by simple majority decision unless otherwise required by the Articles, requires a Reserved Matter Approval in accordance with Clause 8 of this Agreement or the Applicable Laws of Hong Kong.

12.5. A resolution in writing signed by or on behalf of each of the Shareholder entitled to receive notice of a meeting of Shareholders shall be as valid and effective for all purposes as a resolution of Shareholders duly passed at a general meeting of the Company duly convened, held and constituted provided that when a Shareholder has signed a resolution by facsimile, or scan and email, the original of the signed copy shall be deposited with the Secretary or the Company in its registered office or such other office as the Company may designate for this purpose from time to time by such Shareholder as soon as possible thereafter. Any such resolution may consist of several documents, provided that each such document is signed by one or more Shareholders.

12.6. A Shareholder may in respect of any Shares held by it attend by proxy any meeting of the Shareholders which it is entitled to attend in person, and vote by proxy (but not on a show of hands if more than one proxy is appointed) on any resolution at any such meeting on which it would, if present in person, otherwise be entitled to vote in respect of such shares. A proxy need not be a member of the Company.

12.7. case may be).

13. BUDGET, BUSINESS PLAN AND OTHER FINANCIAL MATTERS

13.1. Budget

The Shareholders shall procure that the Company, and each Shareholder shall, use Commercially Reasonable Efforts to ensure that the Directors adopt an annual Budget for the Company [3 (three)] month(s) before the beginning of each Financial Year and a quarterly budget for the Company [30 (thirty)] days before the beginning of each quarter of the Financial Year, in such forms and contents approved by the Directors.

13.2. Business Plan

13.2.1. The Shareholders shall procure that the Company, and each Shareholder shall, use Commercially Reasonable Efforts to ensure that the Directors adopt an annual Business Plan for the Company [3 (three) month(s) before the beginning of each Financial Year [and a quarterly Business Plan for the Company 30 (thirty) days before the beginning of each quarter of the Financial Year, in forms and contents approved by the Directors.

13.2.2. The Business Plan shall include but not be limited to the following information:

13.2.2.1. business strategy and targets;

13.2.2.2. product and service strategy and targets;

13.2.2.3. pricing policy;

13.2.2.4. personnel policy and hiring plans;

13.2.2.5. a financial plan;

13.2.2.6. financing requirements for working capital, investment and expansion;

13.2.2.7. revenue and profit targets and a profit and loss plan; and

13.2.2.8. a marketing plan.

13.3. Books and Records

The Shareholders shall exercise their powers in relation to the Company so as to ensure that the Company shall:

13.3.1. keep true, proper and accurate books and records in accordance with the provisions of applicable law in Hong Kong and, in the case of books of accounts and financial and related records, also in accordance with

HK IFRS and shall procure such books of accounts and financial records to be audited, at the expense of the Company, by the Auditors as soon as practicable after the end of each Financial Year; and

13.3.2. allow each of the Shareholders and its authorised representative(s) during normal business hours to inspect the books, accounting records and any other documents of the Company, if and when such Shareholder shall so request, and to make any extract and copy therefrom or arrange for audit of the same at their own expense. The Shareholders shall be entitled to make copies of any such books, accounting records and documents, and to attend the facilities of the Company and inspect its assets and to discuss the business, operations, and affairs of the Company with the respective Directors, accountants, lawyers and other advisors.

14. FINANCIAL STATEMENTS, INFORMATION AND ACCESS

14.1. The Company shall prepare annual financial statements in accordance with the Companies Ordinance and HK IFRS and shall have those annual financial statements audited.

14.2. The accounting records shall be kept at the registered office of the Company and shall at all times be open to inspection by the Board and Shareholders.

14.3. The Directors shall cause to be prepared and laid before the Company at its Annual Meeting at least such annual financial statements, Directors' reports and group annual financial statements and group reports, if any, as are required in terms of the Companies Ordinance.

14.4. Denel shall be at liberty from time to time to make such disclosure to another member of the Denel Group in relation to the business affairs and financial position of the Company as it may in its reasonable discretion think fit.

14.5. Delivery of Financial Statements to Shareholders

The Shareholders shall procure the Company to deliver, at the Company's own cost, to each of the Shareholders and the Directors:

14.5.1. as soon as practicable, but in any event within ten (10) days after the end of each calendar month, an unaudited balance sheet and profit and loss statement of the Company as of the end of or for such month;

14.5.2. as soon as practicable, but in any event within twenty (20) days after the end of each calendar quarter, an unaudited balance sheet and profit and loss statement of the Company as of the end of or for such quarter;

14.5.3. as soon as practicable, but in any event within ninety (90) days after the end of each Financial Year and in accordance with the Companies Ordinance, a balance sheet and profit and loss statement of the Company as of the end of or for such Financial Year, and year-end directors' reports of reasonable detail, prepared in accordance with HK IFRS and audited and certified by independent public accountants of internationally recognised standing selected by the Directors;

14.5.4. such other information relating to the financial condition, business prospects or corporate affairs of the Company as any Shareholder may from time to time reasonably request.

14.5.5. Each Shareholder hereby undertakes to procure the Company to keep all the Shareholders fully and timely informed of all material developments in its Business.

15. DIVIDEND POLICY

The Company may, with the approval of the Shareholders declare and distribute by way of dividends any of its profits available for distribution to the Shareholders in accordance with the Companies Ordinance, Provided that where the outstanding principal of the VR Asia Loan and interests accrued thereon have not been fully repaid yet or where the Company has insufficient profits for fully repaying such principal and interests, no dividends shall be declared or distributed by the Company.

16. FINANCING

16.1. VR Asia undertakes to advance and provide to the Company, as Shareholders' Loans, funding in an aggregate amount of up to ZAR100,000,000.00 ("**VR Asia Loan**"), with ZAR 20,000,000 to be advanced and provided for each year in accordance with Sub-Clause 5.14.3. The VR Asia Loan shall be used by the Company for setting up an office for sales and marketing and other operational costs of the Company.

16.2. The VR Asia Loan shall bear interest at the Repo Rate of the South African Reserve Bank per annum. The outstanding principal of the VR Asia Loan plus any interests accrued thereon shall be repaid from and when the Company begins to make profits from its Business. Should the Company be wound up / dissolved at any time prior to the VR Asia Loan being repaid in full, no liability will accrue to Denel to settle the Loan.

16.3. If at any time, additional financing is required (in addition to the VR Asia Loan) to satisfy the working capital requirements of the Company as determined by the Directors, the Shareholders will consider the appropriate action to be taken in order to meet the Company's requirements whether by:

16.3.1. the procurement of Shareholders' Loans or subscription by the Shareholders for additional Shares; or

16.3.2. external financing by loans or overdraft facilities from banks or other financial institutions.

16.4. No Shareholder shall (unless agreed between the Shareholders) be obliged to provide any additional finance to the Company, whether by means of equity or Shareholders' Loans, Provided that if project finance (i.e. funding required for and/or incurred in order to secure business pursuant to a "bid proposal" or by way of demonstration of product) is required and any additional finance is agreed by the Directors to be raised for such purpose, then, unless agreed otherwise by the Shareholders, each Shareholder shall subscribe for additional equity, or advance Shareholders' Loans, in accordance with their Agreed Proportions at the fair market value thereof, as determined in accordance with clause 22.

16.5. The Shareholders undertake and agree to take all steps reasonably necessary to support any determination of the Directors to undertake external financing and to support the Company in obtaining the most favourable terms for loan financing, including approving the giving of such security in relation to the commercial borrowings as the lender may reasonably require and as may be agreed by the Directors, provided that all Shareholders are treated in the same manner.

17. **DEALINGS IN SHARES**

17.1. Each of the Shareholders agrees and undertakes to the other Shareholder(s) that it shall not without the prior written consent of the other Shareholder:

17.1.1. pledge or otherwise Encumber its legal or beneficial interest in the whole or any portion of its Shares; or otherwise use the same as security, or grant options over its legal and beneficial interest in the Shares (for the avoidance of doubt, any action violating this sub-Clause shall, as amongst the Parties, be void and shall be considered a material breach of this Agreement);

17.1.2. enter into any agreement with respect to the exercise (or abstention from the exercise) of the voting rights attached to all or any of its Shares; or

17.1.3. agree, whether conditionally or otherwise, to do any of the foregoing.

17.2. No Shareholder shall have the right to transfer any of its Shares except in accordance with the provisions of this Agreement and the Articles. Each of the Shareholders agrees to follow and comply with the provisions for the transfer of Shares as set out in Clause 17, 18 or Clause 19 (as the case may be).

17.3. The Shareholders shall procure that the Directors shall not register any transfer of Shares which fails to comply with Clause 17, 18 or Clause 19 (as the case may be).

18. **MANDATORY SHARE REPURCHASE**

18.1. Denel has the right from time to time and at any time, to investigate and/or assess the (i) directors, (ii) ultimate beneficiaries and/or (iii) shareholders of VR Asia (and VR Asia shall procure, using its Commercially Reasonable Efforts, that such right and obligation shall extend to its beneficiaries) a view to determining (a) who in fact ultimately Controls and/or benefits from VR Asia, and (b) whether such persons are of sufficient standing so as to avoid Denel suffering any adverse reputational impacts, as the case may be.

18.2. Should Denel, in its discretion but acting reasonably, determine that:

18.2.1. 1 (one) or more of the persons ultimately benefiting from an interest in VR Asia, are Sanctioned Entities;

18.2.2. VR Asia has materially breached any provision of this Agreement; or

18.2.3. if Denel, acting reasonably, is of the view that such persons who are shareholders of VR Asia be detrimental to the reputation and/or business of Denel,

it shall, on written notice to VR Asia, be entitled to require that VR Asia repurchase the shares/interest of that particular person(s) so identified in the notice; in which event VR Asia shall be obliged to implement such share repurchase, immediately and thereby remove that person from being a shareholder of VR Asia.

18.3. Notwithstanding the aforegoing provisions, Denel hereby acknowledges that as at the Signature Date, certain of the ultimate beneficiaries of VR Asia (as disclosed to it in writing) may be a PEP but such Persons, are not considered as potentially detrimental to the business of Denel or the Company. Accordingly, it is recorded and agreed that

the current shareholding and/or ultimate beneficiary structure of VR Asia as at the Signature Date shall not entitle Denel to require a mandatory repurchase of shares in terms of this clause 18.

18.4. Alternatively to the provisions of clause 18.2, should such repurchase by VR Asia, not remedy the situation (as determined by Denel, acting reasonably), or should any of those parties fail to effect such repurchase, then the Company shall repurchase all the Shares held by VR Asia at the lower of (i) the fair market value thereof or (ii) the aggregate amounts of funds invested as the VR Loan Account in by VR Asia, as the case may be.

19. **TRANSFER OF SHARES**

19.1. Disposal of Shares

19.1.1. Except as otherwise agreed to tin writing or as may be provided in this Agreement, -

19.1.1.1. none of the Shareholders may Dispose of any Shares held by such Shareholder unless all Shareholders' Loans owing to such Shareholder (if any) have been fully repaid; or

19.1.1.2. a Shareholder may only dispose of its Shares in one and the same transaction it disposes of that portion of its Shareholder Loan that bears the proportion to its entire Shareholder Loan as the number of shares that it is disposing bears to the aggregate number of its Shares.

19.1.2. Any Disposal of any Shares or Shareholders' Loans not made in conformity with this Agreement shall be null and void and shall not be recorded on the books of the Company.

19.2. Right of First Offer on Sale of Shares

19.2.1. Should Denel cease, for any reason to hold the majority of the Shares in the Company, the Company shall by that fact be obliged to alter its name to remove any reference to the word "Denel" therein.

19.2.2. Each Shareholder grants to the other Shareholder a right of first offer with respect to the Shares held by such Shareholder. Each time when any Shareholder ("**Selling Shareholder**") wishes to sell all or any of its Shares ("**Offered Shares**") to any bona fide third party, the Selling Shareholder

shall first offer such Offered Shares to the other Shareholder ("**Receiving Shareholder**") in accordance with the provisions of this Clause 19.2.

19.2.3. The Selling Shareholder shall deliver a written notice ("**Transfer Notice**") to the Receiving Shareholder stating (i) its *bona fide* intention to sell the Offered Shares, (ii) the name of the proposed buyer ("**Proposed Buyer**"); (iii) the number of Offered Shares proposed to be sold; and (iv) the proposed price, terms and payment and other material terms and conditions upon which it proposes to offer such Offered Shares or received from the Proposed Buyer. The Transfer Notice shall constitute an irrevocable offer from the Selling Shareholder to sell the Offered Shares to the Receiving Shareholder at the same price and on the same terms and conditions as set forth therein.

19.2.4. By written reply to the Selling Shareholder within thirty (30) days after the date of the Transfer Notice, the Receiving Shareholder shall have the right and may elect to purchase, on the terms specified in the Transfer Notice, all or part of the Offered Shares ("**Sale Shares**"). Such reply shall constitute irrevocable acceptance by the Receiving Shareholder of the offer contained in the Transfer Notice.

19.2.5. In the event that the Receiving Party provides to the Selling Party the reply referred to in Clause 19.2.3 then the Receiving Party shall complete the purchase of the Sale Shares upon the terms set forth in the Transfer Notice within thirty (30) days (extended until such date as all required approvals, consents or authorizations in connection with such purchase are obtained) ("**Transfer Period 1**").

19.2.6. In the event that the Receiving Party fails to complete the purchase of the Sale Shares within the Transfer Period 1 or to the extent that the Receiving Shareholder does not elect to purchase all the Offered Shares in accordance with this Clause 19, the Selling Shareholder may during the ninety (90) day period (extended until such date as all required approvals, consents or authorizations in connection with such purchase are obtained) ("**Transfer Period 2**") following the expiration of (i) the Transfer Period 1, or (ii) the thirty (30) day period mentioned in Clause 19.2.3, offer the uncompleted Sale Shares or (as the case may be) the remaining Offered Shares to the Proposed Buyer at a price not less than, and upon terms no more favourable to the Proposed Buyer than those specified in the Transfer Notice. The Selling Shareholder must give a copy of any

agreement with the Proposed Buyer relating to such uncompleted Sale Shares or (as the case may be) remaining Offered Shares to the Receiving Shareholder within three (3) days after execution of the agreement.

19.2.7. If the sale of the uncompleted Sale Shares or (as the case may be) the remaining Offered Shares to the Proposed Buyer referred to in Clause 19.2.5 is not completed within the Transfer Period 2, then the right of the Selling Shareholder to sell such Shares to the Proposed Buyer shall terminate and if the Selling Shareholder subsequently wishes to sell such Shares it shall be required to first re-offer to the other Shareholder in accordance with this Clause 20.2.

19.2.8. Each Shareholder shall procure all Directors nominated by it to approve such share transfers that are effected in compliance with the provisions of this Clause 19.2.

19.3. Transfer to Competitors Prohibited

Notwithstanding any other provisions in this Agreement, no Shareholder may sell any of its Shares to any competitor of the Company or any party affiliated with a competitor of the Company. For purposes of this Clause 19.3 a "competitor" means a company or person or entity engaged in businesses similar to those conducted by and in competition with any of the Shareholders or the Company at any time as reasonably determined by the Directors.

19.4. Obligations Binding on Transferees

19.4.1. It shall be a condition precedent to the right of any Shareholder to transfer any Shares pursuant to this Clause 19, that the transferee shall execute a Deed of Adherence under which the transferee shall agree to be bound by the obligations of this Agreement whereupon that transferee shall become a Shareholder on the date its obligations under the Deed of Adherence take effect. Upon the execution of a Deed of Adherence in accordance with this Agreement, each Party shall be obliged to any transferee to perform its obligations under this Agreement so far as they remain to be performed.

19.4.2. Any Shareholder that transfers its entire legal and beneficial interest (including any interest held by persons it Controls) in Shares in accordance with the provisions of this Agreement shall be released from all obligations under this Agreement with effect from the date of such

transfer except for (i) liability for antecedent breaches of any such obligations, and (ii) any obligations under Clause 29, and (iii) any obligations of Denel and VR Asia under Clauses 5.14, and 5.15 (which obligations shall continue to apply for Denel and VR Asia).

19.4.3. Any transferee that becomes a Shareholder in accordance with the terms of this Agreement shall be entitled to all of the benefits of this Agreement applicable to the Shareholder who transferred the Shares (with only the necessary changes).

19.5. Notwithstanding any provisions in the Articles, the Directors shall not have the right to decline to register any transfer of Shares made pursuant to Clauses 18, 19 and 21.

20. DIRECTORS' RIGHT TO REFUSE REGISTRATION OF TRANSFERS

Without derogating from any other provisions of this Agreement in relation to the conditions for the Registration of Shareholders, the Board may refuse or delay the Registration of transfer of any Share to any person (the "**transferee**") whether or not such transferee is an existing Shareholder, where:

20.1. so required by any Applicable Law;

20.2. the Company has a lien on such Share;

20.3. a holder of any such Share (the "**transferor**") has failed to pay on the due date any amount payable thereon either in terms of the issue thereof or in accordance with the Articles or this Agreement, except if the transferee takes transfer of such Share with all its liabilities and executes such deed or instrument as may be determined by the Board to that effect;

20.4. the transfer is not accompanied by such proof as the Board reasonably requires of the right of the transferor to make the transfer;

20.5. the Board acting in good faith decides in its sole discretion that Registration of the transfer would not be in the best interests of the Company; or

20.6. the transferee is a Sanctioned Entity.

21. DEFAULT

21.1. Events of Default

The provisions of hereof shall apply if any of the following events shall occur with respect to any of the Shareholders ("**Events of Default**"):-

21.1.1. the Shareholder commits any material breach of or omits to observe any of its undertakings or obligations under this Agreement and if any such breach or omission is capable of remedy, the same shall not have been fully remedied within sixty (60) days of the Shareholder being notified of such breach or omission;

21.1.2. a creditor attaches, arrests, seizes, or takes possession of, or a distress, execution, sequestration or other process is levied, executed or enforced upon or sued out against, the whole or any part of the business, undertaking, properties, assets, rights or revenues of the Shareholder and such attachment, arrest, seizure, possession, distress, execution, sequestration or process is not contested on valid grounds, released, lifted, discharged or discontinued within sixty (60) days;

21.1.3. the Shareholder stops or suspends payment of its just and uncontested debts or is unable or admits inability to pay its debts as they fall due or begins negotiations with one or more of its creditors with a view to a general or partial reconstruction, readjustment or rescheduling of all or part of its debts or proposes or enters into any compromise, composition or other arrangement for the benefit of its creditors generally or any class of its creditors or any proceedings are commenced in relation to the Shareholder under any law, enactment, regulation or procedure relating to reconstruction, readjustment or rescheduling of debts;

21.1.4. the Shareholder or any other person takes any action or any legal proceedings are started or other steps taken for (i) the Shareholder to be adjudicated or found bankrupt or insolvent, or (ii) the winding-up, liquidation or dissolution of the Shareholder, or (iii) the appointment of a liquidator, trustee, receiver, receiver manager, administrator, administrator receiver or similar officer of the Shareholder or of the whole or any part of the Shareholder's business, undertaking, properties, assets, rights or revenues;

21.1.5. the Shareholder suspends or ceases or threatens to suspend or cease to carry on its business or a material part thereof;

21.1.6. the Shareholder transfers or Disposes of or proposes or threatens to transfer or Dispose of the whole or a substantial part of the Shareholder's assets; or

21.1.7. VR Asia suffers a change in its Control, which change will (in the determination of Denel) have an adverse impact on the Company.

21.2. Default Notice

Each Shareholder shall immediately notify the Company if it suffers an Event of Default. The Shareholders shall procure the Company to give written notice ("**Default Notice**") to each of the Shareholders (including the defaulting Shareholder) upon the occurrence, or prospective occurrence, of an Event of Default within fifteen (15) days of (a) the date on which the Company is notified thereof or (b) the Company by resolution of the Directors and acting *bona fide* determines that there has been an occurrence or prospective occurrence of such Event of Default.

21.3. Consequence of Event of Default

21.3.1. By written notice ("**Termination Notice**") to the Company within fourteen (14) Business Days after receipt of a Default Notice, the non-defaulting Shareholder shall be entitled to terminate this Agreement, in which case the non-defaulting Shareholder may elect to:

21.3.1.1. serve a notice (the "**Sale Notice**") on the defaulting Shareholder within forty-five (45) days after the date of service of the Termination Notice, offering to sell and requesting the defaulting Shareholder to purchase all of the Shares of the non-defaulting Shareholder at 120% of the fair market value or net asset value, whichever is higher (the "**Put Option Price**"). The defaulting Shareholder must, by itself or through a third party nominee, purchase all of the Shares of the non-defaulting Shareholder at the Put Option Price within forty-five (45) days after service of the Sale Notice; or

21.3.1.2. serve a notice (the "**Purchase Notice**") on the defaulting Shareholder within forty-five (45) days after the date of service of the Termination Notice, offering to purchase and requesting the defaulting Shareholder to sell all of the Shares of the defaulting Shareholder at 70% of the fair market value or net asset value, whichever is lower (the "**Call Option Price**"). The defaulting Shareholder must sell all of its Shares at the Call Option Price within forty-five (45) days after service of the Purchase Notice.

21.3.2. The right of the non-defaulting Shareholder under this Clause 21 shall be in addition and without prejudice to any of its other rights or remedies under this Agreement or at law against the defaulting Shareholder in respect of such default (including any right for compensation of damages).

21.4. Determination of Share Value

In the event that the non-defaulting Shareholder elects to serve a Sale Notice or a Purchase Notice in accordance with Clause 21.3, the Shareholders shall procure the Company to promptly thereafter engage an internationally recognized independent appraiser, which shall be nominated by the Managing Director of KPMG Hong Kong ("**Valuator/s**"), in accordance with the provisions of Clause 22.

21.5. Right of First Refusal

In the event the provisions of this Clause 21 are held to be unenforceable with respect to any of the defaulting Shareholder's Shares, or if all of the defaulting Shareholder's Shares are not purchased pursuant to the provisions of this Clause 21, the non-defaulting Shareholder shall have a right of first refusal if the defaulting Shareholder (or any successor thereof) subsequently desires to transfer such Shares, in which event the defaulting Shareholder (or its successor) shall be deemed to be a "Selling Shareholder" under Clause 21and by all other provisions of this Agreement.

21.6. Power of Attorney

Each Shareholder, by way of security for the performance of its obligations under this Agreement, hereby irrevocably appoints the Company individually to be its attorney, with full power of substitution, and in the name and on behalf and as the act or deed of the Shareholder or otherwise, without any reference to or consent from the Shareholder, to sign, seal, deliver, execute, perfect and do all deeds, instruments, documents, acts and things as may be required or considered expedient by the Company to fully carry out the effect hereof. The Shareholders hereby ratify and confirm and agree to ratify and confirm any deed, instrument, document, act and thing which such attorney may have lawfully executed or done.

22. DETERMINATION OF VALUE OF SHAREHOLDING

22.1. In determining the fair market value of any Shares ("**the Valuation Shares**") when required to do so for any purposes under this Agreement, the Valuators:

22.1.1. shall not apply any minority discount or majority premium to the Shares;

22.1.2. shall not apply any non-marketability discount to the Shares;

22.1.3. act as an expert and not as an arbitrator;

22.1.4. shall value the Company or the relevant equity having regard to the price a willing buyer would pay to a willing seller negotiating at arm's length;

22.1.5. shall not take into account the illiquidity of the equity;

22.1.6. shall not take into account the fact that the relevant equity may be a minority or majority holding;

22.1.7. shall take cognisance of and give recognition to the current/prevailing realisable value of the Valuation Shares as determined by the Valuators at the relevant time;

22.1.8. shall take into account any recent transfer(s) of any Shares and the price at which such transfer(s) took place;

22.1.9. shall take into account the fair value of the goodwill, if any, of the Company and the actual value of the assets of the Company (and not merely their book value);

22.1.10. shall take into account all such other facts relating to the business and affairs of the Company as they may consider necessary or desirable, including those facts which they consider may be taken into account by a *bona fide* independent purchaser in an arm's length transaction;

22.1.11. shall take into account any sworn valuations obtained by the Valuator of any of the assets of the Company if the Valuator deems this necessary;

22.1.12. shall, without conflicting with and/or derogating from the above provisions, determine the proper method to be applied in valuing the Valuation Shares; and

22.1.13. shall act as experts and not as arbitrators and their decision shall (in the absence of manifest error) be final and binding on the Shareholders.

22.2. In determining the value of the Valuation Shares and/or any matter referred to in Sub-Clause 23.1 above, the Valuators shall take into account any written representations made by any Shareholder and/or its appointed representative(s) in this regard.

22.3. The Valuators shall determine the value of the Valuation Shares and inform the Shareholders (or in the event of a Shareholder's insolvency, sequestration, disability or death, his trustee, liquidator, curator or executor) of such value in writing within

15 (fifteen) Business Days (or such other period as may be agreed to between the Shareholders in writing) after being requested by the Company to prepare such Valuation.

22.4. In determining the fair market value of any equity for purposes of this agreement, the Valuators shall value the Loan Account forming part of such equity at the face value thereof, and such value shall be included in the fair market value of the equity.

22.5. For the purpose of hereof, **"net asset value"** means the book value of the Company as determined from its latest available audited Financial Statements, as adjusted for capital increase or decrease of the Company or any other major corporate activities which may affect the content of such Financial Statements, such adjustments to be made and certified by the Auditors within thirty (30) days after service of the Sale Notice or (as the case may be) Purchase Notice.

23. WARRANTIES AND UNDERTAKINGS

23.1. Each of the Parties warrants to the other that:

23.1.1. such Party has the power, legal capacity and authority to enter into and perform the obligations of such Party under this Agreement;

23.1.2. any consents which are required to enable such Party to enter into this Agreement have been obtained; and

23.1.3. the execution and performance of this Agreement have been validly authorised by all necessary action and this Agreement is and will remain valid, binding and enforceable against such Party.

23.2. Each of the Parties undertakes with the other:

23.2.1. to perform and observe and to procure its nominated Directors to perform and observe all the provisions of this Agreement and in a spirit of mutual co-operation, trust and confidence;

23.2.2. so far as it is able to do so, including the exercise of voting rights, to procure that the Company diligently performs and observes its obligations under this Agreement;

23.2.3. to take all necessary steps on its part to give full effect to the provisions of this Agreement;

23.2.4. without prejudice to the generality of the foregoing, to exercise and procure that every person for the time being representing it will exercise

or refrain from exercising any rights of voting at any meeting of the Shareholders or of the Directors and any other rights or powers of control so as to ensure the passing of any and every resolution necessary or desirable to procure that:

23.2.4.1. the affairs of the Company are conducted in accordance with this Agreement;

23.2.4.2. to give full effect to the provisions of this Agreement; and

23.2.4.3. so as to ensure that no resolution of the Company is passed or that any matter is done or any omission is made which does not accord with the provisions of this Agreement;

23.2.5. not to make or permit any dealings with any Shares for the time being owned or controlled by it which will prevent or impede the performance and observance of this Agreement; and

23.2.6. save as the Shareholders may otherwise agree, the Shareholders shall procure the Company to take all reasonable steps to enforce all their material rights under all agreements to which they are parties.

23.3. Each of the Shareholders agrees to co-operate and act in the best interests of the Company in the promotion and development of the Business.

24. DURATION

24.1. Duration

The term of this Agreement shall commence from the date of this Agreement and shall continue until or unless terminated by operation of law or by mutual agreement of the Shareholders or in accordance with the remainder of this Clause 24.

24.2. Termination

24.2.1. This Agreement shall terminate:

24.2.1.1. vis a vis each of the Shareholders, such time as they cease to own Shares in the Company provided that the Shares have been transferred in accordance with the terms of this Agreement (except where the Shareholder involved is Denel or VR Asia, its obligations under Clauses 5.14 and 5.15 shall continue to apply);

24.2.1.2. upon liquidation or the making of an order for the winding-up of the Company (other than for the purpose of reconstruction or amalgamation);

24.2.1.3. upon service of a Termination Notice by a non-defaulting Shareholder in accordance with Clause 40;

24.2.1.4. upon occurrence of a *force majeure* event beyond the control of any of the Parties which leads to the inability of the Company to carry on the Business for a period of twelve (12) months or more.

24.2.2. Determination of this Agreement howsoever occurring shall be without prejudice to the rights, obligations and liabilities of any Party accrued prior to the termination and such of the Clauses of this Agreement as are expressed or designed to have effect after termination shall continue to be enforceable notwithstanding termination of this Agreement.

25. EXIT MECHANISMS AND TERMINATION

25.1. **Grounds for Termination:** In addition to the provisions of clause 21 and 24, this Agreement shall be terminable immediately upon notice in writing to all Parties upon the occurrence of one or more of the following events:

25.1.1. automatically if the Government of the Republic of South Africa directs Denel to cease being a Shareholder and/or otherwise terminate its relationship herein, whether for reasons of national security, or otherwise;

25.1.2. automatically, if (for whatever reason) there is only one Shareholder of the Company;

25.1.3. by agreement of both Parties;

25.1.4. by either Shareholder, if any Applicable Law shall, after applying Commercially Reasonable Efforts, (i) make performance of this Agreement impossible or unreasonably expensive or unreasonably difficult for such Party, or (ii) materially alter the rights and obligations of the Parties from those agreed and contemplated by this Agreement, or (iii) Materially interferes with the benefits reasonably and/or expressly contemplated herein to be received by such Party, if, in each case, the Parties have first been unable to resolve the matter amicably after using

their respective Commercially Reasonable Efforts within 30 (thirty) days of any Party having called upon the others in writing to commence discussions for this purpose;

25.1.5. by either Shareholder, if the other Shareholder shall be or become incapable for a period of 90 (ninety) days of performing any of its material obligations under this Agreement because of *vis major* (superior force) or *casus fortuitous* (fortuitous cause); or

25.1.6. by either Shareholder, if a court order is granted for the other Shareholder's liquidation, receivership, bankruptcy, business rescue process, reorganisation, compulsory composition, judicial management, administration or dissolution, or other similar process and such order has not been rescinded within 90 (ninety) days after the date on which it was granted, or if such Shareholder is unable to pay any of its debts as and when they become due or otherwise committed an act of bankruptcy as contemplated in the Applicable Laws or has explicitly or implicitly suspended payment of any debts as they became due (except debts contested in good faith), or if the creditors of such Shareholder have taken over its management, or if any material or significant part of such Shareholder's undertaking, property, or assets shall be intervened in, expropriated, or totally or partially confiscated by action of any government and the effect of such intervention, expropriation or confiscation is that the Shareholder concerned is prevented from performing its obligations under this Agreement.

25.2. This Agreement shall not be capable of cancellation due to an unremedied breach by a Party of its obligations unless otherwise agreed mutually by the Parties in the terms of clause 25.1 above. In the event of such breach, the rights of the aggrieved Party shall be limited to enforcing the terms of this Agreement, with or without a claim for damages and any other equitable remedy provided for in this Agreement (or under Applicable Law).

25.3. Termination of this Agreement shall be without prejudice to the accrued rights and liabilities of the Parties at the date of termination, unless waived in writing by mutual agreement of the Parties. Any term or provision of this Agreement which expressly purports to survive, or which a reasonable person would assume to be intended to survive termination hereof shall survive termination of this Agreement and shall remain in full force and effect. The provisions of this Agreement which do not survive

termination hereof shall nonetheless be used in construing and interpreting the rights and obligations of the Parties.

26. WINDING UP

26.1. Subject to Applicable Law, and the provisions of clause 26.4 below the Board must apply for the winding-up of the Company:

26.1.1. by the decision of the Board at any time consequent to a Reserved Matter Approval;

26.1.2. in applying the provisions of clause 25; or

26.1.3. upon the happening of any other event under Applicable Law requiring the winding-up,

whichever occurs first.

26.2. Subject to Applicable Law and for the avoidance of doubt, the Company shall not be wound-up on the occurrence of any one or more of the following events:

26.2.1. the bankruptcy, death, insanity, retirement, resignation, withdrawal, expulsion, termination, cessation or dissolution of a Shareholder;

26.2.2. the transfer of any Share or other interest in the Company in contravention of the Articles or this Agreement; or

26.2.3. the redemption, repurchase or cancellation of all the Shares of a Shareholder.

26.3. Upon the happening of any of the events set out in clause 26.1, the assets of the Company may, subject to Applicable Law, be applied in the order set out below, and on such terms and conditions as the Board may decide:

26.3.1. third party debts shall be applied:

26.3.1.1. to creditors in satisfaction of the debts and liabilities of the Company, to the extent permitted by Applicable Law, whether by payment thereof or the making of reasonable provision for payment thereof (other than any loans or advances that may have been made to the Company by any of the Shareholders in their capacity as Shareholders);

26.3.1.2. to the expenses of liquidation, whether by payment thereof or the making of reasonable provision for payment thereof; and

26.3.1.3. to the establishment of any reasonable reserves (which may be funded by a liquidating trust) to be established by the liquidator in amounts determined by it to be necessary for the payment of the Company's expenses, liabilities (including contingent liabilities) and other obligations (whether fixed or contingent); and

26.3.2. Shareholder debts and distributions shall be applied:

26.3.2.1. to the Shareholders, if any, who made loans or advances to the Company in their capacity as Shareholders, in satisfaction of such loans and advances, whether by payment thereof or the making of reasonable provision for payment thereof; and

26.3.2.2. to the Shareholders in accordance with the distribution provisions contained in clause 15.

26.4. Subject to Applicable Law and any requisite regulatory approvals, in the event that liabilities and obligations as set out in clause 26.3.1.1 remain outstanding at such time, the Shareholders may vote:

26.4.1. to place appropriate reserves in trust to cover such obligations and liabilities and to proceed to wind up the Company; or

26.4.2. to provide for such reserves within the Company and to wind the Company up only once all obligations and liabilities have been extinguished,

in either case, the reserving shall be made out of distributions which would otherwise be made to Shareholders and on satisfaction or extinction of all such obligations or liabilities, any remaining reserves shall be distributed to the Shareholders.

26.5. In the event that liabilities and obligations remain outstanding on the happening of an event set out in clause 26.1, the Shareholders shall place appropriate reserves in trust to cover such obligations and liabilities and to proceed to wind up the Company as set out in clause 26.3.1.

27. STATUS OF THIS AGREEMENT AND THE PARTIES' OBLIGATIONS

27.1. Each Shareholder shall:

27.1.1. observe good faith in the implementation of this agreement and their dealings with one another pursuant thereto;

27.1.2. exercise all voting rights and other powers of control lawfully available to him as a Shareholder of the Company so as to procure that, at all times during the term of this agreement, the provisions of this agreement are, using the Commercially Reasonable Efforts of that Shareholder, duly and promptly observed and given full force and effect according to its spirit and intention; and

27.1.3. irrevocably and unconditionally grant in favour of the Secretary a special power of attorney *in rem suam* (as if in its own name and stead) to do all such things as may be necessary to give effect to the provisions of Sub-Clause 27.2 below

27.2. Each of the Parties hereto hereby agrees that none of the Parties, other than the Company, will have the ability, power or capacity to independently to bind the Company in any way, save to the extent specifically provided for in this Agreement or in the Articles.

27.3. If any provisions of the Articles at any time conflict with any provisions of this Agreement, this Agreement shall prevail as between the Parties to it and each of the Shareholders shall, whenever called upon to do so by any other Party, exercise all voting and other rights and powers lawfully available to him as a Shareholder of the Company so as to procure the amendment, waiver or suspension of the relevant provision of the Articles to the extent necessary to permit the Company and its affairs to be administered as provided in this Agreement.

27.4. To the extent that there is any conflict between the provisions of this Agreement and the constitutional documents of the Company or any Subsidiary, and the benefit and/or protections (including any limitations on the powers of the Board) provided for in terms of this Agreement and/or in favour of the Shareholders are greater than the benefits and/or protections provided for in the constitutional documents of that Subsidiary, then the Company shall procure that the constitutional documents of such Subsidiary be amended to provide the benefit and/or protections as set out in this Agreement.

28. **NO PARTNERSHIP**

The Shareholders are not in partnership with each other, nor are they agents of each other.

29. **ANNOUNCEMENTS AND CONFIDENTIALITY**

29.1. **Announcements:** No public announcement or communication of any kind shall be made or issued in respect of the subject matter of this Agreement by any Party, save:

29.1.1. with the prior written consent of the other Party which may not be unreasonably withheld or delayed; or

29.1.2. to the extent required by applicable laws and regulations, provided the Party required to make or issue an announcement or communication has, if and to the extent practicable, first consulted (giving a reasonable amount of information and time to) the other Party or the Company and taken into account the reasonable requirements of the other Party or the Company.

29.2. **Confidentiality:** Each Party shall at all times keep confidential, treat as privileged, and not directly or indirectly make or allow to be made any disclosure or use of any oral or written information relating to the other Party or the Company (including any aspect of that Party's businesses, customers or Intellectual Property Rights) or the existence or subject matter of this Agreement ("Confidential Information"), except to the extent:

29.2.1. required by applicable laws and regulations and then only after advising the other relevant Party or the Company of that requirement and consulting (giving a reasonable amount of information and time to) that other Party or the Company in respect of the relevant matter and taking into account the reasonable requirements of the other Party or the Company;

29.2.2. necessary to obtain the benefit of, or to carry out obligations under, this Agreement, which shall include the ability to disclose Confidential Information to any employees or advisers who need to have it for purposes directly connected with the transactions provided for in this Agreement, provided that the relevant disclosing Party shall advise such employees or advisers of the confidential nature of the Confidential Information and shall use all Commercially Reasonable Efforts to procure that such persons keep the relevant Confidential Information strictly confidential and shall indemnify the other Party or the Company in respect of all costs, claims, actions, proceedings, losses and liabilities in connection with any unauthorised disclosure or use of the Confidential Information by such persons; or

29.2.3. that the information is or becomes available in the public domain without breach by a Party of its confidentiality obligations under this Clause or at law.

Each Party shall, on request by the other Party or the Company at any time, return to the other Party or the Company any Confidential Information which it holds (in whatever form) in respect of that other Party or the Company.

29.3. The provisions and restrictions contained in this Clause 29 shall survive the termination of this Agreement.

30. **NOTICES**

30.1. **Addresses:** Any notice or other communication under or in connection with this Agreement shall be in writing and shall be left at or sent by pre-paid registered post (if posted from and to an address in Hong Kong), pre-paid registered airmail (if posted from or to an address outside Hong Kong) or facsimile transmission to the Party due to receive the notice or communication at its respective addressor facsimile number set out below or to such other address and/or number(s) as may have been last specified by such Party by written notice to the other Party.

To Denel:

Address: Denel SOC Ltd Office, Nellmapius Drive, Irene, Centurion PO Box 8322; Centurion, 0046

Attention: Office of the Group Chief Executive Officer

Facsimile: 012 671 2751

Email: _____

To VR Asia:

Address: 10 Haggie Road, Boksburg, RSA

PO Box 5362, Boksburg North, 1461

Attention: Office of the Chief Executive Officer

Facsimile: 011 306 8018

Email: _____

30.2. **Delivery:** In the absence of evidence of earlier receipt, a notice or other communication is deemed given:

30.2.1. if delivered personally, when left at the address referred to in Clause 31.1;

30.2.2. if sent by registered post except air mail, two (2) days after posting;

30.2.3. If sent by registered air mail, six (6) days after posting; and

30.2.4. if sent by facsimile or email, on completion of its transmission.

30.3. In proving the giving of a notice by mail, it shall be sufficient to prove that the envelope containing such notice was properly addressed and posted.

30.4. In proving such service by facsimile it shall be sufficient to produce an activity or other report from the sender's facsimile machine in respect of the notice or other written communication showing the recipient's facsimile number and the number of pages transmitted.

30.5. For the avoidance of doubt, notice under this Agreement shall not be validly served if sent by e-mail.

31. **GENERAL**

31.1. **Expenses**: Save as expressly provided herein, all expenses incurred by or on behalf of the Parties and their advisers including all fees of agents, representatives, solicitors, accountants, actuaries and other advisers employed by any of them, in connection with the negotiation, preparation or execution of this Agreement, shall be borne solely by the Party who incurred the liability and the other Party shall have no liability in respect of them.

31.2. **Time of the essence**: Time shall be of the essence in this Agreement, both as regards the dates and periods specifically mentioned and as to any dates and periods which may, by agreement in writing between or on behalf of the Shareholders, be substituted for them.

31.3. **No prejudice to rights / waiver**: No failure to exercise, or delay in exercising, any right or remedy under this Agreement will operate as a release or waiver of such right or remedy or any other right or remedy, nor will any single or partial exercise of any right or remedy under this Agreement or provided by law preclude any other or further exercise of it or the exercise of any other right or remedy or prejudice or affect any right or remedy against others under the same liability whether joint, several or otherwise. A waiver of any breach of this Agreement or any right of remedy under this Agreement shall not be effective, or implied, unless that waiver is in writing and is signed by the Party against whom that waiver is claimed.

31.4. **Entire agreement:** This Agreement supersedes any previous agreement between the Parties, including the Co-operation Agreement dated 27 November 2015, in relation to its subject matter and the Parties acknowledge that no claim shall arise in respect of any agreement so superseded by this Agreement. This Agreement (together with the documents referred to herein) contains the entire agreement between the Parties relating to the transactions provided for herein and there are no other warranties, conditions or terms applicable thereto whether express or implied.

31.5. **Variations in writing:** Any variation to this Agreement shall be binding only if it in writing and signed by or on behalf of each Party.

31.6. **Further assurances:** The Parties shall execute such further documents and perform and procure such acts and things as may reasonably be required to give full effect to its obligations under this Agreement.

31.7. **Severability:** If any term in or provision of this Agreement shall be held to be illegal or unenforceable, in whole or in part, under any enactment or rule of law, the term or provision shall to that extent be deemed not to form part of this Agreement and the enforceability of the remainder of this Agreement shall not be affected.

31.8. **Rights cumulative:** The rights and remedies provided in this Agreement are cumulative and not exclusive of any rights or remedies provided by law.

31.9. **Survival:** The rights and obligations contained in this Agreement remain in force after termination, except to the extent that they have been fully performed or where this Agreement provides otherwise.

31.10. **Counterparts:** This Agreement may be executed in any number of counterparts each of which when executed and delivered is an original, but all the counterparts together constitute the same document.

31.11. **Successors:** This Agreement is binding on the successors of each Party.

31.12. **Assignment:** No Party may assign or transfer or purport to assign or transfer any of its rights or obligations under this Agreement without the prior written consent of the other Party.

31.13. **Conflict:** If any provisions of the Articles conflict with any provisions of this Agreement, the provisions of this Agreement, as between the Shareholders, shall prevail.

32. GOVERNING LAW, JURISDICTION AND DISPUTE RESOLUTION

32.1. **Hong Kong law:** This Agreement shall be governed by and construed in accordance with the laws of Hong Kong.

32.2. **Dispute resolution:** If any dispute, controversy or claim arises out of or in connection with this Agreement ("Dispute"), the Parties may seek to have the Dispute resolved amicably by mediation. A Party shall initiate the mediation procedure by written notice to the other Party involved in the Dispute. The mediation shall take place at the Hong Kong International Arbitration Centre ("**HKIAC**") in accordance with its Mediation Rules in force at the date of the aforesaid written notice. If the mediation is abandoned by the mediator or the Parties to the Dispute fail to agree the terms of settlement within thirty (30) days of the initiation of the mediation procedure for any reason, including but not limited to a Party's failure to participate in the mediation proceedings, any Party may refer the Dispute to arbitration as provided for in Clause 33.3.

32.3. If a Dispute cannot be resolved by mediation or any Party to the Dispute does not wish the Dispute to be referred to mediation, any Party may refer the Dispute to be settled by arbitration in accordance with the UNCITRAL Arbitration Rules as at present in force and as may be amended by the rest of this Clause. The appointing authority shall be HKIAC. The place of arbitration shall be in Hong Kong at HKIAC. There shall be only one (1) arbitrator who shall be appointed (in default of an agreement between the Parties to the Dispute) by HKIAC. The language to be used in the arbitral proceedings shall be English. Any such arbitration shall be administered by HKIAC in accordance with HKIAC Procedures for Arbitration in force at the date of this Agreement including such additions to the UNCITRAL Arbitration Rules as are therein contained. The decision or award of the arbitral tribunal shall be binding upon the Parties.

Annexure A. – Denel Asia Business Case

FORMATION OF DENEL-ASIA BUSINESS CASE

FORMATION OF DENEL-ASIA BUSINESS CASE

FORMATION OF DENEL-ASIA BUSINESS CASE

KT-309

AGENDA

1. Purpose
2. Background
3. Rationale
4. Business analysis
5. Proposal

KT-310

AGENDA

6. Intermediary vs Equity Partner
7. Criteria for Choosing a Partner
8. Regulatory requirements
9. Approval required
10. For Noting

KT-311

1. PURPOSE

To provide background and process to date

- Board meeting 10/09/2015; Denel-Asia concept tabled
- Audit and Risk Committee meeting 22/10/2015; Denel-Asia business case presented for noting

KT-312

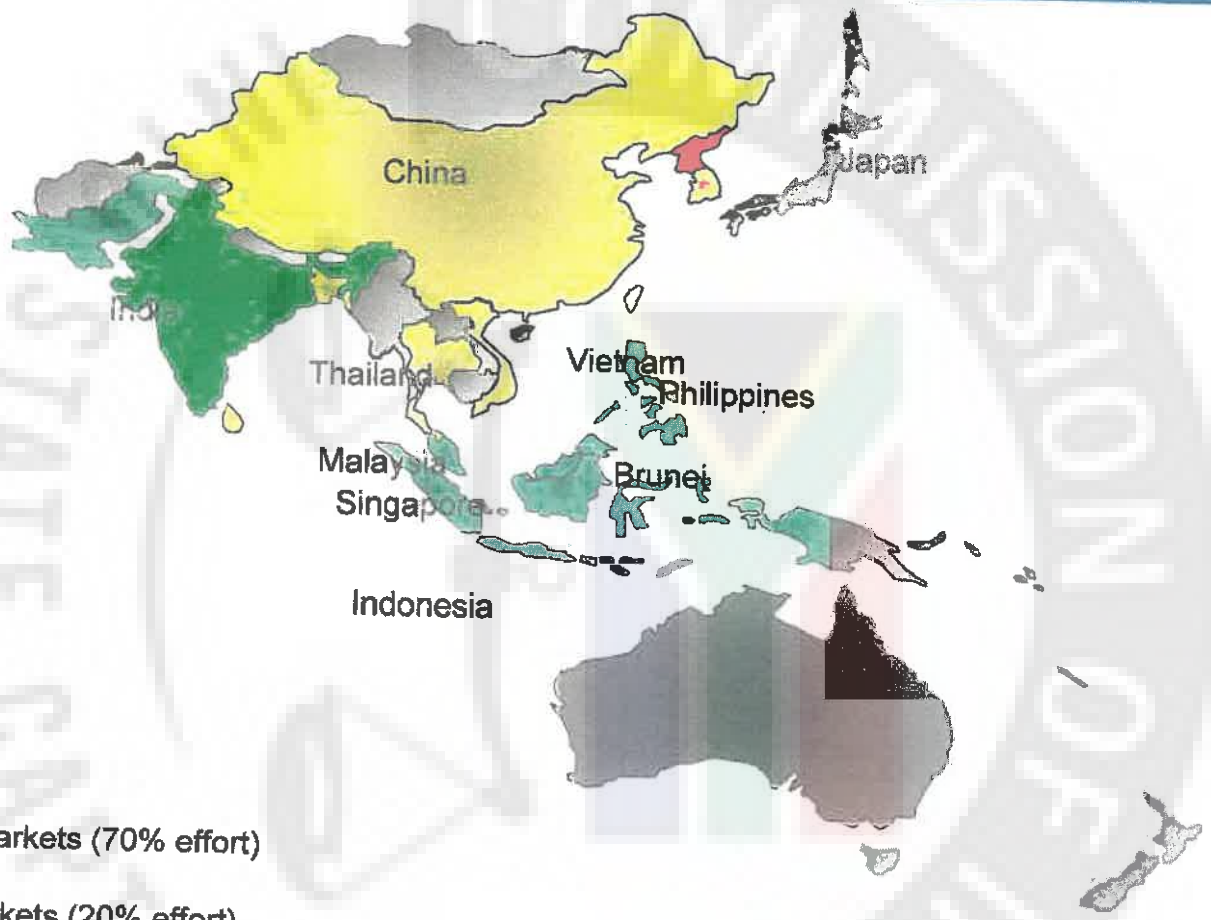
2. BACKGROUND

- Denel active in the region since the early 1990's with minimal success

- Denel's current regional strategy stratifies countries as follows;

KT-313

CURRENT DENEL STRATEGY



- Prime target markets (70% effort)
- Secondary markets (20% effort)
- Reactive approach (10% effort)
- No-Go countries

KT-314

3. RATIONALE

- Region perceived to be the leading global (excluding US) defense market, and a potent force in defense technology innovation.
- Because……

  Increasing defense spending

KT-315

3. RATIONALE

- by 2018 **Defense** budgets across the Asia-Pacific (excluding the US) expected to grow by over 19 percent to about USD612bn by 2018

- **Procurement** budgets expected to increase 28 percent

KT-316

3. RATIONALE

Projected Procurement Budget Increases by country

Country	% Increase (2014-2018)	Growth Focus
Singapore	18+	Technology Partners.
Cambodia	18+	R&D and Industry development focus.
Indonesia	18+	R&D and Industry development focus. Land Based systems
Vietnam	18+	R&D and Industry development focus. Land Based systems and Air Defence
India	25	Develop Industrial base. Land Based systems Artillery and Infantry weapon systems. Air Defence programs
Philippines	85	R&D and Industry development focus. Land Based systems and Air Defence.

3. RATIONALE

- **Research and development** projected growth 28 % – 29% from 2014 – 2018
- Half of non-US global defense procurement and 2/3 of non-US defense research and development spend in the region

Some factors contributing to the defense spend growth are.....

KT-318

3. RATIONALE

1. Rapid economic growth
   - National electricity grids
   - Sea lanes
   - Broadband, mobile telecommunications
   - Financial networks

New forms of protection = increased defense spending

KT-319

3. RATIONALE

2. Increasing Global terrorism

   Pakistan, Philippines, India, Thailand and Bangladesh – accounted for 36 percent of the rise in global terrorist

KT-320

4. BUSINESS ANALYSIS

Identified barriers to entry into this market:

- Lack of multilateral defense relationships
- Inability to provide funding solutions
- Inability to source local production and development partners (India)
- Unable to frequently engage with end user and industry

4. BUSINESS ANALYSIS

- Company visibility in the market place/region from a distance limited
- Need for a conduit for developing/aligning with local business networks
- Inability to participate in regional initiatives

KT-322

5. PROPOSAL

- To incorporate an offshore Hong Kong company that will provide immediate and urgent solutions to the issues raised in the Business Analysis

KT-323

6. INTERMEDIARY VS EQUITY PARTNERS

	Intermediary (Technical Advisor)	Equity Partner
Implementation	Less complicated	Legal structure, more complicated to form
Operational control	Limited	Full control
Sales	Fees make Denel non-competitive Can represent competitive products to same client	Competitive Pricing
Risk	Behaviour could harm Dénel's image Can represent competitive products to client	Permanent relationship with both parties sharing the risk
Foreign Direct Investment (FDI)		Able to go into partnership with local companies

KT-324

6. INTERMEDIARY VS EQUITY PARTNERS

Intermediary (Technical Advisor)	
Advantages	**Disadvantages**
Convenient Less complicated to implement Can cancel in the event of corruption. But that is reactionary	Harm Denel's image Operational control limited Technical Advisor fees can make Denel non competitive Technical Advisor can represent competitors to one client as there is no exclusivity Risky as Technical Advisor has insight into Denel activities and documents

Equity Partners	
Advantages	**Disadvantages**
Permanent relationship with both parties at risk Entity to source partners for foreign direct investment (FDI) (49%) of a defense company in India in line with 'Buy Make India' program (mounted artillery gun)	Legal structure more complicated to form

KT-325

7. CRITERIA FOR CHOOSING A PARTNER

- Provision of quick access to local potential production and development partners
- Deep understanding of the local market and industrial landscape
- Proven ability to align with local business networks
- Access to operational funding for a 5 year period.
- Proven ability to increase visibility in the market/region
- Ability to grow the business

KT-326

8. REGULATORY REQUIREMENTS

1. The P F M A requirements to be met:

- Financial Due diligence
- Legal due diligence
- Competition Commission (South Africa and foreign jurisdiction)
- A Shareholders Agreement finalised
- Licence Agreement finalised
- National Security – Security Clearance

KT-327

8. OTHER REQUIREMENTS

- Organisation for Economic Co-operation and Development (OECD)
- Management of Political Dynamics

KT-328

9. APPROVAL REQUIRED

1. Approval of the regional configuration
2. Approval of the partner identification criteria
3. Approval of the recommended Company X in line with criteria (Partner identification criteria approved)
4. Approval to provisionally engage with identified partner
5. Due Diligence to be conducted

10. FOR NOTING

1. Regulatory requirements
2. Business Case presentation done to Audit and Risk committee
3. Regulatory, Environmental Approval
   3.1 Regulatory Environment briefed and noted

KT-330

Annexure B. - Reserved Matters

Matters Requiring Approval

PART A

1. Altering or amending the Articles;
2. Approval of the Financial Statements received from the Board;
3. Merging with any other person or business or any consolidation, restructuring or reorganisation of the Company;
4. Sale, transfer or Disposal of all or substantially all of the assets of the Company;
5. Save as provided for in clauses26 and 27, Voluntary submission to the insolvency, winding-up, liquidation, dissolution or similar status for the Company;
6. Acquisition, whether by formation or otherwise, of any subsidiary of the Company or the disposal or dilution of the Company's interest, directly or indirectly, in any subsidiary of the Company, or establishing, opening or closing any new operations, branch offices or business sites in any jurisdiction, or the acquisition of the whole or part of the business or assets of another company or entity;
7. Any other matters reserved for approval or determination of the shareholders or a general meeting in accordance with the Companies Ordinance.
8. Any increase, decrease, capitalisation, consolidation, sub-division, purchase, cancellation or conversion of any part of the Company's issued share capital, or reduction in the Company's share capital, allotment of new Shares, alteration in any way of any of the rights or privileges attaching to any of the Shares or any other changes to the issued share capital of the Company;
9. Entering into by the Company of any contract or transaction, or the conduct by the Company of any abnormal or unusual matter, in each case which is not related to or in the ordinary and proper course of Business of the Company, or which is not on arm's length basis and fair market terms;

PART B

1. Appointment and removal of the Chairman of the Board.
2. Appointment of any Technical Advisor and/or payments for agents in countries that allow for these.

3. Approval of the annual and quarterly Budgets and the Business Plans and any material deviation therefrom;

4. Creating or issuing any Encumbrance or other security over the assets of the Company;

5. Negotiating, executing, renewing or terminating any contracts, agreements or arrangements with, or for the benefit of, any Director;

6. Other than in the ordinary course of business, commencing or discontinuing any litigation or arbitration as the plaintiff or claimant, or the settlement of any litigation or arbitration (whether as the plaintiff / claimant or defendant / respondent);

7. Making of any decision in relation to the allocation and/or payment of the VR Asia Loan

Annexure C. - Format of Deed of Adherence

Deed of Adherence

THIS DEED OF ADHERENCE is dated [*Date*]

BETWEEN

(1) [***New Shareholder***] of [*Address of New Shareholder*] (**"New Shareholder"**); and

(2) [**Denel Asia [Company Limited]**], a company incorporated in Hong Kong whose registered office is at [*Address*] (**"Company"**).

INTRODUCTION

(A) This Deed is supplemental to a Shareholders' Agreement made between Denel Soc Ltd and VR Laser Asia Limited dated [*Date*] (**"Shareholders' Agreement"**), a copy of which has been provided to the New Shareholder.

(B) The New Shareholder wishes to have transferred to it / him shares in the capital of the Company and in accordance with the terms of the Shareholders' Agreement. The New Shareholder has agreed to enter into this Deed.

(C) The Company enters into this Deed for itself and on behalf of and as agent for all the existing Shareholder(s) of the Company.

NOW THIS DEED WITNESSES AS FOLLOWS:

1. **INTERPRETATION**

In this Deed, except as the context may require, all words and expressions defined in the Shareholders' Agreement shall have the same meanings when used herein.

2. **COVENANTS AND AGREEMENT**

2.1. The New Shareholder hereby undertakes and covenants with the Company and with the other Shareholder(s) as legally binding obligations and commitments that it / he will adhere to and be bound by all the terms, conditions and obligations under the Shareholders' Agreement which are capable of applying to the New Shareholder as if the New Shareholder had been an original party to the Shareholders' Agreement and named therein.

2.2. The Company and each existing Shareholder shall be entitled to enforce the Shareholders' Agreement against the New Shareholder and the New Shareholder shall be entitled to all rights and benefits under the Shareholders' Agreement in each case as if the New Shareholder had been an original party to the Shareholders' Agreement and named therein.

3. **GOVERNING LAW**

This Deed shall be governed by and construed in accordance with the laws of Hong Kong. The dispute resolution provisions set out in Clauses 18.2 and 18.3 of the Shareholders' Agreement shall apply to this Deed and all matters arising from or connected with it.

IN WITNESS whereof this Deed has been executed the day and year first above written.

SIGNED SEALED and DELIVERED)
by [***New Shareholder***])
in the presence of:)

Witness' signature:
Witness' name:
Witness' address:
Witness' occupation:

The COMMON SEAL of)

Denel Asia SOC Company Limited])
was hereunto affixed with the authority)
of its directors and in the presence of)

_____ Director

_____ Director

Annexure D. - Approvals Framework

It is recorded that the figures reflected in the table below, shall, unless otherwise resolved by the Shareholders, automatically increase with each anniversary of the Signature Date, by the same rate of escalation and/or variation as agreed to by the Parties and failing agreement by inflation for the Financial Year in question, from time to time.

KEY: **A: Final approval** **B: Must agree/approval** **C: Originates**	**Shareholder approval (Reserved Matter Approval/s or simple majority)**	**Board**	**Executive Management**
ACQUISITION / EXPANSION			
Any acquisition of business, share acquisition or expansion into a new area of Business (including joint ventures and partnerships) requires the following:	A (Reserved Matter Approval)	B	C
A full feasibility study presented for consideration by the Board prior to commitment;			C
A post completion evaluation presented to the Board within one year of the effective date of the transaction.			

KEY: A: Final approval B: Must agree/approval C: Originates	Shareholder approval (Reserved Matter Approval/s or simple majority)	Board	Executive Management
The acquisition of a business, share acquisition or expansion into a new area of business (including joint ventures and partnerships).	A (Reserved Matter Approval)	B	C
The taking over or acquisition of the whole or a substantial part of the business of any other person or any merger or amalgamation with other companies or with any other business which would constitute a material transaction for the Company having regard to its assets and business.	A (Reserved Matter Approval)	B and C	

KEY: A: Final approval B: Must agree/approval C: Originates	Shareholder approval (Reserved Matter Approval/s or simple majority)	Board	Executive Management
ALTERATION OF SHARE CAPITAL			
The increase, alteration, acquisition and/or repurchase by the Company, or reduction of the issued and/or authorised share capital and/or share premium of the Company, including the allotment and issue of shares and/or buy-back of its shares by the Company and/or buy-in of shares by any Subsidiary of the Company and the authorisation to issue share certificates of the Company.	A (Reserved Matter Approval)	B and C	
ASSETS – INTANGIBLE			
The registration of trademarks, patents, designs and other IP.		A	C

KEY: A: Final approval B: Must agree/approval C: Originates	Shareholder approval (Reserved Matter Approval/s or simple majority)	Board	Executive Management
The sale, assignment, transfer or other disposition of any of the major part of the Company's intangible assets such as IP goodwill, logos, names, trademarks, copyright, patents or licences, or trademark, patent or licence agreements.	A (Reserved Matter Approval)	B	C
The licensing and/or sub-licencing of IP to any third parties.	A (Reserved Matter Approval)	B and C	
ASSETS – TANGIBLE			
The sale or scrapping of any tangible capital asset: Original cost greater than or equal to HK$50,000.00; Original cost less than HK$50,000.00.	A (simple majority)	B	C A
Policy with respect to minimum value to capitalise assets.		A	C

KEY: A: Final approval B: Must agree/approval C: Originates	Shareholder approval (Reserved Matter Approval/s or simple majority)	Board	Executive Management
Policy with respect to motor vehicles / company cars.		A	C
The purchase or sale of any immovable property or the hiring or letting or sub-letting of any immovable property by the Company otherwise than for the purposes of the ordinary course of company's Business.	A (Reserved Matter Approval)	B and C	
AUDIT			
The appointment or removal of the Auditors.	A (simple majority)	B	
Non-statutory audit or related work (including specialist accounting work): Greater than or equal to HK$50,000.00; Less than HK$50,000.00.	A (simple majority)	B	C A

KEY: A: Final approval B: Must agree/approval C: Originates	Shareholder approval (Reserved Matter Approval/s or simple majority)	Board	Executive Management
BORROWINGS AND INTEREST BEARING DEBT			
Policy with respect to borrowings and interest bearing debt.	A (simple majority)	B	C
The Encumbrance of any assets or furnishing of any guarantees, suretyships, undertakings, indemnities, cessions, pledges, other forms of intercession for the obligations of third parties other than in the ordinary course of business or in relation to the Company's funding activities or approved in the Business Plan.	A (Reserved Matter Approval)	B	C
The incurrence of any general banking facilities or the increase in any existing general banking facilities (whether or not utilised), any borrowing, whether interest bearing or not, financial leases.	A (simple majority)	B	C

KEY: A: Final approval B: Must agree/approval C: Originates	Shareholder approval (Reserved Matter Approval/s or simple majority)	Board	Executive Management
The establishment and opening of a banking account or the removal of a banking account from one banking institution to another or the creation of any inter-company borrowings.	B (simple majority)	A	C
Financial assistance to related and/or inter-related persons	A (Reserved Matter Approval/ Special Resolution)	B	
Inter-company loans and loans to directors and related and inter-related persons	A (Reserved Matter Approval/ Special Resolution)	B	
Policy regarding cheque payments and electronic transfers.	B	A	C
The incurring of long-term debts, the issue of any long-term debentures or any other material borrowing	A (Reserved Matter Approval)	B and C	

KEY: A: Final approval B: Must agree/approval C: Originates	Shareholder approval (Reserved Matter Approval/s or simple majority)	Board	Executive Management
BUDGET AND BUSINESS PLAN			
Annual budget (including lease expenditure and capital expenditure budget) and the Business Plan are to be approved by the Board at the 1st Board meeting immediately prior to the commencement of the financial year to which they relate.	A (simple majority)	B	C
The approval of the annual budget and Business Plan or any amendment and/or any departure from the annual budget or Business Plan.	A (simple majority)	B	C
Any action and/or decision which is not contemplated in, or necessary to give effect to, the Business Plan.	A (simple majority)	B and C	
Discontinuation or suspension of any of the business activities of the business.	A (simple majority)	B and C	

KEY: A: Final approval B: Must agree/approval C: Originates	Shareholder approval (Reserved Matter Approval/s or simple majority)	Board	Executive Management
CAPITAL EXPENDITURE			
A schedule of capital expenditure for presentation to the Board at each Board meeting detailing any item greater than or equal to HK$100,000.00 shown individually, and those less than HK$100,000.00 aggregated globally.			C
Approval for budgeted capital expenditure however financed: Greater than or equal to HK$100,000.00; Less than HK$100,000.00	A (simple majority)	B A	C C
Approval for unbudgeted capital expenditure equal to or in excess of HK$50,000 however financed.	A (simple majority)	B	C
CHANGE IN STATUS OF COMPANY			
The listing of the Company on any recognised exchange.	A (simple majority)	B and C	

KEY: A: Final approval B. Must agree/approval C: Originates	Shareholder approval (Reserved Matter Approval/s or simple majority)	Board	Executive Management
CONTRACTS AND AGREEMENTS			
The conclusion of any profit sharing arrangement.	A (simple majority)	B	C
The conclusion or termination of any material contract.		A	C
The conclusion or termination of any contracts outside the ordinary course of business or the scope of the approved Business Plan or the budgets.	A (simple majority)	B	C
Any payment plan agreed to with any creditor including trade creditors, banks and revenue services.		A	C
The disposal of any rights and/or obligations under any of the contracts concluded between the Company on the one hand and any third party on the other.		A	C

KEY: A: Final approval B: Must agree/approval C: Originates	Shareholder approval (Reserved Matter Approval/s or simple majority)	Board	Executive Management
The transfer of any class of shares in any of the Company's Subsidiaries to any Person other than the Company.	A (simple majority)	B and C	
A compromise entered into with the Company's creditors.	A (simple majority)	B and C	
The incurring by the Company of any material foreign exchange exposure, whether in the ordinary course of its trade or otherwise.	A (simple majority)	B and C	
DEBTORS			
Bad debt write-offs: Greater than or equal to HK$100,000.00; Less than HK$100,000.00.	A (simple majority)	B	C A

KEY: A: Final approval B: Must agree/approval C: Originates	Shareholder approval (Reserved Matter Approval/s or simple majority)	Board	Executive Management
The making of any loan to any third party (other than staff loans to the employees of the Company) exceeding HK$10 000 in aggregate, other than in the ordinary course of business of the Company.	A (simple majority)	B and C	
DEPOSITS			
Deposits by the Company held by third parties made in the ordinary course of business:		A	C
DISTRIBUTIONS			
Dividend policy.	A (simple majority)	B	
The application of any amounts received in respect of any key man life insurance policies taken out on the lives of any of the executive directors or key employees.	A (simple majority)	B	

KEY: A: Final approval B: Must agree/approval C: Originates	Shareholder approval (Reserved Matter Approval/s or simple majority)	Board	Executive Management
DONATIONS			
Policy.		A	C
Donations to organisations / individuals in cash or otherwise which in aggregate exceed HK10,000.00 in a calendar year.		A	C
EXPENDITURE			
Employee reimbursement claims:		B A	C C
The adoption or amendment of employment benefits for any employees including medical aid, pension, provident fund benefits as well as the provision of pensions to anyone otherwise than in terms of Applicable Law or a fund which the Company has established or joined.	A (simple majority)	B and C	

KEY: A: Final approval B: Must agree/approval C: Originates	Shareholder approval (Reserved Matter Approval/s or simple majority)	Board	Executive Management
The fixing and/or alteration of salaries and remuneration of Directors or senior executives of the Company and the payment of any discretionary bonuses, including without limitation, the CEO, COO and CFO or other senior executives of the Company.	A (Reserved Matter Approval)	B and C	
The appointment, dismissal and/or determination and/or increase of the remuneration of senior executives and any other key management staff / managerial level employees of the Company.	A (simple majority)	B and C	
The granting of any bonuses to any Director or senior executive of the Company	A (Reserved Matter Approval)	B and C	

KEY: A: Final approval B. Must agree/approval C: Originates	Shareholder approval (Reserved Matter Approval/s or simple majority)	Board	Executive Management
The institution of any legal proceedings other than those arising in the ordinary course of business (i.e. excluding any debt recovery litigation or litigation claims not exceeding HK$100,000.00	A (simple majority)	B and C	
The payment of any management fees by the Company to any third party.	A (simple majority)	B and C	
FINANCE LEASES AND RENTAL AGREEMENTS			
Policy with respect to finance leases and rental agreements.	A (simple majority)	B	C
Approval for finance lease and rental expenditure: Greater than or equal to HK$100,000.00 per month; Less than HK$100,000.00 per month.	A (simple majority)	B	C A

KEY: A: Final approval B: Must agree/approval C: Originates	Shareholder approval (Reserved Matter Approval/s or simple majority)	Board	Executive Management
FINANCIAL REPORTING			
Monthly management accounts incorporating an income statement, balance sheet and cash flow statement are to be distributed to the Board within 15 (fifteen) days of month-end.			C
Approval of the monthly management accounts.		A	
Audited financial statements are to be produced within 90 (ninety) days of the Company's financial year-end.	A (simple majority)	B	C
Approval of the annual financial statements.	A (simple majority)	B	C
Any material change in the financial and/or accounting policies as used for the financial statements.	A (simple majority)	B	C
The alteration of the Financial Year end of the Company.	A (simple majority)	B	

KEY: A: Final approval B: Must agree/approval C: Originates	Shareholder approval (Reserved Matter Approval/s or simple majority)	Board	Executive Management
ARTICLES			
The amendment of the Articles	A (Reserved Matter Approval)	B and C	

IN WITNESS whereof this Agreement was duly executed by the Parties on this the 10th day of December 2015.

The **COMMON SEAL** of

DENEL SOC LTD

was hereunto affixed with the authority

of its board and in the presence of

_____ Director

_____ Director

IN WITNESS whereof this Agreement was duly executed by the Parties on this the 10th day of December 2015.

The **COMMON SEAL** of

VR LASER ASIA LIMITED)

was hereunto affixed with the authority

of its board and in the presence of

_____ Director

_____ Director

ANNEXURE "B2"

COMMISSION OF INQUIRY INTO STATE CAPTURE

ENSafrica
1 North Wharf Square
Loop Street Foreshore Cape Town 8001
P O Box 2293 Cape Town South Africa 8000
docex 14 Cape Town
tel +2721 410 2500 fax +2721 410 2555
info@ENSafrica.com ENSafrica.com

PER EMAIL
Denel SOC Limited
Nellmapius Drive, Irene
Pretoria, Gauteng Province
Republic of South Africa
Attention: Fortune Legoabe/ Denise Govender
Email: FortuneL@denel.co.za / deniseg@dlsys.co.za
PRIVATE AND CONFIDENTIAL – SUBJECT TO LEGAL PRIVILEGE

Mr Z Bhyat /0402381 our ref
Ms F Legoabe / your ref
Ms D Govender

27 November 2015 date

Dear Fortune and Denise,

RE: DENEL SOC LIMITED / VR ASIA LIMITED: PROPOSED JOINT VENTURE

1. The above matter refers.

2. **BACKGROUND**:

We are instructed that:

2.1. Denel SOC Limited (**"Denel"**) has undertaken commercial discussions with each of:

2.1.1. VR Laser Asia Limited (Company Registration No.: 2111273), a Hong Kong private limited liability company, of Block A, 15/F, Hillier Comm Building, 65-67 Bonham Strand East, Shueng Wan, Hong Kong (**"VR Asia"**); and

2.1.2. VR Laser Services Proprietary Limited (Registration No. 2007/031329/07), a South African private company, of 10 Haggie Road (opposite Kent Road), Dunswart Ext 5, Gauteng, South Africa (**"VR RSA"**),

with a view to forming a joint venture company incorporated in Hong Kong Kong (**"JV Co"**) whereby, amongst other things:

2.1.3. JV Co would market and sell Denel product in the Asia Pacific region, and in the Republic of India (**"India"**) in particular;

2.1.4. Denel shall acquire and hold at least 51% (fifty one percent) of the entire issued share capital of JV Co;

2.1.5. VR Asia shall acquire and hold the remaining 49% (forty nine percent) of the entire issued share capital of JV Co;

2.1.6. Denel would supply its product to JV Co on arm-length, but preferential terms, in order to enable JV Co to on-supply the same to its customers in India; and

2.1.7. VR RSA would, on arms-length terms, be appointed by JV Co to manufacture product on behalf of JV Co;

2.2. on 27 October 2015, Denel concluded a written cooperation agreement with VR Asia ("**Cooperation Agreement**"), in terms whereof, amongst other things, it was agreed that, subject to (i) Denel's board of directors approving of the transaction and (ii) Denel obtaining the relevant approvals required in terms of sections 54(2) and 66 of the Public Finance Management Act, 1999 (Act No. 1 of 1999) ("**PFMA**"), -

2.2.1. VR Asia and Denel would establish JV Co under the name "Denel Asia";

2.2.2. JV Co would be used by the parties as the vehicle in which to market and supply Denel products to India;

2.2.3. VR Asia would over a period of 5 years fund JV Co, on loan account, in a maximum amount of R100,000,000.00, advanced in 5 equal annual payments of R20,000,000.00 each;

2.2.4. VR Asia would procure that it would introduce its sales leads and marketing prowess to facilitate JV Co acquiring business in Asia. VR Asia would also assist JV Co in its supply obligations to Asian customers; and

2.2.5. VR Asia and Denel would conclude a shareholders' agreement in relation to JV Co in order to regulate their respective relationships as between themselves all on the terms as detailed in the Cooperation Agreement.

3. **INSTRUCTIONS AND MANDATE:**

3.1. We confirm that Denel instructed us to render legal and advisory services in relation to it and in particular to provide:

3.1.1. an open source anti-money laundering/anti-bribery forensic due diligence investigation in relation to VR Asia and/or JV Co and/or their respective affiliates, if any (collectively, the "**Due Diligence**");

3.1.2. advice on incorporating JV Co;

3.1.3. negotiation support in relation to the proposed arrangements with VR Asia and/or JV Co;

3.1.4. drafting and/or commenting on all applicable transactional documents required; and

3.1.5. preparing opinions for Denel in relation to compliance with all regulatory matters, including in particular:

3.1.5.1. the rationale for using Hong Kong as the country of incorporation for JV Co;

3.1.5.2. the viability of the business case and intended operations of JV Co, as this will directly impact on costings and funding requirements;

3.1.5.3. impact of the National Conventional Arms Control Act, 2002 (Act No. 41 of 2002) ("**NCAC**") in relation to JV Co; and

3.1.5.4. the impact of the Competition Act, 1998 (Act No. 89 of 1998), in relation to JV Co.

4. EXECUTIVE SUMMARY

4.1. We emphasise that this executive summary must be read in conjunction with the remainder of this advisory letter. It is not intended to be a stand-alone section, and all of the terms, limitations and qualifications highlighted in **Annexure A**, apply equally hereto.

4.2. For the reasons that follow, we are of the opinion that:

4.2.1. <u>in relation to the Due Diligence</u>:

4.2.1.1. there are certain "red flag" items/risks identified, as detailed therein which ought to give Denel caution – These relate primarily to (i) the industry in which the business is to be conducted, (ii) historic adverse press and (iii) the presence of politically exposed persons.

4.2.1.2. these "red flag" items/risks identified are however not insurmountable and provided that Denel implements the measures opined on in the Due Diligence report (including in particular (i) having a detailed anti-corruption policy and compliance framework), (ii) actively monitoring activities so as to ensure rigorous adherence to the said anti-corruption policy and compliance framework, these risks can be mitigated; and

4.2.1.3. based on the information supplied to us (and in cognisance of the mandate and scope contained in our Due Diligence report), we are unable to comment on and/or determine:

4.2.1.3.1. the extent of VR Asia's marketing networks in Asia and in particular, India; and

4.2.1.3.2. VR Asia's ability to meet its funding obligations in relation to JV Co. We understand that VR RSA is to fund VR Asia but in our view, VR RSA, may not itself be in a position to so fund VR Asia unless (a) its business is and/or becomes more profitable and/or (b) VR RSA's shareholders' grant financial assistance to VR RSA;

4.2.2. in relation to incorporating the JV Co in Hong Kong: We have requested clarity from VR Asia and/or VR RSA in relation to the chosen jurisdiction but as at the date hereof, we were not furnished with any reasons therefore. Based on the information supplied to us (and in cognisance of our mandate and scope), we are thus unable to find a cogent reason for incorporating JV Co in Hong Kong, as opposed to any other jurisdiction in the World;

4.2.3. Transactional documents: Pursuant to our mandate, we instructed Hong Kong counsel, Deacons, to prepare a subscription and shareholders' agreement in compliance with the provisions of the Cooperation Agreement and Hong Kong Laws. In addition, we have discussed and negotiated these provisions with the representative of VR Asia. Subsequent to the aforegoing, the latest draft of this agreement is enclosed herewith for your perusal, consideration and further comment, if any. We note that subsequent to our negotiations with VR Asia, there is no longer a need for the conclusion of a licence agreement between Denel (as provider) and JV Co (as client); and

4.2.4. General Advice and Opinions:

4.2.4.1. Pursuant to our mandate, we instructed Indian counsel, Singhania and Partners LLP, to advise us regarding Indian aspects of JV Co. A copy of such advice is enclosed herewith for your information and records.

4.2.4.2. We note that generally, the transaction to be pursued with VR Asia would be subject to receipt of the following approvals, namely:

4.2.4.2.1. Denel's board of directors approving the same;

4.2.4.2.2. VR Asia's board of directors approving the same;

4.2.4.2.3. Denel's shareholder approving the same in accordance with the provisions of sections 51(1)(g), 54(2) and 66 of the PFMA;

4.2.4.2.4. JV Co being appropriately licenced in terms of the National Conventional Arms Control Act, 2002 (Act No. 41 of 2002); and

4.2.4.2.5. Denel obtaining approval from the financial surveillance department of the South African Reserve Bank for the establishing of a subsidiary outside of the common monetary area.

4.2.4.3. In our view, no approvals are required from the relevant Competition Authorities of South Africa or Hong Kong in relation to the establishment of JV Co.

5. **ADVICE:**

5.1. Due diligence:

We enclose herewith a copy of our limited high level open source due diligence review report incorporating an overview of discussions of the financial position and cooperation agreement entered into with VR Asia, dated 26 November 2015. A summary of this Due Diligence report is contained at paragraph 4.2.1.

5.2. Advice on Incorporating the JV Co in Hong Kong:

5.2.1. We understand that, -

5.2.1.1. Hong Kong is Asia's business capital in that it has one of the best locations and transport links across Asia;

5.2.1.2. all of the Asian region's key markets are within 4 hours flight time,

5.2.1.3. Hong Kong has a well-established common law system based on English law, where the rule of law is upheld by an independent judiciary. This legal system coupled with a permissive regime regarding capital movement and a laissez-faire approach to business activities encourage investment. This is in turn supported by Hong Kong's low and simple tax system. Corporate profits tax is a maximum of 16.5%, and personal income tax 15%. There is no sales

tax, no withholding tax, and no tax on capital gains, dividends or an individual's estate; and

5.2.1.4. Hong Kong recently undertook a comprehensive exercise to rewrite its Companies Ordinance (Cap. 32) with the aims of modernising Hong Kong's company law and enhancing its status as a major international business and financial centre.

5.2.2. We note however that in so far as Denel is concerned, it is not particularly concerned regarding maximisation of tax efficiency. The choice of jurisdiction within which to establish JV Co is thus a neutral one for Denel. Denel's proposed joint venture partner, VR Asia may however be more attuned to the maximisation of tax efficiency, hence its recommendation of Hong Kong as the jurisdiction of choice. Although we had requested clarity regarding this from VR Asia, we have yet to hear their views.

5.2.3. We note further that:

5.2.3.1. Hong Kong does not in fact have a double tax agreement between it and India. Consequently, there may be tax leakages between conducting business in India and remitting profits thereof to Hong Kong. This is however not a position that we have fully considered nor do we opine thereon;

5.2.3.2. Dubai, United Arab Emirates, may also be considered by JV Co as a base of its operations (notwithstanding its incorporation in Hong Kong) due to ease of travel and proximity to India. We have requested clarity regarding this from VR Asia but as at the date hereof, we have yet to hear their views; and

5.2.3.3. conducting business in India may require that JV Co establish a presence and/or a corporate entity in India. Consequently, there may be a duplication of entities and structures – with the JV Co being in Hong Kong and an operating entity in India. This may result in duplication of costs and governance requirements. We have however not considered these aspects fully nor do we opine thereon.

5.2.4. Based on the information supplied to us (and in cognisance of our mandate and scope), we are thus unable to find a cogent reason for incorporating in Hong Kong, as opposed to any other jurisdiction in the World.

5.3. **Transactional documents**:

5.3.1. We note that:

5.3.1.1. the Cooperation Agreement contains fairly extensive and detailed provisions regarding the establishment and operation of JV Co. This detailed arrangement has thus been used as the basis on which to draft the proposed shareholders' agreement in relation to JV Co; and

5.3.1.2. intensive and positive discussions was held with Mr Pieter van der Merwe in his capacity as representative of VR Asia on 25 November 2015, at Denel's office, at which a number of in-principle agreements were reached.

For ease of reference, we enclose herewith a draft of the latest version of the shareholders' agreement in relation to JV Co reflecting the said principles of the Cooperation Agreement and our negotiations and discussions with Mr van der Merwe. We note further that after consideration and debate with Mr van der Merwe it was agreed that Denel need **not** conclude any licence agreement with JV Co provided that Denel would need to support VR RSA's proposed manufacturing processes for product to be sold by JV Co. This is an aspect regulated in terms of the draft shareholders' agreement.

5.3.2. By way of summary we advise that the draft shareholders' agreement:

5.3.2.1. contemplates that:

5.3.2.1.1. JV Co will serve as a centralised marketing and sales office in Asia, with a particular focus in India;

5.3.2.1.2. JV Co will seek to supply Denel products to Indian customers by way of:

5.3.2.1.2.1. preferential procurement of product from Denel; and

5.3.2.1.2.2. VR RSA supplying contract manufacturing and specialised fabrication services to it; and

5.3.2.1.3. JV Co will primarily be funded by VR Asia;

5.3.2.2. recognises that Denel remains in control over a number of key aspects of the business and operations of JV Co;

5.3.2.3. recognises that JV Co would be subject to the same governance and compliance framework as that of Denel, including it too being subject to the provisions of the PFMA; and

5.3.2.4. delineates the respective roles and contributions of Denel and VR Asia to JV Co.

5.4. **General Advice and Opinions**:

5.4.1. In relation to Hong Kong competition law aspects, we advise that while there is a competition law coming into effect in Hong Kong later this year, there is currently no general merger control approval/filing system in Hong Kong. There are however merger rules which already apply specifically to the telecoms industry, but we assume that those would not apply to JV Co.

5.4.2. We enclose herewith an advisory memorandum prepared by Singhania and Partners LLP detailing the applicable legal framework in India in relation to JV Co as is relevant to the Indian defence and armaments procurement industry including in particular the applicability and impact of:

5.4.2.1. any tax treaty or investment protection treaty that may be in existence between India and Hong Kong and/or India and the United Arab Emirates;

5.4.2.2. the Defence Procurement Procedure 2013 – Capital Procurement and its emphasis on indigenisation;

5.4.2.3. the Foreign Investment Promotion Board;

5.4.2.4. the Foreign Exchange Management Act, 1999;

5.4.2.5. the Reserve Bank of India; and

5.4.2.6. the Companies Act, 2013; and

5.4.2.7. advice regarding any other pertinent considerations which Denel ought to be aware of in relation to JV Co undertaking business (in the defence sector) in India.

5.4.3. In relation to South Africa, we advise that:

5.4.3.1. as a state owned company, Denel is subject to the provisions and regulations of the Companies Act, 2008 (Act No. 71 of 2008) ("**Companies Act**"). As you are aware, the Companies Act has, via

section 72 of the Companies Act as read with regulation 43 to the regulations promulgated thereunder, introduced an obligation for Denel to appoint a Social and Ethics Committee ("**S&E Committee**");

5.4.3.2. the Denel S&E Committee must monitor Denel's progress and compliance with regard to the implementation of the OECD recommendations on corruption, as well as the duty to observe the United Nations' Global compact principles Principle 10 thereof creates a duty to reduce corruption;

5.4.3.3. in terms of the OECD recommendations for Multinational Enterprises on Combating Bribery, Bribe Solicitation and Extortion (2011), Denel should not, directly or indirectly, offer, promise, give, or demand a bribe or other undue advantage to obtain or retain business or other improper advantage. Denel must amongst other things:

5.4.3.4. not offer, promise or give undue pecuniary or other advantage to public officials or the employees of business partners;

5.4.3.5. not use third parties such as agents and other intermediaries, consultants, representatives, distributors, consortia, contractors and suppliers and joint venture partners for channelling undue pecuniary or other advantages to public officials;

5.4.3.6. develop and adopt adequate internal controls, ethics and compliance programmes or measures for preventing and detecting bribery, developed on the basis of a risk assessment addressing the individual circumstances of Denel; and

5.4.3.7. ensure, taking into account the particular bribery risks facing the enterprise, properly documented due diligence pertaining to the hiring, as well as the appropriate and regular oversight of agents, and that remuneration of agents is appropriate and for legitimate services only;

These obligations have been catered for in the draft shareholders' agreement in relation to JV Co;

5.4.4. in our view, Denel is not required to seek or obtain any permissions under the Competition Act, 1998 (Act No. 89 of 1998) as its proposed transaction in relation to JV Co, as the transaction does not satisfy the requirements of *inter alia* sections 3(1) and 12 of the Competition Act, 1998;

5.4.5. in relation to the provisions of the NCAC, it is our view that JV Co will be required to (i) register and (ii) apply to National Conventional Arms Control Committee for a permit under section 13 of the NCAC in order to enable it to export controlled product from South Africa for end-use in India;

5.4.6. in addition to the NCAC, it is our view that if and to the extent that JV Co will seek to export firearms and ammunition from South Africa, it would need to register with Registrar under the Firearms Control Act, 2000 (Act No. 60 of 2000);

5.4.7 in relation to exchange control aspects, we advise that:

5.4.7.1. Denel, as a Schedule 2 entity under the PFMA may make an investment outside of the common monetary area which does not exceed R1 billion with the approval of an authorised dealer;

5.4.7.2. in order to obtain permission, it is required that Denel submit to its authorised dealer amongst other things:

5.4.7.2.1. its name and registration number, as well as the names and domicile of its shareholder;

5.4.7.2.2. its latest available audited Financial Statements verifying, *inter alia*, the nature of its business;

5.4.7.2.3. an outline of the anticipated benefits of the foreign direct investment; and

5.4.7.2.4. proposed structure through which the foreign target entity will be held, including details of existing or new foreign holding companies; and

5.4.7.3. it is to be noted that the following criteria will be strictly applied by Authorised Dealers when considering a request by Denel, namely:

5.4.7.3.1. Denel may not use tax haven countries as a conduit for outward foreign direct investments elsewhere in the world. This moratorium is not applicable where the investment is made directly into a tax haven country; and

5.4.7.3.2. at least 10 per cent of the foreign target entity's voting rights must be obtained.

6. We trust that the above is in order and look forward to hearing from you. Should we not have made ourselves clear, or should you wish to discuss matters further, please do not hesitate to contact the writer.

Yours faithfully,

EDWARD NATHAN SONNENBERGS INC. T/A ENSAFRICA

PER: Zeyn Bhyat

(THIS LETTER WAS ELECTRONICALLY TRANSMITTED, HENCE IS NOT SIGNED)

COMMISSION OF INQUIRY INTO STATE CAPTURE

Annexure A Qualifications, Benefit and Limitation

QUALIFICATIONS, BENEFIT AND LIMITATION

1. QUALIFICATION AND ASSUMPTIONS:

1.1. The views expressed in this advisory letter are based on our understanding of the facts, as instructed and our interpretation of the South African law as at the date hereof. We thus emphasise that our interpretations, as expressed in this advisory letter, may be subject to change, dependent on the fact and as our law develops or as further insights are gained.

1.2. In expressing our opinion herein, we have assumed that:

1.2.1. all signatures on all agreements reviewed and/or referred to in this letter (collectively, the "**Agreements**"), whether originals or copies, are genuine, and all the Agreements are authentic and complete;

1.2.2. none of the parties to the Agreements were subject to or responsible for any duress or undue influence, misrepresentation, mistakes, corruption, collusion or any other circumstances that would in law render any of the Agreements void or voidable;

1.2.3. the conclusion and entering into of the Agreements is not and would not be deemed to be a fraudulent preference, and the Agreements have been entered into in good faith and not with the intention to defraud creditors;

1.2.4. the Agreements comprise the only agreements relating to the transactions contemplated by the parties and there are no agreements or arrangements in existence between the parties to the transactions which affect, amend or vary the terms of the transactions as set out in the Agreements;

1.2.5. all the Agreements and documents furnished to us have been validly and duly authorised and executed; and

1.2.6. the Agreements and all obligations to be performed under them which are governed by laws other than South African law, are legal, valid and binding and enforceable in accordance with their tenor under such governing law.

2. BENEFIT AND LIMITATIONS

2.1. We are qualified to practice law in South Africa and do not purport to be experts on, or to express any opinion herein concerning any other law other than the laws of South Africa. We have reviewed a number of documents and/or Agreements which are subject to the laws of jurisdictions other than that of South Africa. We have reviewed such documents from a

common-sense perspective and have assumed the application of general legal principles similar to South African law. Save as expressly indicated to the contrary, we have not sought the advice of local counsel on the contents of these documents or this advisory letter.

2.2. This advisory letter is:

2.2.1. provided to Denel and the Denel group of companies solely for its use and benefit and may not be relied upon by any other person, nor transmitted to any other person, nor quoted or referred to in any public document, nor filed with any governmental agency or person, without our express consent; and

2.2.2. is given solely based on the facts and law known to us as at the date of this advisory memorandum and we have no duty to update this advisory letter or to inform you of any changes to facts or South African law.

2.3. The opinions contained herein are confined to the matters stated herein and do not extend, by implication or otherwise, to any other matter and are limited to South African law as of the date of this advisory letter.

2.4. As a stipulation for the benefit of the directors (and employees) from time to time of Edward Nathan Sonnenbergs Inc. ("**ENSafrica**"), acceptable by it/them at any time without notice, ENSafrica's total aggregate liability for any claim whatsoever arising as a result of the opinions set forth in this advisory letter shall be limited to and shall not exceed the amount recovered by way of recourse against ENSafrica, its assets and its professional indemnity cover as read with ENSafrica's standard terms of engagement. There shall be no direct recourse against the directors, officers or employees of ENSafrica in connection with this advisory letter.

ANNEXURE "B3"

COMMISSION OF INQUIRY INTO STATE CAPTURE

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MEMORANDUM OF ADVICE

To: Zeyn Bhyat, Edward Nathan Sonnenbergs Inc. t/a ENSafrica

From: Ravi Singhania

Reference: 0402381

Dated: 03 December, 2015

We understand that VR Laser Asia Limited, a company incorporated in Hong Kong (**"VR Asia"**) and Denel SOC Limited, a company incorporated in South Africa (**"Denel"**) has entered into a cooperation agreement wherein VR Asia and Denel propose to incorporate a Joint Venture company in Hong Kong (**"NewCo"**). Denel will hold 51% equity shareholding of the NewCo and VR Asia will hold remaining 49%. The NewCo will market and supply Denel's products in the Asian Market. The following products of Denel will be marketed and supplied in India:

1. Turrets/Vehicles (Infantry Fighting Vehicle Program);
2. T6 Artillery Turrets
3. T5-52 Truck Mounted Artillery Gun;
4. G6-52 Wheeled Artillery Gun;
5. SS77 Machine Gun;
6. 35mm Air Defence Cannon;
7. Automatic Grenade Launcher;
8. NTW20 Anti-Materiel Rifle;
9. Unmanned Aerial Vehicle;
10. 155mm Ammo; and
11. Bi-Modular Charges.

The following products will be marketed and supplied in Bangladesh:

1. 105mm Towed Artillery Gun;

New Delhi
P-24, Green Park Extension,
New Delhi 110016, India
t: +91 (11) 4747 1414
e: delhi@singhania.in

Bangalore
401, Prestige Meridian II
30, Mahatma Gandhi Road
Bangalore 560001, India
t: +91 (80) 4113 1900
e: blr@singhania.in

Hyderabad
614, Babukhan Estate
Basheer Bagh
Hyderabad 500001, India
t: +91 (40) 4210 2424
e: hyd@singhania.in

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2. 155mm Towed Artillery Gun;
3. 105mm Ammo;
4. 155mm Ammo; and
5. Bi-Modular Charges.

In light of the above, we herein below discuss the provisions of the Indian legislations/regulations with respect to defence and armaments procurement which will have impact on the above transaction:

Legal framework in India -

The Indian legal system is similar to the English legal system. It has a written constitution, which is quasi-federal in nature. There are two sets of governments, one at the central level and the other at state level and the distribution of powers between them is enshrined in the Union, State and Concurrent lists. The Union List is exclusively reserved for the federal parliament and includes subjects like, national defence, incorporation of companies, banking etc. The State List on the other hand is exclusively reserved for various state legislatures and includes subjects like, agriculture, land and trade and commerce within the state; The Concurrent List contains subjects on both the federal and states legislature.

The Supreme Court of India is the highest judicial forum in India. There are high courts having jurisdiction over a particular states. High courts are the principal civil courts of original jurisdiction in the state and can try all offences including death penalty. The courts at the district level administer justice at district level. These courts are under administrative and judicial control of the High Court of the relevant state. The district court has appellate jurisdiction over all subordinate courts situated in the district on both civil and criminal matters. Subordinate courts, on the civil side (in ascending order) are, Junior Civil Judge Court, Principal Junior Civil Judge Court, Senior Civil Judge Court. Subordinate courts, on the criminal side (in ascending order) are, Second Class Judicial Magistrate Court, First Class Judicial Magistrate Court and Chief Judicial Magistrate Court.

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Those companies incorporated in India are governed by the Companies Act, 2013 and the rules laid thereunder. There are several other corporate laws which are applicable to Indian companies including wholly owned subsidiaries of a foreign body corporate such as Contract law, Securities and Exchange Board of India Act, Income Tax Act, Arbitration Act etc.

A. HISTORICAL BACKGROUND OF VR ASIA IN INDIA

Pursuant to our extensive research on the website of Ministry of Corporate Affairs and various other ministries/organisations we did not find any information relating to the presence of VR Asia or its principals in India either directly or through any branch office or liaison office or a wholly-owned subsidiary. Further, consequent to our general research by the name of the company, we could not find any details of VR Asia or its principals present in the public domain.

B. FOREIGN EXCHANGE MANAGEMENT ACT, 1999 ("FEMA") AND RESERVE BANK OF INDIA ("RBI")

RBI has issued various regulations and rules under FEMA. A copy of the FEMA can be made available should you require. As per the relevant RBI regulations business in India, by a non-resident entity can only be done through certain specified entities/place of business. Depending upon the type of activities to be carried out, a foreign entity has the option to establish any of the following type of places of business:

1. Branch Office;
2. Liaison Office;
3. Project Office;
4. Subsidiary Company;
5. Joint Venture Company.

Foreign Exchange Management (Establishment in India of Branch or Office or Other place of business) Regulations, 2000 ("**Regulations**") issued under FEMA provide for establishment of a place of business viz. liaison office/branch office/project office in India. A copy of these can be made available should you require. The Regulations also prescribe the type of activities which may be undertaken by a liaison office, branch office or by a project office. It may be noted that the very name of the type of office indicates that only certain types of business activities can be carried out by each of these offices.

1. Branch Office

The Regulations have prescribed the following list of permitted activities which can be undertaken by a branch office in India:

(i) Export/Import of goods;
(ii) Rendering professional or consultancy services;
(iii) Carrying out research work, in which the parent company is engaged;
(iv) Promoting technical or financial collaborations between Indian companies and parent or overseas group company;
(v) Representing the parent company in India and acting as buying/selling agent in India;
(vi) Rendering services in Information Technology and development of software in India;
(vii) Rendering technical support to the products supplied by parent/group companies;
(viii) Activities of foreign airline/shipping company.

Retail trading activity of any nature is not allowed for a branch office in India.

Eligibility:

For a branch office, the applicant should have a profit making track record during the immediately preceding five (5) financial years in its home country and should also

have net worth being not less than USD 100,000 or its equivalent. It may be noted that branch office cannot undertake any manufacturing or processing activity, directly or indirectly except in Special Economic Zone (SEZ). Special Economic Zones (SEZ) are those regions in India approved by the concerned authority for trade and commerce in order to promote export of goods and services, manufacturing, FDI and other business activities in India. All the SEZs are governed by The Special Economic Zones Act, 2005 and rules laid thereunder. A copy of the relevant legislation can be made available should you require.

Also, in order to establish a branch office in India the prior approval of RBI has to be obtained. Further, a branch office is also required to be registered with the Registrar of Companies ("**ROC**") under the Indian Companies Act, 2013 ("**CA, 2013**"). A copy of the CA,2013 can be made available should you require.

Time-Line:

A branch office can be opened with the prior approval of RBI which can generally takes about 3-4 months.

Tax Liability

It may further be noted that a Branch office will be treated as a non-resident company in India and hence, any income earned by it in India will be taxed at the rates as are applicable to foreign companies. The rate of income tax applicable to foreign companies is higher as compared to the rates applicable to Indian companies. The current income tax rate applicable to foreign companies is 40%. In addition, there will be a surcharge of 2% or 5% of the income tax where total income is exceeding INR 10 million or INR 100 million respectively.

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2. Liaison Office

Under the Regulations, a liaison office has been defined as a place of business which acts as a channel of communication between the head office and entities in India, and does not undertake any commercial/trading/industrial activities. Further, liaison office is required to maintain itself out of the inward remittances received from abroad (from its head office) through normal banking channels. Following activities only have been permitted to be undertaken by a liaison office in India:

(i) Representing in India the parent company/group companies;
(ii) Promoting export import from/to India;
(iii) Promoting technical/financial collaborations between parent/group companies and companies in India.
(iv) Acting as a communication channel between the parent company and Indian companies.

Eligibility

Further for liaison office, the applicant should have a profit making track record during the immediately preceding three (3) financial years in its home country and should also have net worth being not less than USD 50,000 or its equivalent. Please note that in order to establish a Liaison office in India a prior approval of RBI have to be obtained. Further, a liaison office is also required to be registered with the Registrar of Companies under the CA, 2013.

Time-Line

A liaison office can be opened with RBI approval within 3-4 months.

It may be noted that a liaison office is treated as an extension of foreign company and hence its status in India will be that of a non-resident.

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3. **Project Office**

The Regulations also provide that a foreign company may open a project office in India provided it has secured from an Indian company a contract to execute a project in India. The object of setting up a project office is for the limited purpose of executing the contract awarded to it, e.g., for supply of goods/services in India or for executing an on-site project like installation, construction, erection and related services. The project life would also determine, as evidenced by the contract, the life of the project office as it does not generally extend beyond the life of the project. Also, project office can be established in India either under automatic route, or under approval route where prior approval of RBI has to be obtained. Further, a project office is also required to be registered with the Registrar of Companies under the CA, 2013.

Tax Aspect

It may be noted that a Project office will be treated as a non-resident company in India and hence, any income earned by it in India will be taxed at the rates as are applicable to foreign companies, which is 40% (exclusive of surcharge and cess). The rate of income tax applicable to foreign companies is higher as compared to the rates applicable to Indian companies.

We understand that the NewCo has not been awarded with any project in India and therefore, it cannot establish its project office in India. Further, it cannot establish a liaison office as liaison office is not permitted to carry out any commercial, trading or industrial activity in India. Therefore, NewCo will not be able to enter into the market and supply the products of Denel in India through its liaison office. The NewCo can establish its branch office in India, however, the same can act only as a buying or selling agent or can carry out other permitted activities as stated above. Keeping in view the proposed activities of NewCo in India, it would be more appropriate for NewCo to set up a branch office in India. However, whether branch office would be an eligible entity

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under DPP will depend on the terms of procurement. So, NewCo may also consider to initially open a Liaison office for purpose of liaisoning in India. Once, the terms of procurement are known then a decision may be taken as to whether a branch office or an Indian subsidiary would be a suitable entity.

Further, the NewCo will require registration under the CA, 2013 within 30 days of establishment of its place of business in India. The following documents/information shall be furnished to the concerned Registrar of Companies for registration:

- Approval from the RBI under FEMA or Regulations, and also from other regulators, if any, approval is required by NewCo to establish a place of business in India or a declaration from the authorized representative of NewCo that no such approval is required;
- A certified copy of the charter, statutes or memorandum and articles of the NewCo or other instrument constituting or defining the constitution of NewCo and, if the instrument is not in the English language, a certified translation thereof in the English language;
- The full address of the registered or principal office of NewCo;
- A list of the directors and secretary of the company containing such particulars as may be prescribed including (i) personal name and surname in full; (ii) any former names or names or surnames in full; (iii) father's name or mother's name and spouse's name; (iv) date of birth; (v) residential address; (vi) nationality; (vii) if the present nationality is not the nationality of the origin, then the nationality of the origin; (viii) passport number, date of issue and country of issue; (if a person holds more than one passport then the details of all the passports to be given); (ix) income tax permanent account number (PAN), if applicable, (x) whether directorship in any other Indian company , (Director Identification Number (DIN), Name and Corporate Identity Number (CIN) of the Company (xi) other directorships held and (xii) email id;
- The name and address or the names and addresses of one or more persons resident in India authorised to accept on behalf of NewCo service of process and any notices or other documents required to be served on it;

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- The full address of the office of NewCo in India which is deemed to be its principal place of business in India;
- Particulars of opening and closing of a place of business in India on earlier occasion or occasions;
- Declaration that none of the directors of NewCo or its authorized representative in India has ever been convicted or debarred from formation of companies and management in India or abroad; and
- Any other information as may be required.

Once the NewCo is registered under the CA, 2013, it will further need to comply with the following periodic requirements under the CA, 2013 and the Companies (Registration of Foreign Company) Rules 2014 ("**Rules**"). A copy of the aforesaid rules can be made available should you require:

1. NewCo shall prepare a balance sheet, profit and loss account of its Indian Business Operations in accordance with Schedule III of the CA, 2013 or as near thereto as may be possible for every financial year. NewCo shall then file the balance sheet and profit and loss account along with the following documents:
    - Documents relating to the copies of the latest consolidated financial statement of NewCo, as submitted by NewCo to the prescribed authority in the country of its incorporation;
    - Statement of Related Party Transaction;
    - Statement of Repatriation of Profits;
    - Statement of Transfer of Funds (including dividend if any) in relation of any fund transfer between place of business of Foreign Company in India and any other related party of foreign company outside India.

    It should be noted that the accounts shall be audited by a Chartered Accountant in India.

    Timeframe - Within 6 months of the close of the financial year of the foreign company to which the documents relate.

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2. NewCo shall ensure that it conspicuously exhibit on the outside of its office(s)/place(s) where it carries on business in India, in all business letters, bill-heads, letter-papers, notices and its other official publications, the name of NewCo and the country in which it is incorporated, in letters easily legible in English characters, and also in the characters in the language or one of the languages in the general use in the locality in which the office or place is situate.

   In case the liability of the members of NewCo is limited, it must also be conspicuously exhibited as indicated above.

   Timeframe - Immediately on registration.

Penalties for Contravention

It is pertinent to note here that non-compliance with the above is punishable under the CA, 2013. A non-complying Foreign Company is punishable with fine which shall not be less than INR 100,000 but which may extend to INR 300,000. Further, in case of any continuing offence, an additional fine which may extend to INR 50,000 for every day after the first during which the contravention continues, may be imposed.

Penalty for non-compliance is also provided for the officer of the Foreign Company who is in default which includes imprisonment for a term which may extend to six (6) months or with fine between INR 25,000 (USD 400 approximately) to INR 500,000 (USD 8,000 approximately) or both.

C. THE COMPANIES ACT, 2013

A foreign investor can also setup a subsidiary company in India by incorporating a company under CA, 2013 and bring in foreign investment in the form of equity capital for financing the business. The Indian subsidiary may also avail loan funding from its foreign shareholders subject to the External Commercial Borrowings (ECB)

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guidelines laid down under FEMA. As per the aforesaid guidelines, a company may avail a loan from its foreign equity shareholders up to USD 5 million if the lender is holding at least 25% of the equity shares capital in the company. ECB exceeding USD 5 million may be availed provided the lender is holding more than 25% of equity shares in the company and also the ECB liability-equity ratio shall not exceed 4:1 and subject to the other conditions which are required to be fulfilled for availing ECB including end use restriction. ECB shall have a minimum average maturity period of 3 years. Further, ECB can be utilised only for certain specified purposes like import of capital goods, new projects, infrastructure sector etc. Companies operating in manufacturing, infrastructure, hotels, hospitals and software sector may avail ECB from direct foreign equity holder for general corporate purposes provided the minimum average maturity of ECB is 7 years. ECB for general corporate purposes may also be availed by companies operating in other sectors with the prior approval of the Reserve Bank of India. The entity so established may be a joint venture or a wholly owned subsidiary company and may carry out any business activity subject to the Foreign Direct Investment (FDI) Policy. The copy of the FDI Policy can be made available should you require. The CA, 2013 provides that a company can be incorporated either as a private limited company or a public limited company.

A private limited company requires a minimum 2 (Two) shareholders and minimum 2 (Two) directors. As per Indian laws, a private limited company incorporated in India must have at least 2 (Two) shareholders and minimum 2 (Two) directors at all times during its existence. However, NewCo may appoint a nominee shareholder in order to comply with the aforementioned legal requirement. In case of nominee shareholder, the beneficial interest in shares held by nominee shareholder shall remain with NewCo. Shares of a private limited company are not freely transferrable, and invitation to public to subscribe for its shares or debentures is also prohibited. A private limited company can start its business operations immediately on the receipt of certificate of incorporation. **It is preferable to conduct business through private limited company as it requires fewer regulatory restrictions and compliances as compared to a public limited company.**

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A public limited company, on the other hand, requires minimum 7 (seven) shareholders and minimum 3 (Three) directors. Public company is required to adhere to more regulatory compliances than a private limited company. So, foreign companies generally prefer to set up its subsidiary as a private company. A public limited company can also start its business operations immediately on the receipt of certificate of incorporation.

Tax Aspect

A wholly owned subsidiary of a foreign company will be treated as an Indian company for all purposes. It will be taxed at the rates as are applicable to any other Indian company which currently is 30%. In addition, there will be surcharge of 5% or 10% of income tax where the total income is more than INR 10 million or INR 100 million respectively. Indian subsidiary, being a separate legal entity, will be solely liable for all its acts and obligations. Holding company, being only a shareholder of Indian subsidiary, will not be liable for any acts or obligations of the Indian subsidiary.

Timeline

A subsidiary company can be established in about 3-4 weeks, once all the requisite documents are in place. The document required by the ROC include but are not limited to the following:

1. Charter documents of the Company- Memorandum and Articles of Association of the proposed company.
2. Digital signature and Director Identification Number of the directors. For obtaining Digital signature and Director Identification Number
3. Board resolution of NewCo and other shareholder (in case of the company);

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4. No Objection Certificate (NOC) in case the name of the proposed subsidiary contains the name of the shareholders;
5. Identity and address proofs of the shareholders and directors;
6. Other declarations and documents as per the Act.

Further, a subsidiary company can be wound up with the permission of the high court and such procedure takes about 5-6 months.

Restriction on Foreign ownership:

FDI policy of the Government of India provides for various conditions for foreign ownership in Indian companies. 100% foreign investment is allowed in most of the sectors under "automatic route". Under automatic route no prior approval is required for foreign investment however, certain filings need to be done with the authorities post foreign investment in the Indian company. In few sectors there is a cap on foreign ownership. In some cases prior government approval is required for foreign ownership beyond the specified threshold.

Based on the information and/or documents provided to us, we understand that the NewCo will only be marketing and supplying the products of Denel i.e. defence products in India and would not do any manufacturing activities in India. In such a case, the Indian subsidiary of the NewCo will merely do the wholesale trading business and the same shall under fall under the "cash and carry wholesale trade" activity under FEMA. However, the items to be distributed are restricted items so the proposed activity may not qualify for "cash and carry wholesale trade". Consequently, Indian subsidiary would be able to undertake only advisory or liaisoning activities for NewCo.

However, please note that in the event any manufacturing activity (which may include assembling of partly constructed product) is carried by the Indian subsidiary of NewCo, the same shall fall under the defence sector in FEMA. Foreign Direct Investment under the defence sector is allowed upto 49% under

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automatic route i.e. no approval is required upto 49%. However, Foreign Direct Investment above 49% may be permitted with the prior approval of Foreign Investment Promotion Board..

Since the products of NewCo and its subsidiary are restricted products and cannot be market or sold in the wholesale market. **Therefore, in our view it is advisable to form a liaison office in India which would help NewCo to facilitates with the government authorities and market its products in India.**

Foreign Investment Promotion Board ("**FIPB**")

In order to obtain FIPB approval, NewCo will be required to file an online application along with the necessary documents. The list of documents required to be submitted for obtaining the aforesaid approval are as follows:

1. Summary of Proposal;
2. Certificate of Incorporation(COI);
3. Memorandum of Association(MOA) and Articles of Association (AOA);
4. Board Resolution;
5. Audited Financial Statement of the last financial year;
6. Income Tax Return of the last year;
7. A copy of the JV agreement/shareholders. Agreement/ technology transfer/trademark/brand assignment agreement, as the case may be;
8. Diagrammatic representation of the flow and funds from the original investor to the Investee Company and Pre and Post shareholding pattern of the Investee Company; and
9. The comments of the Indian partners/technical/trademark collaborators about the new venture, on their official letter heads, with name and contact address of the signatory of the comments.

Upon submission of the aforementioned documents, all the original documents are required to be submitted physically with the FIPB within 10 days of filing an online application. Consequent to which FIPB, if it deems fit, will extend its approval. In the

event that the applicant could not submit the documents within 10 days of filing an online application then the application filed shall be deemed to be cancelled.

D. DOUBLE TAXATION AVOIDANCE AGREEMENT (DTAA)

- **Between India and Hong Kong**

  India does not have any tax treaty with Hong Kong as on the date of this memo. However, it is understood that India is undergoing negotiations with Hong Kong to enter into a tax treaty.

- **Between India and United Arab Emirates (UAE):**

  DTAA has been entered into between the Government of India and the UAE for avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and on capital. DTAA was entered into on 22nd September, 1993 and various amendments have been made to it thereafter.

  DTAA provides that a person shall be liable to pay tax in a country only on that part of income which arises in that country and shall not be taxed for the same income in the other country.

  For the purposes of DTAA entered into between India and UAE, the term "permanent establishment" (PE) plays a very vital role in determining the location where the income would be taxable. As per DTAA, PE means a fixed place of business through which the business of an entity is wholly or partly carried on. It includes a place of management, a branch, an office, a factory, a workshop, etc.

  PE shall not include the following:

  1. The use of facilities solely for the purpose of storage, display or delivery of goods or merchandise belonging to the enterprise;
  2. The maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage, display or delivery;

3. The maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise;
4. The maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise, or of collecting information, for the enterprise;
5. The maintenance of a fixed place of business solely for the purpose of carrying on, for the enterprise, any other activity of a preparatory or auxiliary character.

As per DTAA, the manner in which tax on various kinds of income shall be paid by the person is as follows:

Business Profits

DTAA provides that the profits of an entity shall be taxable in that particular country only where it is carrying on the business. However, if an entity carries on business in the other country through a permanent establishment situated in that other country, then the profits of the entity may be taxed in that other country also, but only for the amount that is attributable to that permanent establishment situated in the other country.

Immovable Property

If any income is derived by a person from any immovable property situated in the other country, then that person shall be liable to pay tax on such income only in that other country where the immovable property is situated and will not be taxed for the same in its own country.

Also, in case any capital gain is derived by a person from the alienation of any immovable property situated in the other country, then tax for the same has to be paid only in that other country where the property is situated and will not be taxed for the same in its own country.

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Dividends

With regard to the dividends paid by a company of one country to any resident of the other country, tax is to be paid in that other country. However such dividends may also be taxed in the country where the company is located depending on the laws of that country.

Royalty

With regard to the income tax on royalty income arising in one country and are paid to a resident of the other country, tax is to be paid in that other country. However, such royalties may also be taxed in the country where they arise, depending on the laws of that country.

E. DEFENCE PROCUREMENT PROCEDURE, 2013 ("DPP")

The DPP covers all the capital acquisitions undertaken by the Ministry of Defence, Defence Services and Indian Coast Guard and provides the procedure for procurement of defence equipment. However, the Defence Public Sector Undertakings and Defence Research and Development Organisation will continue to follow their own procedures for procurement.

The DPP covers procedure for following capital acquisitions:

- Acquisition covered under the 'Buy' decision: 'Buy' is further classified as "Buy (Indian)" and "Buy (Global)". 'Buy' means an outright purchase of equipment. Buy (Indian) means purchase from Indian vendors while Buy (Global) means purchase from Indian as well as foreign vendors. However, for acquiring equipment from Indian vendors, there has to be a minimum of 30% indigenous content on cost basis.

- Acquisition covered under the 'Buy & Make' decision: This will include purchase from a foreign vendor followed by licensed production or indigenous manufacturing in India.
- Acquisition covered under the 'Buy & Make (Indian)' decision: This will include purchase from an Indian vendor followed by licensed production or indigenous manufacturing in India. The requirement under this acquisition is of having a minimum of 50% indigenous content on cost basis.
- Acquisition covered under the 'Make' decision: This will include high technology complex systems or critical components to be designed, developed and produced indigenously.

In light of the above, we believe that the proposed transaction will fall under 'Buy (Global)' acquisition wherein the equipment will be purchased from the foreign vendor.

The acquisition process would involve following functions:

1. Services Qualitative Requirements (SQRs);
2. Acceptance of Necessity (AON);
3. Solicitation of Offers;
4. Evaluation of Technical offers by Technical Evaluation Committee (TEC);
5. Field Evaluation;
6. Staff Evaluation;
7. Oversight by Technical Oversight Committee (TOC) for acquisitions above INR 3 billion (Approximately USD 50 million);
8. Commercial negotiations by Contract Negotiation Committee (CNC);
9. Approval of Competent Financial Authority (CFA);
10. Award of Contract/ Supply Order (SO);
11. Contract Administration and Post Contract Management.

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It is to be noted that as per the DPP, preference will be given to indigenous design, development and manufacture of defence equipment. Whenever the required arms, ammunition and equipment are possible to be made in India within the time lines required by the Defence services, the procurement will be made from indigenous sources. A locally incorporated company would qualify as being from an indigenous source.

Further, for the defence procurement procedure under the 'Buy (Global)' acquisition the provisions of Defence Offset Guidelines will also have to be followed. These provisions are applicable in case of outright purchase from a foreign vendor where the estimated cost of the acquisition proposal is Indian Rupees 3 billion or more. 30% of the estimated cost of the acquisition will be required value of the offset obligations. The discharge of offset obligations can be done through following methods:

1. Direct purchase or executing export orders for eligible products manufactured by, or services provided by Indian enterprises;
2. Foreign Direct Investment in joint ventures with Indian enterprises for the manufacture and/or maintenance of eligible products and provision of eligible services;
3. Investment in 'kind' in terms of transfer of technology (TOT) to Indian enterprises for the manufacture and/or maintenance of eligible products and provision of eligible services;
4. Investment in 'kind' in Indian enterprises in terms of provision of equipment through the non-equity route for the manufacture and/or maintenance of eligible products and provision of eligible services;
5. Provision of equipment and/or TOT to Government institutions and establishments engaged in the manufacture and/or maintenance of eligible products and provision of eligible services;
6. Technology acquisition by the Defence Research and Development Organization in areas of high technology.

The date of discharge of offset obligation under point 1 shall be the date of invoice or the date of final payment whichever is later. In case of point 2 till 6, the date of completion of the transaction shall be the date of discharge of offset obligation.

The offset condition will form a part of the Request for Proposal (RFP) and subsequently of the main contract. A separate offset contract will be executed simultaneously with the main contract. A copy of the standard form offset contract can be made available should you require

The responsibility to discharge the offset obligations shall be upon the vendor of the equipment under the main procurement contract. Offset obligations can be discharged within a time frame that can extend beyond the period of the main procurement contract by a maximum period of two years. A minimum of 70% of the offset obligation must be discharged by any one or a combination of point 1 to 4 above.

In case a vendor fails to fulfil the offset obligation in a particular year in accordance with the annual phasing as agreed in the offset contract, a penalty equivalent to 5% of the unfulfilled offset obligation will be levied on the vendor. The maximum amount of penalty that can be levied under the guidelines is 20% of the total offset obligation during the period of the main procurement contract. Any vendor who fails to implement the offset obligations will be liable to be debarred from participation in future defence contracts for a period upto 5 years.

DEFENCE PROCUREMENT MANUAL, 2009

In addition to the above, the foreign vendors have to comply with the provisions of Defence Procurement Manual, 2009 (**"DMP, 2009"**). The DPM, 2009 is applicable on procurement of goods and services by the Ministry of Defence or by any unit or establishment thereunder. Accordingly to DPM, 2009 "procurement' means acquiring all types of goods such as equipment, stores, spares, technical literature as well as all types of services including packing, unpacking, preservation, transportation, insurance etc.

Types of procurement under the DPM, 2009 includes:

- Capital Procurement;
- Revenue Procurement;
- Financial powers for procurement;
- Indigenous Procurement;
- **Foreign Procurement (Import);**

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- Central Procurement;
- Local Procurement

Foreign Procurement of goods and services is covered under chapter 9 of the DMP, 2009. The procedure of procurement includes:

1. Registration of foreign vendors with the service headquarters of ministry of Defence;
2. Receipt of indent (i.e. a requisition) along with the necessary documents duly approved and authenticated by the competent authority;
3. Selection of vendors by the competent authority;
4. Inviting tenders through global tenders enquiry or limited tenders enquiry or single tender enquiry or PAC enquiry;
5. The Request for Proposal (RFP) shall include:
    - Bidding procedures;
    - Contract terms;
    - Details of good an services;
    - Deadline for submission of quotations;
    - Technical Specifications;
    - Inspection clause;
    - Special Conditions;
    - Quality Assurance;
    - Mode and terms of delivery and transportation;
    - Delivery Schedule;
    - Arbitration;
    - Liquidated Damages;
    - Advance Payments;
    - Risk and Expense clause;
    - Force Majeure

The mode of payment to foreign vendors is through irrevocable Letters of Credit or Direct Bank Transfer (DBT). For contracts below USD 100,000, the payment shall be made only through DBT mode. In case of procurement of high value with long gestation period, performance security deposit in the form of bank guarantee is taken from the supplier. The

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DPM, 2009 provides for standard conditions of contract in case of foreign procurement including but not limited to:

- Commencement and validity of the contract;
- Prices should be lowest and inclusive;
- Terms of payment;
- Terms of Delivery;
- Inspection;
- Packaging and Dispatch;
- Warranty and claims;
- Technical Life;
- Termination of Contract; and
- Arbitration.

Therefore in light of the above laws applicable on the transaction and the nature of the business that the NewCo or its subsidiary would undertake in India, it is advisable to initially register a Liaison office in India for purpose of liaisoning with authorities in India. Once terms of procurement are known then an appropriate entity viz. branch office or a subsidiary company may be considered.

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COMMISSION OF INQUIRY
INTO STATE CAPTURE

DENEL SOC LIMITED

PROPOSED BUSINESS EXPANSION IN ASIA PACIFIC REGION

LIMITED HIGH LEVEL OPEN SOURCE DUE DILIGENCE REVIEW REPORT INCORPORATING OVERVIEW OF DISCUSSIONS OF FINANCIAL POSITION AND COOPERATION AGREEMENT ENTERED INTO WITH VR LASER ASIA LIMITED

PRIVILEGED AND CONFIDENTIAL

ATTORNEY CLIENT WORK PRODUCT

02 DECEMBER 2015

Prepared for Zeyn Bhyat of ENSafrica

ENSafrica Forensics (Pty) Ltd

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ENTITIES, INDIVIDUALS AND OTHER TERMINOLOGY REFERRED TO

Abbreviation	Entity	Nature of relationship
Aerohaven	Aerohaven Trading (Pty) Ltd	Minority shareholder in VR Laser RSA
CIPC	CIPC	Companies and Intellectual Property Commission of South Africa
Craysure	Craysure Investments (Pty) Ltd	Minority shareholder in VR Laser RSA
Denel	Denel SOC Limited	State-owned commercially driven company
Denel Asia / JV entity	Denel Asia	Anticipated name of the joint venture trading entity to be registered in Hong Kong
Denel Land Systems	Denel Land Systems	Division of Denel currently maintaining business relationship with VR Laser RSA
Elgasolve	Elgasolve (Pty) Ltd	Majority shareholder of VR Laser RSA
ENS	ENSafrica Forensics (Pty) Ltd	Independent consultants to Denel
Issar Capital	Issar Capital (Pty) Ltd	Sole shareholder of VRLS Properties
JIC Engineering Services	JIC Engineering Services (Pty) Ltd	A wholly owned subsidiary of Westdawn Investments (Pty) Ltd
JIC Mining Services Africa	JIC Mining Services Africa (Pty) Ltd	Provides core services to the mining industry. Westdawn Investments (Pty) Ltd acquired JIC Mining Services in 2006
Sahara	Sahara Holdings	Houses the Gupta family's IT interests
VRLS Investments	VRLS Investments (Pty) Ltd	Former holding company of VR Laser RSA
VRLS Properties	VRLS Properties (Pty) Ltd	Privately owned property company currently leasing premises to VR Laser RSA
VR Laser Asia	VR Laser Asia (Pty) Ltd	Recently incorporated privately owned company based in Hong Kong

VR Laser RSA	VR Laser Services (Pty) Ltd	Privately owned company registered in South Africa and based in Boksburg, South Africa
Westdawn	**Westdawn Investments (Pty) Ltd**	**Trading as JIC Mining – related entity and provider of loan finance to VR Laser RSA. Referred to in the media as a 'Gupta company' and reported to be the sole shareholder of Craysure Investments**
Abbreviation	**Individual**	**Nature of relationship**
A Gupta	Atul Gupta	Middle Gupta brother. Director of Sahara Holdings and Oakbay Investment
Burger	Stephan Burger	Chief Executive Officer – Denel Land Systems
Essa	Salim Aziz Essa	Active director of VR Laser RSA. Sole shareholder of VR Laser Asia. Sole shareholder and sole director of Elgasolve.
Govender	Pushpaveni Govender	Active director of VR Laser RSA
Lourens	Louis Botha Lourens	Active director of Craysure Investments Propriety Limited and Divisional Director of JIC Mining
McNeil	Ian McNeil	Former director and current operational manager of VR Laser RSA
Ntshepe	Zwelakhe Ntshepe	Acting Group Chief Executive Officer of Denel
R Gupta	Rajesh Gupta	Active director of Westdawn Investments
Ragavan	Ronica Ragavan	Active director and sole shareholder of Aerohaven. Active director of Westdawn. Close friend and business associate of Rajesh Gupta.
Sharma	Iqbal Sharma	Active director and owner of Issar Capital
Singhala	Kamal Singhala	Active director of VR Laser RSA
Tomsett	Claire Tomsett	Financial manager of VR Laser RSA
V Gupta	Varun Gupta	Nephew of Atul Gupta. Director of Shiva Uranium, Oakbay Investments, JIC Mining Services
Van den Berg	Gert Petrus Johannes Van Den Berg	Active director of Craysure Investments Propriety Limited and Financial Director of JIC Mining

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van der Merwe	Pieter van der Merwe	Chief Executive Officer of VR Laser RSA
Zuma	Duduzane Zuma	Son of President Jacob Zuma. Director of Westdawn. Close friend and business associate of Rajesh Gupta

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1. BACKGROUND

1.1. Denel is a state-owned commercially driven company and strategic partner for innovative defence, security, aerospace and related technology solutions. It groups together several defence and aerospace divisions and associated companies. Denel is managed as one integrated business with an executive management team responsible for daily operations, reporting to an independent Board of Directors appointed by the South African Government through the Minister of Public Enterprises.

1.2. VR Laser Asia is a shell company, duly registered in Hong Kong on 20 June 2014. VR Laser Asia is associated with VR Laser RSA by virtue of its common shareholding. VR Laser RSA is a privately owned entity duly registered on 31 October 2007 (with the operational business trading through former related entities since 1999) and specialises in the manufacturing of a variety of steel products for a broad range of end-users, including the defence, mining, rail and transport industries. VR Laser RSA is situated in Boksburg, with a factory area of almost 22,000 square meters.

1.3. Denel and VR Laser Asia entered into a cooperation agreement, signed on 27 October 2015 by Ntshepe (Acting Group Chief Executive Officer of Denel) and van der Merwe (Chief Executive Officer of VR Laser RSA). The cooperation agreement was signed after Asia and more particularly, India, were identified as key strategic regions for cooperation between the parties.

1.4. The parties agreed to register a company named Denel Asia in Hong Kong and committed to working together to:

1.4.1. support the requirements of key local and/or international clients;

1.4.2. trade in various defence products;

1.4.3. market, sell, manufacture and deliver products currently manufactured or sold by Denel; and

1.4.4. bid for or become involved in special projects for the provision of defence products and expertise as and when such opportunities arise within the identified Asian territories.[1]

[1] As set out in the 'Inputs to the Denel Asia Company Business Case – 9 October 2015' the preliminary identification of the following target territories have been stipulated: India, Bangladesh, Singapore, Thailand, Indonesia, Philippines, Vietnam and Myanmar.

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1.5. As detailed in the cooperation agreement, it is anticipated that:

1.5.1. Denel will own 51% of the issued share capital in Denel Asia ("the JV entity") and VR Laser Asia will hold the remaining 49% of the issued share capital of the JV entity.

1.5.2. Ntshepe and Burger will represent Denel, while van Der Merwe[2] and Singhala will represent VR Laser Asia on the Board of Directors of the JV entity.

1.6. Based on discussions between ENS and Fortune Legoabe ("Legoabe") of Denel (Group Legal Counsel), it was agreed that assistance was required in conducting independent interviews with management of VR Laser RSA in order to obtain a high level overview of the financial position of VR Laser RSA, to assist the Board of Denel in making an informed decision regarding any identified risks relating to the proposed business expansion in partnership with VR Asia. The specific mandate is set out in paragraph 2 below.

[2] We draw your attention to the fact that van der Merwe is not a statutorily appointed director of VR Laser RSA.

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2. MANDATE

Our brief from Denel management was a specific request to independently verify certain information relating to VR Laser RSA and VR Laser Asia insofar as these entities are to be involved in the planned business expansion into the Asia Pacific region, as follows:

2.1. Perform an open source anti-corruption due diligence on VR Laser RSA and VR Laser Asia;

2.2. Reporting on the **ultimate beneficiaries/controllers** of the aforementioned entities;

2.3. Reporting on whether the aforementioned entities have **existing business links/relationships in India** and other Asia Pacific countries;

2.4. Reporting on whether the aforementioned entities are able to **lawfully solicit business in the Asia Pacific region** and India in particular; and

2.5. Commenting on whether there is any substance to the indication by management of VR Laser RSA (in relation to VR Laser Asia) that the **entities have the financial wherewithal to fund** the soon-to-be registered Denel Asia in the amount of **R100 million,** to be advanced in five equal instalments (of R20 million) over the ensuing five year period.

Due to the tight deadlines for completion of this assignment, it was agreed with the management of Denel that we only utilise all open source information available and collated as part of the desktop anti-corruption due diligence on VR Laser RSA and VR Asia. Furthermore, we agreed to limit our review of operations and the current financial position of the aforementioned entities to high level discussions with management and key role players of the parties bound by the cooperation agreement. Due to the confidential nature of the business proposal, we have been specifically requested by management of Denel, not to contact any external third parties and not to independently verify or corroborate any verbal evidence provided by the relevant parties. Consequently, our financial review has been limited to discussions with management of VR Laser RSA without performing any formal financial due diligence procedures. As instructed in this regard, we have not obtained supporting documentary evidence to corroborate statements provided by management of VR Laser RSA or Denel during the interview process and during the high level review of the current financial position of the entities.

The open source due diligence review findings are set out in Section A of this document and the findings of the site visit and management interviews are set out in Section B of this document.

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3. LIMITATIONS

3.1. The findings set out in this high level due diligence review report are based on open source information gathered in the public domain as well as information provided to us by Denel and VR Laser RSA respectively and sourced during interviews conducted with various key staff members and stakeholders. Our high level findings are based on the facts established from documentation reviewed and information obtained during the course of the interview process which was performed over the course of one day and followed up by further information supplied to us. Should we receive any additional information after date of issuing this document, we reserve the right to amend our findings and recommendations as hereinafter contained.

3.2. The procedures followed in this high level financial review do not constitute an audit in accordance with International Standards on Auditing and we do not express an audit opinion. The findings of this review do not form part of any audit report.

3.3. Whilst every effort is made to reflect accurate and up to date information, we must also point out that we rely on third party databases to perform company, credit and media research and accordingly cannot guarantee the veracity of information sourced from third parties. The content of this document is derived from information found in the public domain, including company registers and media articles. Although we endeavour to be as comprehensive as possible in gathering information, we cannot guarantee the accuracy or completeness of information obtained from external sources and further, the scope of our review has been limited to the details as set out above.

3.4. As discussed with management, we have not been instructed to and have not been able to take reasonable steps to ensure that the information obtained is authentic and we cannot guarantee the veracity or accuracy of the information disclosed in our findings. Our findings are based on information at hand at the date of this document. As such, we cannot conclude that we have had sight of all relevant information. We have indicated below in this document, the extent to which we believe management should attempt to obtain supporting and corroborating evidence in order to make a suitably informed decision about the planned expansion of the business in the Asia Pacific region.

3.5. This document is to be used solely for the purposes and subject to the limitations as set out in this paragraph. This document may not be used for any other purpose, without our prior consent. Information is provided to you on the basis that it will remain confidential and will not be disclosed to any third party, unless agreed thereto in writing.

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4. EXECUTIVE SUMMARY: SECTION A: OPEN SOURCE ANTI CORRUPTION DUE DILIGENCE

4.1. You requested that we perform an open source, desktop anti-corruption due diligence check on VR Laser RSA and VR Laser Asia. Our enquiry includes a comprehensive check of "Politically Exposed Persons" (PEP's), available sanctions, embargo and watch lists. It also includes internet and media search inquires. These searches use open source databases and public information to search a wide range of business journals, websites, industry publications and mainstream media. We have performed a series of tests in order to identify potential adverse information regarding these entities / individuals or affiliations to government officials and/or politicians which might constitute a risk. The internet searches may include a profile portrayed by the public media, articles, papers and written scripts regarding the entity or individuals linked thereto, or prepared and/or published by the entity or individuals linked thereto.

4.2. By way of introduction we point out that a joint venture of the nature envisaged will be regarded by regulators as a high corruption risk. In this regard, the armaments industry *per se* is regarded by regulators as a high corruption risk industry, and further, the newly created joint venture will operate in jurisdictions, which are regarded by regulators as high corruption risk.[3] This means that Denel will have to initiate proportional anti-corruption controls that are greater than normal in order to remediate compliance risks.

4.3. Apart from the intrinsic risk flowing from the industry sector and jurisdiction of the proposed joint venture, the desktop due diligence review has identified a number of anti-bribery/corruption compliance concerns, ("red flags") which will have to be remediated, should Denel proceed with the opportunity.

4.4. The key red flags identified by the desk top review relate to adverse media, the participation of PEPS (explained below) and unlawful payments to a third party consultant in the United States which highlighted concerns related to adverse history as well as Anti-Corruption compliance deficiencies regarding the on-boarding of business partners, agents and intermediaries. These are detailed below:

[3] According to the Transparency International 2014 Corruption Perception Index, India is ranked 85 out of 174. South Africa is ranked 67 out of 174. The Corruption Perceptions Index ranks countries and territories based on how corrupt their public sector is perceived to be. Like India, a large number of the Asian countries appear at the bottom half of the index.

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4.4.1. We identified adverse media relating to VR Laser RSA and its reported links to the controversial Rajesh Gupta and to Duduzane Zuma. R Gupta is noted as an RCA as his brother was reportedly previously a special advisor to the Prime Minister of Lesotho. Zuma is the son of Jacob Zuma, the President of South Africa. The above individuals are regarded by regulators as politically exposed persons, (PEPS). The fact that PEPS are involved in the shareholding entities of VR Laser South Africa does not constitute a 'red flag' that cannot be remediated. Denel will have to ensure that the joint venture entity has "**adequate procedures**" that will mitigate the risk that the entity may secure unlawful business advantages flowing from relationships that PEPS might have with political office bearers. (As conveyed during our meeting, we can assist Denel with the development of "adequate procedures" for the joint venture).

4.4.2. The open source checks also identified that the sole shareholder and director of VR Laser Asia, Salim Essa is also a PEP, in that he is reflected on corporate databases as a non-executive director of Broadband Infraco, a licensed state owned company (SOC) in the telecommunications sector. Broadband Infraco was established to improve market efficiency in the long distance connectivity segment by increasing available long distance network infrastructure. Essa was appointed in October 2011. Due to this affiliation, Essa is flagged as a PEP. During 2006 Essa was reflected as an employee of the Department of Health. As conveyed, this risk can be remediated by the implementation of "adequate procedures" within the JV entity.

4.4.3. Further, additional media reports indicate that a retired United States Army major Dennis Haag admittedly illegally exported firearms to an employee of VR Laser RSA from 2008 to 2012 when Haag was a federally licensed firearms dealer. The filing further states that Dennis Haag pleaded guilty to receiving unlawful pay and to illegally shipping firearms to South Africa, facing a maximum of 25 years in prison and a fine of up to USD 1.25 million. There are a number of concerns emanating from the above incident.

4.4.4. The first concern is that adverse media regarding unlawful payments to a consultant is a red flag to a regulator. That history, coupled to the fact that Denel itself has adverse media related to its prior activities in India (even though Denel was never convicted of any charges), means that the JV entity may well be subject to greater scrutiny by regulators.

4.4.5. The second concern is that the above incident reflects that VR Laser's due diligence procedures regarding the appointment of consultants was historically not optimal. It will accordingly be important for Denel to implement robust due diligence procedures when the joint venture entity appoints business partners, agents and intermediaries.

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4.4.6. An additional concern that we noted from the above incident is that, even though VR Laser operates in the high corruption risk armaments sector, they do not appear to have an anti-bribery/corruption program with anti-bribery policies and procedures. In the light of the fact that we have confirmed that VR Laser South Africa is a strategic business partner of Denel, it may be useful for Denel to ensure that this deficiency is rectified in future. (The lack of anti-bribery policies and procedure was confirmed during the site visit and interviews and we record that the Chief Executive Officer of VR Laser South Africa indicated a willingness to agree to the implementation, adherence or acceptance of any Anti-Bribery policy should this be required).

4.4.7. We must point out that this identified weakness in respect of an existing business partner to Denel is indicative of the fact that there may be potential deficiencies in Denel's own Anti-Corruption Compliance Program as all business partners, agents and intermediaries of Denel should have certified that they have their own anti-corruption compliance programs and should be providing annual certifications that they will not bribe. We have also identified deficiencies regarding the implementation of anti-corruption clauses in contracts and agreements as well as representations and warranties which should be in place with business partners in order to protect Denel against being held accountable by regulators for the illicit activities of its appointed agents and intermediaries.

Anti-corruption compliance due diligence on business partners, agents and intermediaries is one of the critical elements of the OECD recommendations which have been built into regulation 43 of the South African Companies Act (act 71 of 2008), which as a state-owned company, Denel needs to comply with. As discussed in our meeting, we can assist Denel in ensuring that the company itself has **"Adequate Procedures"** to prevent bribery.

In order to mitigate the bribery risks in the proposed joint venture, we recommend that Denel use its influence as the majority shareholder to implement a robust anti-corruption compliance program within the joint venture entity, underpinned by controls and procedures to mitigate the bribery risk.

A robust internal control framework helps to prevent, detect and remediate corrupt activity within the organization. (In the event that the opportunity is pursued, we will provide Denel with an overview of the envisaged program which makes provision for "adequate procedures"

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This includes an anti-bribery policy, controls, training, monitoring and incorporates due diligence procedures for all appointed business partners, agents and intermediaries of the joint venture) as well as the specific recommendations set out above.

5. EXECUTIVE SUMMARY: SECTION B: SITE VISIT, INTERVIEWS AND HIGH LEVEL OVERVIEW OF VR LASER RSA (ADDRESSING FOUR QUESTIONS)

5.1. Ultimate beneficiaries/controllers of VR Laser Asia

5.1.1. The sole shareholder and director of VR Laser Asia is Essa.

5.2. VR Laser Asia's existing business links/relationships in Asia (specifically India)

5.2.1. VR Laser Asia is a shell company duly registered in Hong Kong, but is yet to commence trading.

5.2.2. VR Laser RSA is a related party entity that appears to be the operational and technical expertise behind the proposed business expansion into the Asia Pacific region in accordance with the cooperation agreement with Denel.

5.2.3. VR Laser RSA does not appear to have an international footprint with business operations solely trading in the South African market and unfavourable publicity with regards to a former subsidiary trading in the American defence industry.

5.2.4. VR Laser has a long standing business relationship with Denel, and more particularly their division, Denel Land Systems.

5.2.5. Management of VR Laser RSA will be looking to obtain synergies from their relationship with Denel, who they claim have the business connections and relationships in the Asian Pacific market.

5.3. VR Laser Asia's ability to lawfully solicit business in the Asia Pacific market

5.3.1. VR Laser Asia is a shell entity that is yet to trade in the Asian Pacific market

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5.3.2. VR Laser RSA does not yet appear to have taken into consideration the ability of Denel Asia to lawfully solicit business in Asia.

5.3.3. VR Laser RSA management have indicated that this is a consideration that the newly constituted Management Committee (set up in accordance with the cooperation agreement) will need to address, including concerns regarding laws and legislation in the target territories' jurisdictions.

5.4. VR Laser Asia's financial wherewithal to fund the operations over the next five years

5.4.1. VR Laser Asia is a shell entity that is yet to trade.

5.4.2. It appears that VR Laser RSA shareholders will be the ultimate providers of financial assistance and funders of the capital requirements to set up operations in the Asian Pacific market, but this fact cannot be confirmed.

5.4.3. It appears that VR Laser RVR SA has a number of politically exposed persons that have a vested interest in VR Laser RSA, who will ultimately fund the trading operations of Denel Asia.

It has been highlighted throughout our document that consideration of the applicable countries' and South African laws and regulations in respect of anti-corruption and anti-bribery compliance must be adhered to and that this represents a significant risk for the proposed JV entity.

We have however, made extensive recommendations to assist Denel in managing such risks. The anti-bribery/corruption compliance controls that we have recommended are designed to protect Denel and the proposed JV entity against potential risk of enforcement action. We also point out that the remedial measures that we have recommended will assist Denel and the proposed JV entity in mitigating potential penalties emanating from non-compliance. In this regard we point out that one of the greatest risks for the proposed JV entity relates to how that business secures opportunities in Asia and India. It will be imperative for the proposed JV entity to have optimal anti-bribery controls including robust due diligence of business partners, agents and intermediaries. In the absence of appropriate remedial controls the entity and potentially its parent, Denel could be held accountable for the illicit acts of third parties.

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SECTION A: DETAILED FINDINGS OF THE LIMITED HIGH LEVEL OPEN SOURCE DUE DILIGENCE REVIEW

6. VR LASER SERVICES (PTY) LTD ("VR LASER RSA")

6.1. Regulatory checks

6.1.1. In South Africa, searches were conducted with the Financial Services Board (FSB) of South Africa, the South African Reserve Bank, the South African National Credit Regulator (NCR), the South African Competition Commission, the South African Human Rights Commission and the Auditor-General of South Africa. In the United States, searches were conducted with the Securities and Exchange Commission (SEC) and the Office of Foreign Assets Control (OFAC). In addition to the authorities mentioned above, searches were conducted of international media and internet sources. The searches yielded that following results:

6.2. International media and internet searches

6.2.1. According to a document entitled "Broad Based Black Economic Empowerment Scorecard" published on the VR Laser RSA website and records filed with the Companies and Intellectual Property Commission of South Africa, VR Laser Services (Pty) Ltd, hereafter referred to as VR Laser Services, is a South Africa-based proprietary limited company registered under entity registration number 2007/031329/07 and VAT number 4690244837.

6.2.2. According to its website, VR Laser Services, established in 1999, is a manufacturer of steel products for the defence and security, mining, rail and transport industries. VR Laser RSA operates a steel plate processing centre in Boksburg.

6.2.3. VR Laser RSA's website lists the following individuals as members of the management team :

- Pieter van der Merwe – Chief Executive Officer
- Ian Mc Neil – Operations/Technical Manager
- Claire Tomsett – Financial Manager

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- Pieter Grundlingh – Manager Supply Chain and Integration
- Wikus Weber – Logistics and Security Manager

6.2.4. The website of the South African Aerospace Maritime & Defence Industries Association (AMD) lists VR Laser RSA among AMD's members.

6.2.5. A 1 April 2008 Creamer Media's Engineering News press release reported that VR Laser RSA secured a ZAR 270 million Black Economic Empowerment (BEE) deal with empowerment partner Benny Jiyane. The article further reported that the result of this agreement will result in a 30 percent BEE shareholding stake for VR Laser RSA. According to its website, VR Laser Services is a Level 3 contributor to Broad Based Black Economic Empowerment.

6.2.6. A 30 June 2009 Business Excellence article reported that VR Laser RSA is a major supplier of armour plate in South Africa. The biggest customer of VR Laser Services has reportedly been Land Systems South Africa, a subsidiary of the defence company BAE Systems Plc. The article further reported that VR Laser RSA imports steel from Swedish Steel AB.

6.2.7. According to a 19 March 2012 defenceWeb article, VR Laser RSA conducts business with Barloworld Equipment in the field of underground mining vehicles. The same article reports that VR Laser RSA's premises were visited by the Minister of Defence of Benin.

6.2.8. According to a 26 March 2014 publication on the website of the Bureau of Alcohol, Tobacco, Firearms and Explosives under the U.S. Department of Justice, during 2011 and 2012, Dennis Haag, a retired U.S. Army major, received unlawful pay worth about USD 40,000 from VR Laser RSA in return for representing them to obtain military contracts when Haag worked for the U.S. Military. However, there has been no evidence that any public contract, as a result of this arrangement, was actually obtained by VR Laser RSA. The filing further states that Dennis Haag admittedly illegally exported firearms to an employee of VR Laser RSA from 2008 to 2012 when Haag was a federally licensed firearms dealer. Dennis Haag pleaded guilty to receiving unlawful pay and to illegally shipping firearms to South Africa, facing a maximum of 25 years in prison and a fine of up to USD 1.25 million.

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6.2.9. Judi Haag, wife of Dennis Haag, also pleaded guilty to assisting her husband in receiving unlawful pay. She might receive a year in prison and a fine of USD 100,000. Both individuals were also proposed for debarment from participating in future federal contract work. Note that this article does not provide any further information on this case and research was unable to identify any further references to this case.

6.2.10. A 4 July 2014 Mail & Guardian article reported that :

6.2.10.1. VR Laser RSA is 25.1 percent owned by Craysure Investments, which in turn is owned by Westdawn Investments, company of Rajesh "Tony" Gupta and Duduzane Zuma, son of the South African president Jacob Zuma. The remaining 74.9 percent stake is held by Elgasolve, a company wholly owned by Salim Essa.

6.2.10.2. In June 2014, the National Union of Metalworkers of South Africa submitted a report to the Public Protector, raising concerns over a ZAR 50 billion tender for locomotives by the state-owned company, Transnet. The public procurement procedure was questioned, following accusations raised against Iqbal Sharma ("**Sharma**"), the chairperson of Transnet's tender board. Sharma allegedly negotiated a share purchase in VR Laser Services (Pty) Ltd., a potential subcontractor of the four winning bidders, in order to gain benefits from the tender. Rajesh "Tony" Gupta and Duduzane Zuma, son of the South African president Jacob Zuma, were reported to have secretly held stakes in VR Laser RSA since February 2014 through Craysure Investments, a subsidiary of their company, Westdawn Investments. Sharma denied any conflict of interest and claimed that VR Laser Services (Pty) Ltd did not and had no intentions to engage in business relations with Transnet. In August 2014, Iqbal Sharma filed a complaint with the Press Council of South Africa (PCSA) against Mail & Guardian, claiming that the news article was untruthful, misleading, unbalanced and has caused harm to his reputation and dignity. On 28 August 2014, the complaint was dismissed by the PCSA on the ground that the reporting was not determined to be malicious or have harmed Sharma's reputation and dignity.

6.2.10.3. VR Laser RSA is a registered supplier to Transnet, a state-owned rail transportation enterprise, of steel equipment for its locomotive fleet. The article further reported that since 2006 VR Laser Services has been providing services to Transnet totalling ZAR 1 million.

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6.2.11. A document published on the website of Saflii states that VR Laser RSA has been involved in a lawsuit with an individual named 'Andy Wehmeyer' to be heard on 4 June 2013 at Court 9D. No further details were provided, and research was unable to identify any additional references to this case.

6.2.12. A City Press article, sourced by News24.com, dated 31 August 2014 reported that VR Laser RSA had been supplying steel components for the Hoefyster project, launched by the Armaments Corporation for the supply of 264 infantry combat vehicles for South Africa's National Defence Force. However, Fikile Mhlontlo, financial director of the state-owned defence company Denel, responsible for the project, denied any involvement of VR Laser RSA.

6.2.13. According to a 27 August 2015 The Witness article, VR Laser RSA has been engaged in a contract for the provision of components and equipment to manufacturing new armoured vehicles for an army project in South Africa.

6.3. Directors

6.3.1. According to the Companies and Intellectual Property Commission ("**CIPC**"), the active directors of VR Laser are noted as :

Name	ID Number	Status	Appointment Date
Salim Aziz Essa	7801155017084	Active	14 January 2014
Pushpaveni Ugeshni Govender	7504240157085	Active	01 February 2015
Kamal Kant Singhala	9210256052180	Active	08 December 2014

6.4. Shareholders

6.4.1. According to Share Certificates provided by van Der Merwe the CEO of VR Laser RSA, the following entities are the shareholders:

- Elgasolve (Pty) Ltd – 649 ordinary shares
- Craysure Investments Propriety Limited – 251 ordinary shares
- Aerohaven Trading (Pty) Ltd – 100 ordinary shares

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7. PUSHPAVENI UGESHNI GOVENDER ("GOVENDER") – VR LASER RSA DIRECTOR

7.1. Background

7.1.1. Govender with South African identification number 750424 0157 085 is noted as an active director of VR Laser RSA.

7.2. Company links.

According to CIPC, Govender has 13 active directorships and 2 resigned. The table below summarises these associations:

Ref	Directorship	Registration Number	Director Type	Director Status
1	Pyramid Trading (Eleven)	2004/005032/07	Director	Active
2	All Craze 20	2002/022239/07	Director	Active
3	Itj Retails	2006/020447/07	Director	Active
4	Drisdale Investments	2006/038458/07	Director	Active
5	Mfazi Investments	2007/011822/07	Director	Active
6	Mahila Investments	2007/011858/07	Director	Active
7	S B Resources	2007/018402/07	Director	Active
8	VR Laser Services	2007/031329/07	Director	Active
9	Cyret Technologies	2008/014823/07	Director	Active
10	Aforika Borwa Mining Solutions	2014/162785/07	Director	Active
13	Before The Wind Investments 220	2006/019925/07	Director	Active
11	Bloemfontein It Solutions	2007/006613/23	Member	Resigned

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12	Before The Wind Investments 220	2006/019925/07	Director	Resigned

7.2.1. We suggest that Denel review the list of company associations to determine whether there are any potential conflicts which we may not be aware of.

7.3. Sequestration records

7.3.1. No sequestration records were found in the name of Govender.

7.4. International media and internet searches

7.4.1. No results were found for Govender.

7.5. Civil court record search

7.5.1. No court records or bad debt information was found on Govender.

7.6. Employment history

7.6.1. In 2010 Govender's employer is noted as Sahara Computers.

7.6.2. According to a Mail & Guardian article entitled *The Beginners' Guide to the Guptas* published in May 2013, Sahara is one of the better known Gupta companies. It is reported to be the first company established by the Gupta family after arriving in South Africa.

8. KAMAL KANT SINGHALA ("SINGHALA") - VR LASER RSA DIRECTOR

8.1. Background

8.1.1. Singhala with South African identification number 921025 6052 180 is noted as an active director of VR Laser RSA.

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8.2. Company links

8.2.1. According to the CIPC, Singhala has 2 active directorships. The table below summarises these associations:

Ref	Directorship	Registration Number	Director Type	Director Status
1	K2014107338 (South Africa)	2014/107338/07	Director	Active
2	VR Laser Services	2007/031329/07	Director	Active

8.2.2. We suggest that Denel review the list of company associations to determine whether there are any potential conflicts which we may not be aware of.

8.3. Sequestration records

8.3.1. No sequestration records were found in the name of Singhala.

8.4. International media and internet searches

8.4.1. According to SaveRisk.com, Singhala is reported to be a director of Doon Leisure and Hospitality Limited (a Public Company incorporated on 20 August 2004. The company is classified as Indian Non-Government Company and is registered at Registrar of Companies, Delhi).

8.4.2. Other directors include Mukul Teckchandani and Anil Kumar Gupta.

8.5. Civil court record search

8.5.1. No court records or bad debt information was found on Singhala.

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8.6. Employment history

8.6.1. In 2015 Singhala's employer is noted as VR Laser Services.

9. SALIM AZIZ ESSA ("ESSA") - VR LASER RSA Director AND VR LASER ASIA - SOLE DIRECTOR AND SOLE SHAREHOLDER

9.1. Background

9.1.1. Salim Aziz Essa with South African identification number 780115 5017 084 ("Essa") is noted as an active director of VR Laser RSA and the sole director of Elgasolve (Pty) Ltd, the majority shareholder of VR Laser RSA. Essa is also the sole director and shareholder of VR Laser Asia.

9.2. Company links

9.2.1. Essa is noted to be a non-executive director of Broadband Infraco, a licensed state owned company (SOC) in the telecommunications sector. Due to this affiliation, Essa is flagged as a PEP.

9.2.2. Broadband Infraco was established to improve market efficiency in the long distance connectivity segment by increasing available long distance network infrastructure. Essa was appointed in October 2011.

9.2.3. According to the CIPC, Essa has 37 active and 11 resigned directorships. The table below summarises these associations:

Ref	Directorship	Registration Number	Director Type	Director Status
1	VR Laser Services	2007/031329/07	Director	Active
2	Inca Energy	2009/022231/07	Director	Active
3	Elgasolve	2010/017836/07	Director	Active
4	Inca Komsberg Wind	2011/000151/07	Director	Active

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5	Targatorque	2011/009253/07	Director	Active
6	Ujiri Mining	2011/010963/07	Director	Active
7	Apartment 12216	2013/108204/07	Director	Active
8	Premium Security And Cleaning Services	2013/127549/07	Director	Active
9	Antares Capital	2013/184858/07	Director	Active
10	Trillian Holdings	2015/168302/07	Director	Active
11	Good Value 104 Investments	2007/252349/23	Member	Active
12	Broadband Infraco	1989/001763/30	Non-Executive Director	Active
13	Polycom Africa	2001/022154/07	Director	Active
14	Syf Investments	2002/017966/07	Director	Active
15	In Excess Trading 181	2003/004532/07	Director	Active
16	Khulu Telecoms	2003/019536/07	Director	Active
17	Southbridge Investment Company	2003/019537/07	Director	Active
18	Lutravert Investments	2010/010303/07	Director	Active
19	3 Syllables Trading	2010/017424/07	Director	Active
20	Nu Age Energy	2010/024567/07	Director	Active
21	Inca Velddrif Wind	2010/025059/07	Director	Active
22	Inca Swellendam Wind No 2	2011/000003/07	Director	Active
23	Inca Sutherland Solar	2011/000011/07	Director	Active

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24	Inca Moorreesburg Wind	2011/000162/07	Director	Active
25	Inca Gouda Wind	2011/000277/07	Director	Active
26	Inca Graafwater Solar	2011/003022/07	Director	Active
27	Inca Beaufort West Wind	2011/003094/07	Director	Active
28	Sam Ax Trading	2003/075157/23	Member	Active
29	Fifty Four On Fourth Investments	2007/080484/23	Member	Active
30	Moya Multimedia	2007/137351/23	Member	Active
31	Premium Security And Cleaning Services	2011/021469/23	Member	Active
32	Limpopo Roof Trusses	2006/159899/23	Member	Active
33	Premier Cleaning Chemicals	2007/238155/23	Member	Active
34	Inca Sweilendam Wind No 1	2011/000360/07	Director	Active
35	National Agricultural Development Project	2006/010137/07	Director	Active
36	Essa Steel Manufacturers	2000/070096/23	Member	Active
37	Inca Dana Bay Wind	2011/000371/07	Director	Active
38	Broadband Infraco	1989/001763/30	Director	Resigned
39	Yellow Star Trading 1099	2000/020259/07	Director	Resigned
40	Moxisign	2009/020089/07	Director	Resigned
41	Inca Kakamas Solar	2011/000446/07	Director	Resigned
42	Inca De Aar Solar	2011/000358/07	Director	Resigned

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43	Inca Vredendal Wind	2011/000359/07	Director	Resigned
44	Daqo South Africa	2012/198829/07	Director	Resigned
45	Gade Oil And Gas	2013/083265/07	Director	Resigned
46	Moya Multimedia	2009/014875/07	Director	Resigned
47	Frv Inca 3	2011/000065/07	Director	Resigned
48	Sodersa	2011/001419/07	Director	Resigned

9.2.4. We suggest that Denel review the list of company associations to determine whether there are any potential conflicts which we may not be aware of.

9.3. Sequestration records

9.3.1. No sequestration records were found in the name of Essa.

9.4. International media and internet searches

9.4.1. According to a 4 July 2014 Mail & Guardian article:

9.4.1.1. Essa is a business associate of Sharma, the chairperson of Transnet's board tender committee. The two are reported to have approached VR Laser and offered to purchase the company. The sale was purportedly agreed on in December for an "undisclosed sum".

9.4.1.2. In a move possibly designed to create distance between Sharma and the day-to-day operations of VR Laser – perhaps to ward off accusations of a direct conflict with his Transnet role – a company owned by Essa purchased VR Laser.

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9.4.1.3. Through his investment company, Sharma bought a related company, VRLS Properties, which owns the two factory premises where VR Laser operates.

9.4.1.4. John van Reenen, one of VR Laser's founding co-owners, confirmed that Sharma had bought VRLS Properties and that Essa had bought the operational side, VR Laser Services. However, Van Reenen recalled that during initial purchase negotiations Sharma represented both companies. "It was always made quite clear to me that he [Sharma] had this associate [Essa], who would be taking over the steel company, and that Sharma was negotiating on Essa's behalf."

9.4.1.5. Essa has previously been profiled as one of the "leaders" of Sharma's investment company, Issar Capital, which owns VRLS Properties. A screen grab of the Issar Capital website, taken in May last year, shows that Essa was then directly involved with Sharma in Issar Capital. Essa no longer appears on this website. Given this back story, Essa was strangely evasive about his connection with Sharma, claiming not to know who owned VRLS Properties. On being told that Issar Capital owns the property company, Essa said he had "heard of the name" and then hurriedly excused himself from the call. He did not respond to further written questions.

9.4.1.6. Sharma and Essa are co-directors in another business, solar panel manufacturing company Daqo South Africa, since November 2012. Daqo is headquartered in Issar Capital's Sandton office.

9.4.1.7. They are also co-directors in a third company, National Agricultural Development Project, since December 2012. This company is not located at Issar Capital. Incidentally, the company's share register shows that Sharma and Essa each acquired a shareholding in National Agricultural Development Project from Gupta-owned companies on the same day in November last year.

9.4.2. According to a 24 April 2015 Mail & Guardian article :

9.4.2.1. T-Systems made the bid for the Transnet contract as part of a consortium with state IT infrastructure company, Broadband Infraco.

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9.4.2.2. A T-Systems source said, while working with Infraco, T-Systems executives became acquainted with Salim Essa, an Infraco director.

9.4.2.3. Essa is a flamboyant businessperson, with wide-ranging business interests, who apparently loves to invite colleagues for cigars at his Melrose Arch offices after sealing a deal.

9.4.2.4. His associates include the Gupta family and Duduzane Zuma, his partners in an engineering firm that manufactures steel components intended for, among others, Transnet locomotives.

9.4.2.5. Essa's wife is also a co-shareholder with the Guptas and Zuma in the mining company, Shiva Uranium.

9.4.2.6. Another of Essa's associates is none other than Matjila, whom he advised about deals entered into by Kopano ke Matla when Matjila was its chief executive. Kopano is the trade union federation Cosatu's investment arm.

9.4.2.7. Another T-Systems source said, when it became clear that T-Systems risked losing the Eskom deal, Essa approached it and offered to help lobby Eskom to retain the contract. Essa "wiggled his tits", the source said, offering to lobby for T-Systems.

9.4.2.8. In return, said the source, Essa requested a fee.

9.4.2.9. The source said the approach was discussed by management, but was "never consummated" because of opposition by the T-Systems board.

9.4.2.10. The first T-Systems source confirmed hearing about Essa's approach through the company's grapevine, although the source claimed to have no direct knowledge of it.

9.4.2.11. T-Systems, in its response, ignored questions about Essa and said only that it was "confident that due process has been followed"

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9.4.2.12. It is unclear if Essa did lobby Eskom on T-Systems' behalf.

9.4.3. According to a 24 October 2014 Mail & Guardian article :

9.4.3.1. A SizweNtsalubaGobodo report, finalised in February this year, investigated the sale of Cosatu's old offices and purchase of new headquarters.

9.4.3.2. It found Kopano had acted for Cosatu and that a task team led by Matjila (Matjila was chief executive of Cosatu investment company Kopano ke Matla) negotiated both property transactions.

9.4.3.3. The report quotes Matjila as saying that the Kopano task team was "informally assisted" by a Salim Essa, who had "previously worked with Kopano ke Matla on an energy project, through an entity named Inca Energy, which was jointly owned by Kopano and Essa".

9.4.3.4. AmaBhungane identified Essa as a majority partner in a precision steel cutting company whose minority partner is owned by Rajesh Gupta and Duduzane Zuma.

9.4.4. According to a petition entitled *Expel the Guptas* on Petitions24.com:

9.4.4.1. Guptas are connected to Iqbal Sharma - ex DG of the DTi TISA and his cronies - Salim Essa and Matthew Moodley. They are the BEE partners in all the luxury good chains - LV, Gucci etc.

9.4.4.2. The petition has received 320 signatures to date.

9.5. Civil court record search

9.5.1. No court records or bad debt information was found on Essa.

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9.6. Employment history

9.6.1. In 2006, Essa's employer is reflected as the Department of Health. There are no recent employment records for Essa.

10. ELGASOLVE (PTY) LTD – VR LASER RSA SHAREHOLDER

10.1. Directors

10.1.1. According to the CIPC, the only active director of Elgasolve is:

Name	ID Number	Status	Appointment Date
Salim Aziz Essa	7801155017084	Active	2 December 2012

10.2. International media and internet searches

10.2.1. The Transnet SOC Ltd. debt note programme issued on the London Stock Exchange notes that Sharma is a director of Elgasolve. The relevant excerpt reads :

Mr. Sharma was appointed as an independent non-executive director of the Board of Directors on 13 December 2010. Mr. Sharma currently serves as executive chairman of Issar Investment Holdings (Pty) Ltd and as ***director of*** *Issar Capital (Pty) Ltd, Daqo South Africa (Pty) Ltd,* ***Elgasolve (Pty) Ltd (our emphasis)****, GMT Concepts (Pty) Ltd and Nulane Investments 204 (Pty) Ltd. He served previously as a member of the board of directors of the Export Credit Insurance Corporation of South Africa, the Immigration Advisory Board and the Proudly South African campaign. He was previously deputy director general at the Department of Trade and Industry in South Africa. Mr. Sharma obtained his Bachelor of Science (Honours) in Economics and Business Administration from the University of Wisconsin, Oshkosh.*

10.2.2. This statement however is not supported by CIPC, who notes Essa as the sole director.

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11. CRAYSURE INVESTMENTS PROPRIETY LIMITED - VR LASER RSA SHAREHOLDER

11.1. Directors

11.1.1. According to the CIPC, the active directors of Craysure are:

Name	ID Number	Status	Appointment Date
Louis Botha Lourens	6205315076082	Active	13 February 2014
Gert Petrus Johannes Van Den Berg	5304265035080	Active	13 February 2014

11.1.2. According to the website of Westdawn Investments (t/a JIC Mining), Louis Lourens is noted as a divisional director and Gert Van Den Berg as the financial director of JIC Mining.

11.1.3. The directors of Westdawn Investments (Pty) Ltd with registration number 2006/020386/07 are noted as:

- Rajesh Kumar Gupta (also known as Tony Gupta);
- Duduzane Zuma; and
- Ronica Ragavan

11.2. International media and internet searches

11.2.1. According to a 4 July 2014 Mail & Guardian article, Craysure is reportedly owned by Westdawn Investments, the Gupta-owned company that trades as JIC Mining. The same article reports that Jiyane, VR Laser's (then) empowerment partner, ceded his stake to Craysure Investments in February 2014. Jiyane first played dumb about the Gupta-Duduzane stake When challenged, Jiyane changed his tune, saying he "intended to sell" to Craysure subject to "certain confidential conditions". He later conceded that he had in fact been dealing with the Guptas, saying: "I think Craysure has something to do with Sahara."

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12. GERT PETRUS JOHANNES VAN DEN BERG ("VAN DEN BERG") – CRAYSURE INVESTMENTS DIRECTOR

12.1. Background

12.1.1. Van den Berg with South African identification number 530426 5035 080 is noted as an active director of Craysure Investments.

12.2. Company links

12.2.1. According to the CIPC, Van den Berg has 5 active directorships and 15 resigned directorships. The table below summarises these associations:

Ref	Directorship	Registration Number	Director Type	Director Status
1	Gerleka Investments	1996/014995/07	Director	Active
2	Sparax Trading 67	2005/009630/07	Director	Active
3	Lexshell 702 Investments	2006/028454/07	Director	Active
4	Newshelf 960	2008/005492/07	Director	Active
5	Craysure Investments	2013/173148/07	Director	Active
6	Lexshell 230 Investment Holdings	1998/018486/07	Director	Resigned
7	Rebserve Residential Services	1998/025428/07	Director	Resigned
8	Madoda Timber	1967/008856/07	Director	Resigned
9	Holley Agro-Industrial	1974/003658/07	Director	Resigned
10	JIC Mining Services (1979)	1979/004936/07	Director	Resigned
11	Molope Cleaning Services	1995/008872/07	Director	Resigned
12	Titan Timber	1996/003052/07	Director	Resigned
13	Faberin Investments	1997/015562/07	Director	Resigned
14	Muller And Muller Medical Electronics	1998/009480/07	Director	Resigned
15	M R S Residential Services	1998/012448/07	Director	Resigned
16	Miemanda Beleggings	1970/011845/07	Director	Resigned

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17	Erbessem Beleggings	1967/006521/07	Director	Resigned
18	M D P Beleggings	1978/000736/07	Director	Resigned
19	Professional Action	1980/000158/07	Director	Resigned
20	Malan En Du Preez Bestuursdienste	1986/016133/23	Member	Resigned

12.2.2. We suggest that Denel review the list of company associations to determine whether there are any potential conflicts which we may not be aware of.

12.3. Sequestration records

12.3.1. No sequestration records were found in the name of Van den Berg.

12.4. International media and internet searches

12.4.1. According to the South African Institute of Tax Professionals (SAIT) website, Van den Berg is noted as a Master Tax Practitioner (SA) of the Gauteng Branch. Entry was last updated: 2015/08/19.

12.5. Civil court record search

12.5.1. No court records or bad debt information was found on Van den Berg.

12.6. Employment history

12.6.1. In 2006 Van den Berg's employer is reflected as "Provisiale Hospitaal". There are no recent employment records for Van den Berg.

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13. LOUIS BOTHA LOURENS ("LOURENS") - – CRAYSURE INVESTMENTS DIRECTOR

13.1. Background

13.1.1. Lourens with South African identification number 620531 5076 082 is noted as an active director of Craysure Investments.

13.2. Company links

13.2.1. According to the CIPC, Lourens has 2 active directorships. The table below summarises these associations:

Ref	Directorship	Registration Number	Director Type	Director Status
1	Craysure Investments	2013/173148/07	Director	Active
2	Aforika Borwa Mining Solutions	2014/162785/07	Director	Active

13.2.2. We suggest that Denel review the list of company associations to determine whether there are any potential conflicts which we may not be aware of.

13.3. Sequestration records

13.3.1. No sequestration records were found in the name of Lourens.

13.4. International media and internet searches

13.4.1. Louren's LinkedIn profile reflects his current position as "Deputy CEO of JIC Mining Services (Pty) Ltd"

13.5. Civil court record search

No court records or bad debt information was found on Lourens.

13.6. Employment history

13.6.1. In 2008, Lourens' employer is noted as JIC mining services.

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14. AEROHAVEN TRADING (PTY) LTD – VR LASER RSA SHAREHOLDER

14.1. Directors

14.1.1. According to the CIPC the active directors of Aerohaven Trading are:

Name	ID Number	Status	Appointment Date
Ronica Ragavan	7709170007081	Active	27 June 2008

14.1.2. We note that Ronica Ragavan is also an active director of Westdawn Investments.

14.2. International media and internet searches

14.2.1. According to an article entitled *He Who Pays the Piper, Calls the Tune* published on Questia.com :

14.2.1.1. Both TNA Media and Infinity are controlled by India's Gupta family (a secondary source confirms that Atul Gupta is the Executive Chairman of TNA Media).

14.2.1.2. Infinity shareholders include Essel Media (35%), Oakbay Investments, the Gupta family's investment vehicle (35%), Mabengela Investments, a South African B-BBEE company (21%), and a further 9% is reserved for staff and management.

14.2.1.3. The biggest shareholder in Mabengela Investments is Duduzane Zuma, son of President Jacob Zuma, who holds a 45% stake, with other shareholders including Rajesh Kumar Gupta (25%), Aerohaven Trading (15%), Fidelity Investments (10%), Mfazi Investments (3%) and Ashu Chawla (2%).

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15. RONICA RAGAVAN (ALSO KNOWN AS RONICA GOVENDER) ("RAGAVAN") – AEROHAVEN TRADING DIRECTOR

15.1. Background

15.1.1. Ragavan with South African identification number 770917 0007 081 is noted as the sole director of Aerohaven Trading (Pty) Ltd.

15.2. Company links

15.2.1. According to the CIPC, Ragavan has 25 active directorships and 3 resigned directorships. The table below summarises these associations:

Ref	Directorship	Registration Number	Director Type	Director Status
1	Sahara Consumables	2001/019162/07	Director	Active
2	Barmin Mining	2005/043755/07	Director	Active
3	Tegeta Resources	2007/024754/07	Director	Active
4	Newshelf 960	2008/005492/07	Director	Active
5	Foskor Bee Spv 1	2008/027545/07	Director	Active
6	Wilink Telecoms	2007/035277/07	Director	Active
7	Woodlane Consortium	2007/031952/07	Director	Active
8	Tirupati Trading	2007/125533/23	Member	Active
9	Lilac Tree Trading	2004/027151/07	Director	Active
10	Sahara Systems	2000/007320/07	Director	Active
11	Annex Distribution	2002/023324/07	Director	Active
12	Micawber 492	2006/009606/07	Director	Active

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13	Micawber 495	2006/009891/07	Director	Active
14	Micawber 478	2006/013786/07	Director	Active
15	Tegeta Exploration And Resources	2006/014492/07	Director	Active
16	Westdawn Investments	2006/020386/07	Director	Active
17	JIC Engineering Services	2007/005004/07	Director	Active
18	Linkway Trading	2007/009012/07	Director	Active
19	Mfazi Investments	2007/011822/07	Director	Active
20	S B Resources	2007/018402/07	Director	Active
21	Aerohaven Trading	2008/014743/07	Director	Active
22	Localiga	2008/018512/07	Director	Active
23	Joviwiz	2013/032610/07	Director	Active
24	Claudia Henkel Investments	2006/117905/23	Member	Active
25	Radius Infratel (Sa)	2012/073788/07	Director	Active
26	Mahila Investments	2007/011858/07	Director	Resigned
27	Moneyline 1705	2007/026614/07	Director	Resigned
28	Oakbay Resources And Energy	2009/021537/06	Director	Resigned

15.2.2. We suggest that Denel review the list of company associations to determine whether there are any potential conflicts which we may not be aware of.

15.3. Sequestration records

15.3.1. No sequestration records were found in the name of Ragavan.

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15.4. International media and internet searches

15.4.1. According to a published JCPS Cluster Report regarding the investigation into the landing of a chartered commercial aircraft at air force base Waterkloof, Ragavan is cited as a representative of the Gupta family and in her capacity as such sent a letter to SAPS Provincial Commissioner on 19 April 2013 to request protection for the convoy travelling from the base to Sun City.

15.5. Civil court record search

15.5.1. No court records or bad debt information was found on Ragavan.

15.6. Employment history

15.6.1. In 2010 Ragavan's employer is reflected as Sahara Systems (Pty) Ltd. There are no additional historical employment records.

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16. VR LASER ASIA LIMITED ("VR LASER ASIA")

16.1. Regulatory Checks

16.1.1. In Hong Kong, searches were conducted with the Hong Kong Monetary Authority (HKMA), the Hong Kong Stock Exchange (HKEx), the Hong Kong Joint Financial Intelligence Unit (JFIU), the Hong Kong Independent Commission Against Corruption (ICAC), the Hong Kong Securities and Futures Commission (SFC), the Financial Reporting Council of Hong Kong, and the Financial Services and the Treasury Bureau of Hong Kong. In the United States, searches were conducted with the U.S. Securities and Exchange Commission (SEC) and the U.S. Office of Foreign Assets Control (OFAC). In addition to the authorities mentioned above, searches were conducted of international media and internet sources. There were no results for VR Laser Asia.

16.2. International media and internet searches

16.2.1. According to VR Laser Asia registration record, filed with the Hong Kong Integrated Companies Registry Information System (ICRIS), VR Laser Asia Limited was incorporated on 20 June 2014 as a private company limited by shares under commercial registration number 2111273. It is currently a live company.

16.2.2. According to VR Laser Asia's annual return filed with ICRIS, its registered office is located at Block A, 15/F Hillier Commercial Building, 65-67 Bonham Strand East, Sheung Wan, Hong Kong.

16.2.3. The ICRIS records list PAMM Corporate Secretary Limited as the company secretary and Salim Aziz Essa as the sole director of the VR Laser Asia. Salim Aziz Essa holds a South African passport and resides at 2 New Forest Road, Forest Town, Johannesburg 2193, South Africa.

16.2.4. The Inland Revenue Department Business Registration Office of Hong Kong reports that VR Laser Asia is registered under business registration number 63488433-000.

16.2.5. At the time of this document, no website was available for VR Laser Asia.

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16.2.6. The ICRIS records state that VR Laser Asia has an issued share capital of HKD 10,000 and lists Salim Aziz Essa as the sole shareholder.

17. INTERNATIONAL WATCHLISTS

17.1. VR Laser RSA and VR Laser Asia and the associated individuals mentioned in this document were checked against available international watchlists. Checks were conducted against the following names:

Name	Position
VR Laser Services Proprietary Limited	Subject company
VR Laser Asia Limited	Subject company
Craysure Investments Propriety Limited	Associated company
Elgasolve (Pty) Ltd	Associated company
Aerohaven Trading (Pty) Ltd	Associated company
Westdawn Investments (Pty) Ltd	Associated company
JIC Mining Services Africa (Pty) Ltd	Associated company
JIC Engineering Services (Pty) Ltd	Associated company
Van Reenen Steel (Pty) Ltd	Associated company
VRLS Properties (Pty) Ltd	Associated company
VRLS Investments (Pty) Ltd	Associated company
VR Mining Products SA (Pty) Ltd	Associated company
VR Dragline Maintenance (Pty) Ltd	Associated company

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Advanced Laser Cutting (Pty) Ltd	Associated company
CVR Air (Pty) Ltd	Associated company
Salim Aziz Essa	Associated individual
Ronica Ragavan	Associated individual
Gert Petrus Johannes Van Den Berg	Associated individual
Louis Botha Lourens	Associated individual
Pushpaveni Ugeshni Govender	Associated individual
Kamal Kant Singhala	Associated individual
Ravindra Nath	Associated individual
Varun Gupta	Associated individual
Rajesh Kumar Gupta	Associated individual
Duduzane Zuma	Associated individual

17.2. The review represents a check against over 900 international lists. Our compliance database searches were run on 12 November 2015, at which time all updates from the list-issuing bodies had been processed and were up to date.

17.3. The search yielded results for :

17.3.1. Atul Gupta – PEP – former Special Adviser to the Prime Minister of Lesotho

17.3.2. Rajesh Kumar Gupta – RCA (Relative or close associate) - brother of Atul Gupta

17.3.3. Duduzane Zuma – RCA (Relative or Close Associate) – Jacob Zuma's son

17.3.4. Aziz Salim Essa - (PEP - Politically Exposed Person) – Director of Broadband Infraco – SOE

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18. SUGGESTED REMEDIAL INTERVENTIONS

We set out below our suggested remedial interventions which will assist Denel in managing bribery and corruption risks:

18.1. To mitigate the bribery risks in the proposed joint venture, we recommend that Denel use its influence as the majority shareholder to implement a robust anti-corruption compliance program within the joint venture entity, underpinned by controls and procedures to mitigate the bribery risk. A robust internal control framework helps to prevent, detect and remediate corrupt activity within the organization. (In the event that the opportunity is pursued, we will provide Denel with an overview of the envisaged program which makes provision for "adequate procedures". This includes an anti-bribery policy, controls, training, monitoring and incorporates due diligence procedures for all appointed business partners, agents and intermediaries of the joint venture);

18.2. To mitigate the risk of either the JV entity or its agents paying bribes to secure orders in Asia and India, we recommend that potential business partners, intermediaries, agents (including lobbyists) are subjected to robust due diligence screening to ensure that such agents do not have adverse histories or links to government in the jurisdictions pursued by the joint venture. In the event that politically exposed persons (PEPS) are identified within such entities, we can assist Denel with appropriate measures to mitigate the risk;

18.3. One of the control measures that is required is that appropriate provision be made for clear, detailed and robust anti-bribery clauses and/or the option of audit rights in any contracts with VR Laser RSA and/or VR Laser Asia. We have provided optimal clauses in this regard to Denel.

18.4. The potential joint venture may require government contract/permit negotiations. A clearly documented procedure on bidding for government contracts must be in place and monitored at each interaction the JV may have with government bidding;

18.5. Payments to any, business partner, agent or intermediary of the joint venture will have to be properly scrutinised, to ensure that there is no scope for suspicious payments, or for a bribe to be concealed within a payment to a consultant; Anti-corruption compliance will require monitoring to identify and address corruption risks for the duration of the association. Denel must clearly document that the agreed activities took place. This can be in the form of a newspaper article, a list of attendees, a presentation or anything which confirms that the event actually happened. Should a regulator review the transaction, it will be evident that Denel was vigilant and followed through until the conclusion of the agreement.

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We set out below a summary of our research regarding the corruption risk in India specifically:

18.6. The World Economic Forum identifies corruption as among the top three most problematic factors for doing business in India. The World Bank ranks India in the bottom third of countries in terms of ease of doing business. Certain regulatory requirements and procedures often make conducting business in India cumbersome and complex. Widespread red tape, a bottom-heavy bureaucracy, high tolerance for corruption and inefficient enforcement actions present operational risks. Companies must continuously strive to formulate ways to address and manage corruption risks in order to minimize negative impacts on their investments and operations in India.

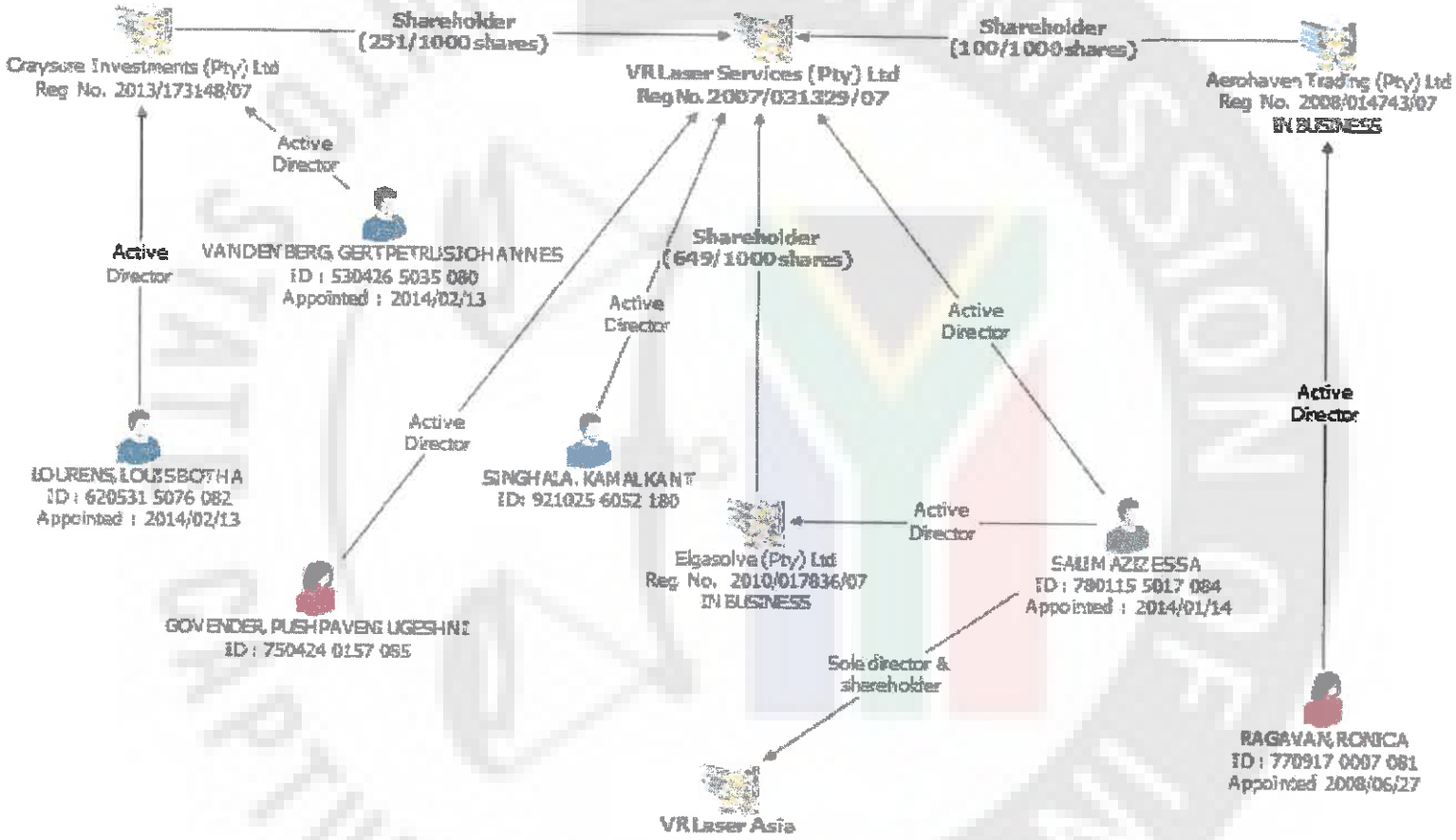
18.7. The main law governing corruption in India is the Prevention of Corruption Act (PCA). The focus under the PCA is primarily on the bribe taker; it makes the receipt of a bribe by a public official (and related offenses) punishable under law. In contrast, the U.S. Foreign Corrupt Practices Act (FCPA) focuses on the briber giver. An important difference in the two schemes is that facilitation payments are illegal in India under the PCA.

18.8. Several other Indian statutes also cover corruption-related activity, from the Indian Penal Code of 1860,8 to the recently passed Lokpal and Lokayuctas Act, 2013, which provides for anti-corruption watchdog organizations at the central and state levels. Six important bills awaiting parliamentary approval are also elements of the government's anti-corruption framework, including the Prevention of Corruption Act (Amendment) Bill, which expands the definition of taking a bribe and makes giving a bribe an offense, and which has authority over commercial organizations. Another bill awaiting parliamentary approval criminalizes the act of bribing officials of foreign governments and public international organizations.

18.9. India continues to be among the world's top investment destinations. Despite the risk of corruption, numerous global players successfully conduct large operations there. What is common among those who succeed in managing corruption risk is the focus on growth, maintenance of a strong internal control system, and implementation of a customized and effective anti-corruption compliance program.

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See below for a visual depiction of the directors and shareholder of VR Laser Services (Pty) Ltd and VR Laser Asia.



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SECTION B: ON SITE DUE DILIGENCE AND MANAGEMENT REVIEW

As conveyed in the introduction to this document, we were specifically requested by Denel to perform a site visit to the premises of VR Laser RSA, incorporating both interviews and an inspection of the VR Laser RSA operation. The critical questions that we were requested by Denel to address during the site visit, interviews and limited document review included the following:

- the ultimate beneficiaries/controllers of VR Laser Asia;
- existing business links/relationships in India;
- VR Laser's ability to lawfully solicit business in the Asia Pacific region;
- financial wherewithal to fund the proposed business operations.

19. WORK PERFORMED

19.1. Background and supporting information that was provided to ENS for our consideration and review, included but was not limited to the following:

19.1.1. Copy of the Cooperation Agreement entered into between Denel and VR Laser Asia, dated 27 October 2015.

19.1.2. Copies of the issued share certificates of the current shareholdings in VR Laser RSA.

19.1.3. Copy of the Certificate of Incorporation of VR Laser Asia, issued on 20 June 2014.

19.1.4. The Articles of Association of VR Laser Asia.

19.1.5. Copy of the "*Declaration of Trust*", dated 23 June 2014 reflecting the beneficial owner of the shares in VR Laser Asia as Mr Salim Aziz Essa.

19.1.6. Copy of form COR39 – "*Certificate of Confirmation*", detailing the status of VR Laser RSA as issued by the CIPC (dated 28 April 2015).

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19.1.7. Various email communications between van der Merwe and/or Tomsett and ENS regarding clarification of, or providing supporting documentation for queries raised during the course of the assignment.

19.1.8. BBBEE scorecard – certificate number: BM12848-230415 for VR Laser RSA issued by BEE~Matrix (Pty) Ltd with expiry date 22 April 2016.

19.1.9. ISO 9001:2008 compliance certificate for VR Laser RSA issued by TUV Rheinland Cert GmbH effective until 31 May 2016.

19.1.10. Signed audited annual financial statements ("AFS") for VR Laser RSA for the following periods:

19.1.10.1. Year ended 30 June 2012, issued by Deloitte on 14 November 2012

19.1.10.2. Year ended 30 June 2013, issued by Deloitte & Touche on 17 September 2013

19.1.10.3. Year ended 30 June 2014, issued by KPMG Inc. on 24 March 2015.

19.1.11. Management accounts for the period from 01 July 2015 to 31 October 2015 including a 'Balance Sheet' as at each respective month-end and a 'Manufacturing and Income Statement' for each respective month with year-to-date figures covering the 4 month financial period to the end of the last complete month of trading .

19.1.12. Debtors listing of VR Laser RSA as at 31 October 2015.

19.1.13. Creditors listing of VR Laser RSA as at 31 October 2015.

19.1.14. An electronic copy of a spreadsheet titled "*Inputs to the Denel Asia Company Business Case – 9 October 2015*", detailing anticipated turnover (revenue), percentage probability and expected order dates of pipeline business for Denel Asia.

19.2. ENS held meetings with Denel management on 24 November 2015, including the following attendees: Ntshepe, Burger, Legoabe, Denise Govender (Denel Land Systems – Executive Legal), Odwa Mhlwana (Denel Vehicle Systems – Chief Financial Officer), Gawie van Zyl (Denel – Financial Manager), and Matodzi Ramashia (secondee – Denel legal department).

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19.3. ENS visited the physical premises of VR Laser RSA on 24 November 2015 and conducted interviews with van der Merwe, Tomsett and McNeil. We also performed a site visit and walk through of the secure fabrication area and storage areas.

19.4. ENS perused the financial information, supporting documentation and copy of contracts as set out in 19.1 above in order to formulate high level questions that were posed to management (as set out in 19.2 and 19.3 above).

FINDINGS AND RECOMMENDATIONS RESULTING FROM WORK PERFORMED

20. ULTIMATE BENEFICIARIES/CONTROLLERS OF VR LASER ASIA

20.1. Findings

Essa is the sole shareholder of VR Laser Asia, as determined per a review of the following documents:

20.1.1. Copy of the Certificate of Incorporation of VR Laser Asia issued on 20 June 2014,

20.1.2. The Articles of Association of VR Laser Asia, and

20.1.3. Copy of the Declaration of Trust dated 23 June 2014, reflecting the beneficial ownership of the shares in VR Laser Asia.

Based on discussions and communication with van der Merwe, it has been established that VR Laser Asia is a recently incorporated privately owned entity based in Hong Kong that is yet to commence trading – "*VR Laser Asia is at this stage an empty shell*". The reason provided that this entity has yet to trade is that VR Laser RSA conveyed that: "*... do not want to compete with our customers (OEM's), therefore selling products to end-users*".

Based on discussions with van der Merwe, he indicated that VR Laser RSA will be responsible for providing the capital injection into Denel Asia to fund the proposed business operations in Asia. See paragraph 23 for further information in this regard.

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20.2. Perceived Risk

We can confirm that Essa is the sole shareholder of the Hong Kong based entity. Based on the business intelligence gathered as part of the open-source anti-corruption due diligence investigation, we can confirm that Essa is a related party by virtue of his 100% shareholding in Elgasolve, which in turn owns 64.9% of the issued share capital of VR Laser RSA. Furthermore, Essa has previously been linked with Sharma through Issar Capital, the 100% shareholder of VRLS Properties – the landlord of VR Laser RSA and source of loaned funds to VR Laser RSA. Essa and Sharma are purportedly also co-directors in two further businesses, namely Daqo South Africa (Pty) Ltd, since November 2012 (headquartered in Issar Capital's Sandton office) and the National Agricultural Development Project ("NADP").

Essa and Sharma are also purportedly co-shareholders in NADP, since December 2012. Both Essa and Sharma allegedly acquired their shareholding from Gupta-owned companies on the same day as each other in November 2013.

20.3. Recommendation

We recommend that Denel establish who has effective control of VR Laser Asia to ensure that all reasonable steps are taken to confirm compliance with the relevant laws and regulations promulgated under the South African Anti-Corruption legislation and anti-bribery compliance program requirements. It is important that Denel ensure that due care and professional scepticism is maintained throughout the procurement processes in soliciting work, particularly with reference to the legal scrutiny and regulatory oversight that is evident in the sensitive industry within which Denel Asia will operate.

21. EXISTING BUSINESS LINKS/RELATIONSHIPS IN INDIA

21.1. Findings

Based on discussions held with van der Merwe and a review of the cooperation agreement, it was indicated that VR Laser Asia (through its association with VR Laser RSA) would be providing the necessary skills and know-how in steel processing, particularly providing unique solutions for the defence industry and vehicle protection. This includes, inter alia, laser cutting, armour works, fabrication, machining related to such fabrication and integration, supported by the latest technology. Furthermore, VR Laser Asia purportedly understands the international fabrication market and industrial landscape.

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It is van der Merwe's opinion that Denel has the business links and technical expertise in respect of offering turn-key solutions for defence equipment to its clients based on high-end technology. He is of the opinion that Denel has numerous existing equity partnerships, joint ventures and cooperation agreements with international players in the defence industry and that it is this synergistic relationship that will enable Denel Asia to "*grow from strength to strength in the Asian market*".

When probed regarding the "*Asia Company Business Case – 9 October 2015*" schedule of expected orders, product turnover and probability of realising future revenues, van der Merwe indicated that Burger would be best positioned to answer these questions and that the spreadsheet had been drawn up by Denel management when meeting to discuss the proposed cooperation agreement and business expansion.

Based on our discussions with van der Merwe, McNeil and Tomsett, we further note that VR Laser RSA had previously attempted to expand into the American market and set up operations in Philadelphia through an entity styled VR Laser Services USA, Inc. a wholly owned subsidiary of VRLS Investments. This investment did not prove successful for VRLS Investments as laws and regulations in the USA precluded any foreigner from having access to highly confidential military design plans. As a consequence, we were informed that the USA business was discontinued. A search on open-source information reflected on the Bloomberg Business website reflects that VR Laser Services USA, Inc. was in fact sold to Metals USA Holdings Corp. in 2009. Furthermore, we have been informed that VR Laser RSA has no further foreign operations or entities currently trading and only has a presence in South Africa.

21.2. Perceived risk

Without carrying out a more detailed review and forensic investigation we cannot comment on the ability of VR Laser Asia to be able to establish business links/relationships in Asia. Denel runs the risk that the statement in the cooperation agreement that "*VR Laser Asia Ltd has an established network of potential business sources, which continues to expand*" may be unfounded, given that VR Laser Asia is a shell company and its related entity, VR Laser RSA has little exposure to marketing its business directly in foreign jurisdictions.

21.3. Recommendation

It is our recommendation that Denel consider this matter jointly with management of VR Laser RSA through the Management and Advisory Committees established in accordance with the cooperation agreement. It is important once again to evaluate the risk of non-compliance with relevant laws and regulations within the highly regulated industries of the foreign based business operations.

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22. VR LASER ASIA'S ABILITY TO LAWFULLY SOLICIT BUSINESS IN THE ASIA PACIFIC REGION

22.1. Findings

As detailed above, it is not possible for us to comment on whether the shell entity (VR Laser Asia), which is currently dormant, is able to lawfully solicit business in the Asia Pacific region.

23. FINANCIAL WHEREWITHAL TO FUND THE PROPOSED BUSINESS OPERATIONS

23.1. Findings

As set out in the cooperation agreement, VR Asia shall lend to Denel Asia, the equivalent of up to R100 million, over five years (R20,000,000 per year) as a shareholders loan, to set up an office for sales and marketing. It is not clear at this stage as to whether Denel will be required to fund the operations to any extent, however, it is apparent that all sources of finance will be from VR Laser Asia. As detailed in the findings set out above, VR Laser Asia is a shell company with no current trading operations. Consequently, it has been indicated that the funding will be provided by the related entity VR Laser RSA.

Based on a high level review of the most recent signed AFS of VR Laser RSA, along with a perusal of the recent management accounts and other financial information as set out in paragraph 19.1, the company is currently in a technically (factually) insolvent financial position. On the assumption that the financial information reported in the Excel spreadsheets supplied by Tomsett[4] is accurately recorded, the company's current liabilities exceed its current assets by approximately R22 million as at October 2015.

Further to this, it has been noted in the last three sets of signed AFS that VR Laser RSA was issued with qualified audit opinions. The qualifications related to non-compliance with International Financial Reporting Standards for Small and Medium Sized Entities on the basis that a significant and material goodwill balance had not been appropriately impaired and amortised in accordance with the accounting laws and regulations.

4 It was at Denel management's request that these figures have not been traced to the supporting general and subsidiary ledgers or account reconciliations of VR Laser RSA.

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Had these amortisations been processed in the accounting records, the liquidity position would be factually insolvent and there would be a significant increase in the assessed loss reported from operations.

Furthermore, the qualifications detailed that the going concern assumption was inappropriate and that the shareholders loan had to be subordinated in favour of third party liabilities in order to restore solvency in the statement of financial position.

There are a number of other (less significant) financial review findings included under general findings at paragraph 24.

Based on discussions held with Tomsett, the latest financial statement audit for the year ended 30 June 2015 has been completed, however, we have not been provided with the draft AFS or supporting financial information for this year end. According to Tomsett, tax entries and other minor administrative matters are all that remain outstanding in order to finalise the financial statements, however, we are not able to verify this independently with KPMG Inc. or establish the reported statements of comprehensive income and the related cash flows of the company. Consequently, without performing more detailed forensic (and financial due diligence) investigations, we are unable to comment on the financial results for the year ended 30 June 2015.

A cause for concern relates to the fact that VR Laser RSA do not at this stage source finance from third party banking institutions, besides a loan of R30 million currently repayable to the Bank of Baroda. VR Laser RSA therefore ordinarily fund the business operations and capital commitments through loan finance raised from shareholders, when further funds are made available to the company. One such financing arrangement has recently taken place where Westdawn advanced funds of R27,650,000 (R26 million of which was advanced by Westdawn during September and October 2015) in order to support the business operations. It therefore becomes relevant to establish the business and related party relationship with Westdawn and other respective shareholders in VR Laser RSA as these shareholders will inevitably need to fund the VR Laser Asia entity when the need arises.

As set out above in this document, Elgasolve owns 64.9% of issued share capital of VR Laser RSA. As confirmed via a review of copies of the share certificates in question, Craysure and Aerohaven own 25.1% and 10% of the issued share capital of VR Laser RSA respectively.

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The sole shareholder of Elgasolve is Essa. The sole shareholder of Craysure is Westdawn[5] The sole shareholder of Aerohaven is Ragavan[4] (who is also an active director of Westdawn).

The active directors of Westdawn are Zuma, Gupta and Ragavan. It is therefore evident that individuals considered to be politically exposed persons appear to be the current benefactors of trading operations of VR Laser RSA. These individuals are therefore indirectly the future benefactors of VR Laser Asia in the event that the shareholders of VR Laser RSA are required to fund the operational and capital requirements of VR Laser Asia.

23.2. Perceived risk

It appears to be highly probable that the future source of financing of Denel Asia will be sourced from shareholder loans held in VR Laser RSA and that these loans will be due and payable to politically exposed persons. There is a further risk that the CIPC information has changed in the interim period as detailed in the footnote below.

23.3. Recommendation

We recommend that Denel ensure that all reasonable steps are taken to confirm compliance with the relevant laws and regulations promulgated under the South African Anti-Corruption legislation and anti-bribery compliance program requirements. It is important that Denel ensure that due care and professional scepticism is maintained throughout the procurement processes in soliciting work, particularly with reference to the legal scrutiny and regulatory oversight that is evident in the sensitive industry within which Denel Asia will operate. Denel should further establish and fully understand any international laws and regulations (Anti-Corruption compliance requirements of the FCPA, etc.) that may be imposed on Denel Asia when carrying out operations in the foreign countries targeted in the proposed Asia Pacific expansion. As conveyed above Denel will have to ensure that robust due diligence screening is performed on all potential business partners, agents and intermediaries to the joint venture as part of a robust set of adequate procedures incorporated in an anti-bribery compliance program to mitigate the greater than normal corruption risks that the entity may be exposed to.

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[5] We have not been able to obtain direct confirmation of these shareholdings from van der Merwe and as such can only report on the information made available from related discussions held with Tomsett. It is further noted that the CIPC certificates are dated in April 2015. Consequently, there could be further amendments to the shareholding in the interim period of which we are not aware. Tomsett confirmed telephonically (on 25 November 2015) that there had been no changes to the shareholding as set out in this document.

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Denel should further obtain the most up-to-date confirmation of all shareholdings to establish the beneficial shareholders of the respective entities.

24. GENERAL FINDINGS

24.1. Finding

We discussed the adverse media related to the payment of a consultant in the US that was identified during the desktop review with VR Laser RSA management.

As conveyed in this document, a 26 March 2014 publication on the website of the Bureau of Alcohol, Tobacco, Firearms and Explosives under the U.S. Department of Justice, conveyed that during 2011 and 2012, Dennis Haag ("Haag"), a retired U.S. Army major, received unlawful pay worth about USD 40,000 from VR Laser RSA in return for representing VR Laser RSA to obtain military contracts when Haag worked for the U.S. Military. However, there has been no evidence that any public contract, as a result of this arrangement, was actually obtained by VR Laser RSA. The filing further states that Dennis Haag admittedly illegally exported firearms to an employee of VR Laser RSA from 2008 to 2012 when Haag was a federally licensed firearms dealer. Dennis Haag pleaded guilty to receiving unlawful pay and to illegally shipping firearms to South Africa, facing a maximum of 25 years in prison and a fine of up to USD 1.25 million. Judi Haag, wife of Dennis Haag, also pleaded guilty to assisting her husband in receiving unlawful pay. She might receive a year in prison and a fine of USD 100,000. Both individuals were also proposed for debarment from participating in future federal contract work. Note that this article does not provide any further information on this case and research was unable to identify any further references to this case.

This matter was discussed with Tomsett and McNeil, who were both employees of VR Laser RSA at the time of these alleged incidents. The severity of these allegations were played down by both Tomsett and McNeil and it was explained that Haag was merely a consultant to VR Laser RSA promoting business of the VR Laser Services USA, Inc. based entity. Tomsett does not believe that there was any wrongdoing but did state that the consulting fee had to be channelled through Haag's wife's bank account. A further question was raised with van der Merwe and Tomsett as to whether VR Laser RSA has an anti-corruption policy or not and whether VR Laser RSA carries out due diligence on business partners, agents or intermediaries before appointing them. VR Laser RSA have confirmed that they have no anti-corruption policy in place, however they have indicated that they are willing to accept and agree to any terms required by Denel to ensure that the JV is anti-corruption compliant and conveyed that VR Laser RSA is also willing to agree to such requirements in South Africa.

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24.2. Perceived risk

It appears that there are no formal policies or procedures that have been put in place for VR Laser RSA to ensure that third party agents and intermediaries have complied with anti-corruption and anti-bribery warranties and covenants or audit rights.

24.3. Recommendation

We recommend that Denel management ensure that all reasonable steps are taken to ensure that Denel Asia have adequate policies and procedures in place to ensure compliance with the respective target territories' and South African anti-corruption and anti-bribery legislation.

25. POSSIBLE UNSUBSTANTIATED MANAGEMENT FEES ACCRUAL

25.1. Finding

When carrying out the high level review of the financial information, with specific reference to the most recent manufacturing and income statement for the year-to-date 4 month period ended 31 October 2015, it was established that a monthly accrual is currently being made for an amount of R370,000 purportedly in respect of management fees. As per discussion with Tomsett, this accrual relates to a historical expense for consulting fees paid for services rendered in accordance with a management contract to assist VR Laser RSA to navigate the migration of the business to its new shareholders at the time that ownership changed in late 2013. Tomsett commented that this accrual was raised in accordance with a contractual arrangement to do so however *"...this accrual is currently being debated at management level and may no longer be relevant."*

25.2. Perceived risk

It appears that there may be unsubstantiated accruals for services not actually rendered on behalf of VR Laser RSA and there is a possibility that non bona-fide expenses may be paid to third parties or possible related parties that cannot be adequately justified. The true nature and substance of these payments may be unjustly concealed as a management fee.

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25.3. Recommendation

We recommend that Denel management ensure that all reasonable steps are taken to ensure that the legality of these possibly unsubstantiated expenses is investigated further and that all payments made to third parties or related parties are made in accordance with the prevailing accounting and other laws and regulations of South Africa.

26. DIRECTORS INTERESTS IN THE BUSINESS

26.1. Finding

As per the desk-top due diligence work, it was noted that there is very little information available in the public domain with regards to the public profile of the statutorily appointed directors of VR Laser RSA insofar as these directors are involved in the day-to-day operations of VR Laser RSA. The company website of VR Laser RSA makes no mention of the formally appointed directors and the company profile of key personnel details all the operational members of staff without referring to the active directors. Our main point of contact with VR Laser RSA was the Chief Executive Officer, van der Merwe, who although not a statutorily appointed director, is the person responsible for signing the cooperation agreement on behalf of VR Laser Asia. As per discussions with Tomsett, she mentioned that Singhala is regularly on the premises of VR Laser RSA and acts in the role of operational and marketing director although his formal title is purely "Director". Per Tomsett, Singhala was not available on the day of our site visit as *"…he (was) dealing with another acquisition unrelated to VR Laser RSA but would have loved to be (t)here.."*. According to Tomsett, Essa is only occasionally on the premises for visits and Ragavan is actively involved in reviewing the cash flow requirements and management accounts on a regular basis. We record that we have not been afforded direct interaction with the statutorily appointed directors.

26.2. Perceived risk

It is peculiar that the statutorily appointed directors are not visibly involved in the day-to-day running of the business operations of VR Laser RSA. Although we have not specifically requested to see the register of directors' interests in contracts, there is a potential risk that the directors may not have disclosed their interests in contracts or ensured compliance with Company's Act and other legal requirements imposed in South Africa (e.g. compliance with King III Code of Corporate Governance).

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26.3. Recommendation

We recommend that Denel management ensure that all reasonable steps are taken to ensure that the VR Laser RSA director's interests in contracts have been adequately assessed and appropriately disclosed in the permanent statutory registers of VR Laser RSA, including but not limited to being recorded in the minutes of Board meetings of VR Laser RSA.

27. REQUISITE SKILLS AND EXPERTISE OF DIRECTOR

27.1. Finding

As per the CIPC documentation reviewed and the anti-bribery due diligence work performed, it was established that Singhala was appointed as a statutory director of VR Laser RSA in December 2014 when he had just turned 22 years old. Per discussions with Tomsett, Singhala is still a student at university, however he is purported to fulfil the role of marketing and operational director. Per discussions with Tomsett, Singhala may also be a PEP.

27.2. Perceived risk

It is important that all duly appointed directors of an entity have the requisite knowledge and skills and industry expertise to fulfil their statutory rights and obligations for the benefit of the entity. In the absence of performing a more detailed financial due diligence, we would like to highlight the perceived risk that the operational director, Singhala, is extremely young, possibly inexperienced in the highly technical nature of the manufacturing and fabrication processes within the steel supply industry and due to study commitments may not be applying his time in the best interests of the VR Laser RSA business operations.

27.3. Recommendation

We recommend that Denel carry out further investigation into the applicability and good business standing of Singhala's appointment to the Board of VR Laser RSA to ensure that any involvement in the proposed business expansion into the Asian territories is appropriately managed and controlled and that all necessary disclosures have been made in accordance with the anti-corruption and anti-bribery legislation in South Africa and abroad. Our recommendations regarding ensuring that corruption risks related to PEPS are properly managed by the implementation of the recommended anti-bribery controls.

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COMMISSION OF INQUIRY
INTO STATE CAPTURE

COOPERATION AGREEMENT

THIS AGREEMENT IS ENTERED INTO BY AND BETWEEN:

VR LASER ASIA LTD
(Certificate of Incorporation 2111273)
a limited company incorporated and existing in Hong Kong under the Companies Ordinance
(Chapter 622 of the Laws of Hong Kong)
having its business address at
BLK A, 15/F HILLIER COMM BUILDING, 65-67 BONHAM STRAND EAST, SHEUNG WAN, HONG KONG
("VR ASIA")

AND

DENEL SOC LTD
(Registration number: 1992/001337/30)
a company incorporated and existing under the laws of the Republic of South Africa
having its registered address at
Nellmapius Drive, Irene, Centurion, 0046
("DENEL")

COMMISSION OF INQUIRY INTO STATE CAPTURE

WHEREAS **VR LASER ASIA LTD** is a Company registered in Hong Kong and possesses skills and know-how in steel processing, particularly providing unique solutions for the defence industry and vehicle protection which includes, inter alia, laser cutting, armour works, fabrication, machining related to such fabrication and integration which services are supported by the latest technology and further understand the international fabrication market and industrial landscape; and

WHEREAS **VR LASER ASIA LTD** has an established network of potential business sources, which continues to expand.

WHEREAS DENEL SOC LTD **("DENEL")** is a commercially driven state owned Company, renowned for innovative defence, security and related technology solutions. Denel offers turn-key solutions for defence equipment to its clients by designing, developing, integrating and supporting, inter alia, artillery, munitions, missiles, aerostructures, aircraft maintenance, unmanned aerial vehicle systems and optical payloads based on high-end technology; and

WHEREAS Denel has a number of equity partnerships, joint ventures and cooperation agreements with international players in the defence industry; and

WHEREAS both Parties have identified Asia, more particularly India as a key strategic region for cooperation between the Companies and are interested in co-operating with each other to, inter alia, support the requirements of key local and/or international clients and prospective clients in these countries;

NOW THEREFORE, the Parties agree and commit to work together on the terms and conditions contained in this agreement:

1. **COMPANY TO BE FORMED AND INCORPORATED**

1.1 The Parties agree to establish a joint venture company (hereinafter the "Company"), to be registered in Hong Kong.

1.2 The Company's core business will be to trade in various defence products, amongst others the marketing, selling, manufacturing and delivery of any products currently manufactured or sold by DENEL, as well as to bid or otherwise become involved in special projects for the provision of defence products and expertise as and when such opportunities arise within identified territories.

1.3 In addition to this Agreement, certain agreements (including a shareholders agreement) will be entered into among the Parties and the Company, either concurrently with the execution of this Agreements or upon establishment of the Company, alternatively as soon as possible after the incorporation/registration of the Company, in order to give effect to the purpose of this agreement.

1.4 The Parties shall act as quickly as possible to establish a company under the laws of Hong Kong. The name of the Company shall be Denel Asia. The Parties shall immediately attend to all practical requirements in order to register the Company. The Parties agree that KPMG will be appointed to register the Company and to attend to all ancillary agreements and requirements.

1.5 The Company shall adopt Articles of Incorporation pursuant to the laws of Hong Kong. The Articles of Association and Shareholders agreement shall be consistent with the terms of this Agreement and in case of any conflict, the terms of the Articles of Association and Shareholders agreement shall prevail.

2. SHAREHOLDING AND CONTROL

2.1 DENEL shall hold 51% of the share capital of the Company and VR ASIA shall hold 49%.

2.2 VR ASIA shall lend to the Company the equivalent of up to R100 000 000-00, over 5 years (R20 000 000 per year), as a shareholders loan, to set up an office for sales and marketing. This amount shall bear interest at the Repo Rate of the South African Reserve Bank, per annum, and this shareholder's loan plus such interests accruing thereon, shall be repaid from of the first profits of the Company. If there are insufficient profits to pay the full shareholder's loan plus interest no dividends shall be declared until such time as this shareholder's loan plus interest has been fully repaid.

2.3 Until such time as the Company has been formed, the proposed directors in 3.2.1 below shall act as a Management Committee in order to execute the terms and conditions of this agreement, as set out in clause 3.3 below. Each party shall be entitled to alternate their representatives, acting on the Management Committee, with written notice to the other party.

2.4 The Company shall provide for its own loan financing according to the decision of its Board of Directors. The Parties shall support the Company in obtaining the most favorable terms for its loan financing. None of the Parties shall be obliged to make any guarantees of financing unless this is separately agreed by the Parties. If project finance or other funding is required, the Shareholders shall provide financial assistance in proportion to their respective shareholding.

2.5 Neither Party shall, without the prior written consent of the other Party pledge, hypothecate or otherwise use its shares as security, or grant options over its legal and beneficial interest in its shares. Any action of a Party violating this provision shall be void and shall be considered a material breach of this Agreement.

2.6 No Party shall sell, transfer or otherwise dispose of its shares, unless all loans by any Party, to the Company, have been repaid and the party to whom the shares are being transferred to agrees in writing to be party to this Agreement or the shareholders agreement referred to in 1.3. In the case that either Party desires to sell to a *bona fide* third party all or any of its shares of the Company (such Party

hereinafter the "Selling Party"), the other Party shall have a right of first refusal to purchase such shares. The Selling Party shall first give a written notice to the other Party (hereinafter the "Receiving Party") and the Company, setting forth;

i) the number of shares proposed to be transferred (hereinafter the "Offered Shares");

ii) the proposed purchase price, terms and payment and other material terms and conditions received from a bona fide third party; and

iii) an irrevocable offer to sell Offered Shares to the Receiving Party (hereinafter the "Sale Offer") at the same price and on the same terms and conditions as set forth therein.

2.7 The Receiving Party shall have the right to purchase the Offered Shares pursuant to the Sale Offer, in whole or in part, by delivering a written notice to the Selling Party within 30 days from the date of the Sale Offer, irrevocably stating therein that all of the Offered Shares will be purchased by the Receiving Party.

2.8 If the Receiving Party provides to the Selling Party the notice specified in the immediately preceding paragraph, then the Receiving Party shall have 30 days to complete the purchase of the Offered Shares upon the terms set forth in the Sale Offer (hereinafter the "Purchase Period"), provided, however, that the Purchase Period shall be extended until such date as all required approvals, consents or authorizations in connection with such purchase are obtained.

2.9 If the Receiving Party shall not have completed such purchase within the Purchase Period, as extended as provided herein, then the Selling Party shall have the right for 90 days thereafter (hereinafter the "Transfer Period") to transfer the Offered Shares not subject to any of the restrictions set forth in this Agreement; provided, however, that such transfer is consummated on terms not more favorable to the purchasers thereof than the terms specified on the Sale Offer; and provided, further, that the Transfer Period shall be extended until such date as all required approvals, consents or authorizations in connection with such purchase are obtained.

2.10 If at the end of the Transfer Period, as extended as provided herein, the Selling Party has not completed the sale of the Offered Shares, the Selling Party shall no longer be permitted to sell such Offered Shares pursuant to this Section.

2.11 Notwithstanding anything to the contrary of other provisions set forth in this agreement, neither Party shall sell any of its shares of the Company to any Competitors of the Company, or to any other entity which has not signed and agreed to be bound by the provisions of the Company's Articles of Association and Shareholders Agreement. For purposes of this Agreement, a Competitor shall mean a company which conducts similar businesses of any of the parties or the Company at any time.

3. Management Structure and Operation

3.1 Shareholders Meeting

3.1.1 Matters to be decided by the Shareholders Meeting shall be as follows:

(a) Revision of the Articles of Association;

(b) Approval of the balance sheet and other financial statements received from the Board of Directors;

(c) Determination of dividends and of disposition of losses;

(d) Merger, consolidation, restructuring or reorganization of the Company;

(e) Sale of all or substantially all assets of the Company;

(f) Appointment and removal of the Company's auditors;

(g) Voluntary submission by the Company to bankruptcy, or any similar status;

(h) Establishment of subsidiaries, opening and closing of branch offices, acquisition of the whole or part of the assets of another company or business, establishment of new business sites and closing of existing ones;

(i) Liquidation or dissolution of the Company; and

(j) Other matters reserved to the determination of the Shareholders Meeting by the Company Law of Hong Kong.

3.1.2 Matters such as the method of announcing the Shareholders Meeting, the legally required number of attendants, and the required number of votes for decisions shall be in accordance with the Articles of Association of the Company and the Company Law of Hong Kong subject to the following:

a) Each shareholder of the Company shall be given timely, written notice of the time, date, agenda and place of the Shareholders Meeting, in no event later than 15 days prior to the date of such meeting. All notices and agendas of Shareholders Meetings shall be accompanied by accurate and complete English language translations thereof.

b) A quorum for a Shareholders Meeting shall require the presence, in person or by proxy, of shareholders of the Company holding more than 60% of the total outstanding shares of the Company.

c) Resolutions of the Shareholders Meetings, on any of the matters described in 3.1.1 (a) to (i) shall be adopted by the affirmative vote of 75% of the shares represented in person or by proxy at a Shareholders Meeting, at which a quorum is present. Any other matters will be adopted by a normal majority vote.

d) Each share shall be entitled to one vote.

e) In case where a shareholder cannot attend a Shareholders Meeting, such shareholder may appoint a representative by issuing a proxy in writing in accordance with the laws of Hong Kong.

3.2 Directors and Chairman

3.2.1 The Company shall have a minimum of 4 directors. The first directors shall be Zwelakhe Ntshepe (DENEL), Stephan Burger (DENEL), Pieter van der Merwe (VR ASIA) and Kamal Singhala (VR ASIA). Each Party shall be entitled to nominate 2 directors and shall be entitled to replace their nominated directors. The Chairman shall have the casting vote.

3.2.2 If the Company needs to comply with legal requirements for the appointment of independent directors or a company secretary, as will be provided in the Company Law any other laws or regulations, the Parties agree to co-operate in good faith and to work out an appropriate contractual arrangement to maintain the Company as joint venture between the Parties as equal partners with regard to the directors, supervisors and the management of the Company.

3.2.3 The responsibilities of the Board of Directors shall be as follows:

a) Appointment and removal of the Chairman of the Board. The first Chairman of the Board shall be a DENEL appointed representative.
b) Approval of the annual and quarterly budgets (including but not limited to the production plan, the business plan, the profit and loss plan, the capital investment plan, and the financial plan);
c) Change of issued and outstanding share capital of the Company;
d) Determination of long term policies of the Company including substantial change in the organizational structure and business operation of the Company;
e) Determination of employment terms including compensation packages;
f) Setting the limits of authorities of various positions and approving the chart of authorities;
g) Preparation and submission to the Shareholders Meeting of the financial accounts (including dividends and disposition of losses);
h) Creation of pledge, hypothecation, encumbrance or other security on the Company's assets;
i) Transfer, sale or any other disposal of major assets other than in the ordinary course of business in the amount of more than the equivalent (at time of the decision) of R5 000 000-00;
j) Conclusion or termination of agreements regarding intellectual property rights and know how;
k) Conclusion of any agreement or other arrangement with, or for the benefit of any director of the Company;
l) Initiation of new product lines or discontinuation of existing product lines;
m) The commencement of any litigation as plaintiff or the settlement by the Company of any litigation against it;

n) Submission of other matters to the Shareholders Meeting for consideration or approval as may be required by law;

o) Decision of other important matters related to the Company and transactions other than in the ordinary course of business of the Company;

p) Any decision in regards to the allocation and/or payment of the loan amount mentioned in clause 2.2.

3.2.4 All the directors, in person or through representation, shall be necessary to form a quorum. Resolutions/decisions of the Board of Directors, as mentioned in 3.2.3 (a) to (p), shall be in writing, and shall be adopted by a 75% vote of all Directors. All other resolutions shall be adopted by a normal 51% majority.

3.2.5 In case where any director of the Company cannot attend a meeting of the Board of Directors, that director may appoint another director as representative in accordance with the Company law of Hong Kong. All or any of the directors may participate in a meeting of the Board of Directors by means of a video conference which allows all persons participating in the meeting to see and hear each other. A director so participating shall be deemed to be present in person at the meeting and shall be entitled to vote or be counted in a quorum accordingly.

3.2.6 Meetings of the Board of Directors shall be called by the Chairman. Each director of the Company shall be given timely, written notice of the time, date, agenda and place of the Directors meeting, in no event later than 15 days prior to the date of such meeting. In emergency cases the meeting of the Board of Directors can be called by the Chairman by giving a minimum of two working days notice.

3.2.7 Advisory Committee

3.2.7.1 After the Company has been established, an Advisory Committee will be constituted. The Advisory Committee shall provide the Board with advice and shall consist of experts nominated by the Board.

3.3 Management Committee

3.3.1 The parties shall within one month of the Effective Date of this cooperation agreement establish a management committee which shall be responsible for, and shall make decisions or determinations with regard to all matters arising out of this cooperation agreement, including matters which have been referred to it by any of the parties, until such time that the Board of the Company is formed. Notwithstanding any other provision in this agreement, and until the Shareholders agreement has been signed, the Management Committee shall be entitled to take any decision in regards to Denel Asia's anticipated office, including but not limited to its location.

3.3.2 The parties shall be entitled to appoint and replace from time to time by written notice to the other party, representatives on the management committee as follows:

3.3.2.1 DENEL shall appoint and replace 2 (two) representatives on the management committee;

3.3.2.2. VR ASIA shall appoint and replace 2 (two) representatives on the management committee.

3.3.3 Other persons shall be entitled to attend meetings of the management committee or be co-opted by the management committee, by invitation, which invitation shall require the mutual consent of the management committee. A member of the management committee may not unreasonably withhold his consent to the aforesaid invitation. Such co-opted or invited members shall not have any voting rights. Resolutions shall be adopted by a 75% vote of all members present.

3.3.4 The management committee shall meet as frequently as may reasonably be necessary to perform its functions in terms of this cooperation agreement.

3.3.5 A quorum of the management committee shall be a one representative of each party to this cooperation agreement. In the case of neither representatives of a party being able to attend a scheduled meeting and an alternative date cannot be set, the decisions taken at the meeting need to be ratified in writing by the other parties representative to make the said decisions binding. Decisions of the management committee shall be reached by consensus and will be binding on the parties.

3.3.6 In order for a decision of the management committee to have the effect of an amendment of this agreement, the decision must be reduced to writing and signed by a representative of each party who would ordinarily be entitled to sign an amendment to this agreement.

3.3.7 The Parties shall manage their relationship through the Management Committee, which shall be the highest decision making body for purposes of this Agreement.

3.3.8 The Parties shall ensure that their representatives on the Management Committee shall be duly authorised to bind the Parties in respect of all matters arising before the Management Committee.

3.3.9 The Management Committee shall monitor all costs anticipated to be incurred in respect of the obligations performed under this Agreement and shall procure that a quarterly reconciliation is done. The Parties shall reimburse each other to the extent as evidenced by such reconciliation, provided that the Parties may employ set-off where applicable and only make payments of net amounts. The Parties may determine how frequently such payments shall be made, provided that they occur (if applicable) at least twice a year.

4. OPERATIONS

4.1 Due to the nature of each Party's business, VR ASIA shall attend, advise and execute all functions in regards to fabrication, manufacturing and operational aspects at an agreed rate. DENEL shall make available to the Company, all products manufactured by DENEL in South Africa, for manufacturing and sale, and shall transfer all information in regards to these products to the Company on terms to be agreed between Denel and the company. DENEL and VR ASIA shall be jointly responsible for the sales and marketing of the Company and its products. DENEL

VKS

shall enter into a relevant licensing agreement with the Company. For the avoidance of doubt, DENEL shall not alienate its intellectual property in any way whatsoever.

4.2 Notwithstanding anything contained in 4.1 above, it is specifically recorded that VR ASIA shall be obliged to utilize all its resources, including its established network of potential business sources as referred to in the preamble of this agreement, in performing marketing activities on behalf of the Company and in generally ensuring that potential business opportunities are fully exploited within the Company.

4.3 The Company shall be liable for any Offset Obligations and or similar obligations that may arise in the territories in which it has secured opportunities.

4.4 Each of the Parties shall transfer to the Company sufficient start-up training and other transfer support. Each party shall transfer technology, information and training to the Company in order to operate.

4.5 The Parties agree that the Company shall establish it's own information systems organization that is responsible for procuring and/or providing all of the information systems and technology required for the operation of the Company (the "Company's IT Organization"). The Company's IT Organization shall establish and operate the Company's IT infrastructure, including information systems and all supporting services.

4.6 It is specifically agreed that where opportunities are identified which are in the interests of the Company, and in respect of which VR Asia or Denel may also benefit, thereby creating a conflict of interest, VR Asia and Denel shall defer its own interests to those of the Company, and shall ensure that all potential opportunities are first offered to the Company. Should the Board, for any reason, resolve not to pursue any such opportunity, then VR Asia or Denel may pursue such an opportunity and give due notice to the Board.

5. ACCOUNTING

5.1 The accounting year of the Company shall be determined by the Managing Committee.

5.2 Within 10 days after the end of each month and 20 days after the end of each quarter, the Company shall submit to each Party its unaudited balance sheet and profit and loss statement of such month or such quarter, as the case may be.

5.3 Each Party shall have the right to audit or have audited, and/or require copies of the accounts of the Company. The accounts of the Company shall be kept in accordance with the laws of Hong Kong.

5.4 Unless otherwise determined by the Board of Directors, the Parties agree to appoint KPMG as its certified public accountants.

6. DURATION

6.1 This Agreement (other than clause 7, 9, and 10 which shall be binding from the signature date) shall become effective upon final approval in terms of the Public Finance Management Act 1 of 1999 or other approvals required for the implementation of this agreement (hereafter the "Effective Date"), and continue in force unless terminated on the grounds set out herein.

6.2 Other than set forth in the Sections 6.3 and 6.4 of this Agreement, this Agreement shall terminate on –

6.2.1 to the extent that the company is incorporated, the date on which the parties conclude the agreements, including the shareholders agreement, contemplated in 1.3;

It being specifically agreed that the parties may terminate this agreement by mutual consent prior to incorporating the company.

6.3 In case of the occurrence of any of the following circumstances this Agreement may be terminated with immediate effect by either Party by serving written notice (the "Termination Notice") to the other Party:

a) Material breach of this Agreement by a Party (where only the non-breaching Party shall have the right to unilaterally terminate this Agreement as specified in 6.3 and the breaching Party was granted a 60 days cure period before the Termination Notice is served and did not remedy the material breach within this 60 day period);

b) In the case that the non-terminating Party has applied for liquidation or reorganization under applicable insolvency law, or has applied for or is the subject of a third party action for insolvency or business rescue, or is unable to honor its debts, or in the case of a *Force Majeure* which continues uninterrupted for a period in excess of 12 months.

6.4 In the event that all the shares of the Company are transferred to one of the parties, the terms and conditions of this agreement shall still be applicable except insofar as any term refers to the parties as co-shareholders. For the avoidance of any doubt, the terms in regards to the operational duties of each party, such as the duties set out in 4.1 and 4.2 above, shall remain to apply.

6.5 In case any of the circumstances stipulated in Section 6.3 occurs, the Party serving Termination Notice may elect either of the following options:

a) Within 45 days after the day the Termination Notice was served, to serve a sale notice (the "Sale Notice") on the other Party offering to sell all of its shares at 120% of the Market Value or Net Asset Value, whichever is higher (the "Put Option Price"). The Party who receives the Sale Notice must, by itself or through a third party nominee, accept the offer and must purchase all of the requesting Party's shares at the Put Option Price within 45 days after the above notice is served.

b) Within 45 days after the day the Notice was served, to serve a purchase notice (the "Purchase Notice") on the other Party offering to purchase all of its shares at 70% of either the Market Value or Net Asset Value, whichever is lower (the "Call Option Price"). The Party who receives the Purchase Notice must, by itself or through a third party nominee, accept the offer and must sell all of its shares to the requesting Party at the Call Option Price within 45 days after the above notice is served.

6.6 For the purpose of this Section 6.5, Market Value shall mean, the value per share appraised by an internationally recognized independent appraiser, appointed by the Managing director of KPMG Hong Kong.

6.7 For the purpose of this Section 6.5, Net Asset value shall mean the book value of the Company as determined by its latest available audited financial statements, as adjusted for capital increase or decrease of the Company or other major corporate activities which may affect the content of such financial statements, such adjustments to be made and certified by the Company's auditors within 30 days after the Sale Notice or Purchase Notice was served.

6.8 In case of occurrence of the termination event set forth in the Subsection 6.3(a), the non-breaching Party shall, in addition to the rights as set forth in the Section 6.5, be entitled to demand the breaching Party to compensate its damages incurred by such termination event.

7. GENERAL CONDITIONS

7.1 Notwithstanding any other provision, clause 7 shall become effective upon signature date and shall survive termination of this Agreement. No termination shall relieve any Party from liability for any breach of this Agreement.

7.2 Confidentiality and Non-use

7.2.1 During a period beginning at the Effective Date and ending ten (10) years after the later of the termination of this Agreement, it shall be prohibited for either Party to disclose to any third party information which has been disclosed by the other, whether such disclosure is direct or indirect, by any means such as a writing, factory tour, or other means used to communicate information, provided that such information shall be documented or described in a tangible form and shall be marked "Confidential" (hereinafter "Confidential Information"). Any such Confidential Information shall be used only for the purposes of carrying out this Agreement.

7.2.2 Any other use of Confidential Information is prohibited. Each of the Parties will cause its own and employees of the Company to adhere to the obligations of this through provisions in their respective employment agreements or otherwise. Confidential Information specifically includes the terms of this Agreement and its conditions provided however that the Parties may in connection with an actual or proposed merger or acquisition, and in connection with the enforcement of its rights under this Agreement disclose the terms and conditions of this agreements in confidence to its legal counsel, accountants and other advisors.

7.3 Confidential Information does not include information:

a) Which was obtained legally by the receiving Party prior to its receipt from the disclosing Party.
b) Which was or has become public not through any act of the receiving Party.
c) Which has been received from a third party with no obligation of confidentiality;
d) Which has been independently developed by the receiving Party or its Affiliates.
e) This obligation of confidentiality shall not apply in such case that information is requested by a government agency of competent jurisdiction but in any case that Confidential Information is disclosed under this paragraph the Party disclosing Confidential Information to such government agency shall give the other Party (the "Information Owning Party") notice prior to such disclosure which notice shall be reasonably sufficient to allow the Information Owning Party to seek appropriate action to prevent such disclosure.

7.4 Non Circumvention

7.4.1 A Party shall not, without the prior written consent of the other Party, directly or indirectly initiate, solicit, negotiate, contract or enter into any business transactions, agreements or undertakings, with any third party identified or introduced by the other Party or the Company, or seek to bypass, compete, avoid or circumvent the other Party or Company from any business opportunity, that relates to the Company's business, by utilising any information received as a result of this agreement, or by otherwise exploiting or deriving any benefit from such information.

8. FORCE MAJEURE

8.1 In the event that either Party is delayed in performing or is prevented from performing in whole or in part its obligations hereunder due to Force Majeure then the Party so affected shall have no liability to the other Party in respect of any resultant delay in performance or non-performance, partially or in whole, of its obligations under this Agreement (and the other Party shall to a similar extent not be liable for non performance or delay in performance of its obligations).

8.2 For the purpose of this Agreement, a Force Majeure shall exist only if and during a period when an event is beyond the control of the Party claiming Force Majeure. Such event of Force Majeure shall include but not be limited to:

a) labor disputes,
b) fire, explosion directly affecting the facilities concerned,
c) power outages or water shortages and any resultant losses incurred as a result, or
d) war or other hostilities, flood, earthquake, severe weather conditions of an extraordinary nature directly affecting the facilities concerned.

8.3 A Party wishing to invoke Force Majeure shall promptly notify the other Party in writing giving details thereof, and of the anticipated effect on this Agreement and of the estimated duration of Force Majeure. Such Party shall use its best endeavors to resume full performance of its obligations under this Agreement without avoidable delay.

8.4 Notwithstanding any provision in clause 8, Force Majeure cannot be invoked insofar as it relates to the Parties' rights and obligations as shareholders.

9. APPLICABLE LAW AND DISPUTES

9.1 This Agreement shall be construed in accordance with and governed by the laws of South Africa and shall be interpreted thereunder.

9.2 In case of any dispute between the Parties to this Agreement or in case of any alleged breach of this Agreement, the Parties shall cooperate to reach an amicable resolution of such dispute. In such case that they are unable to reach such an amicable resolution, the Parties shall submit such dispute to arbitration under this subsection.

9.2.1 The arbitration shall be held subject to the provisions of this clause:

i) Pretoria;

ii) informally;

(iii) in accordance with the provisions of the Arbitration Act No 42 of 1965, as amended and/or further Rules agreed on between the parties or directed by the arbitrator.

9.2.2 The parties will endeavour to nominate an arbitrator within seven days after the dispute has been referred to arbitration by any of the parties and if the parties are unable to nominate an arbitrator either party may approach the president of the Law Society of the Northern Provinces to appoint an arbitrator.

9.2.3 The arbitrator shall, if the question in issue is:

(i) primarily an accounting matter, an independent chartered accountant, together with a legal arbitrator referred to in ii) below or;

(ii) primarily a legal matter, preferably a retired judge of the High Court of South Africa or a practicing senior counsel practicing at the Pretoria bar of advocates;

(iii) any other matter, an independent person so agreed on or appointed.

9.2.4. The parties irrevocably agree that the decision in the arbitration proceedings shall be final and binding on them, shall be carried into effect and may be made an order of court on application of any of the parties. No party shall have the right to appeal.

9.2.5. Nothing contained in this clause shall preclude any of the parties from approaching a court of competent jurisdiction for interlocutory or urgent relief.

10 **NOTICE**

10.1 All notices required under this Agreement, and all communications made by agreement of the Parties, shall be made in writing, and shall be delivered either personally, by facsimile, e-mail or by mail. The date of actual receipt by the receiving party shall be deemed the date of notice under this Agreement. The addresses of each Party for purposes of notice under this Agreement shall be as follows:

For VR ASIA:

Mr Pieter van der Merwe

10 Haggie Road, Boksburg, RSA

PO Box 5362, Boksburg North, 1461

Tel: 011 306 8000, Fax: 011 306 8018

E-mail: pieterm@vrlaser.co.za

For DENEL:

Mr Zwelakhe Ntshepe

Denel SOC ltd Office

Nellmapius Drive, Irene, Centurion

PO Box 8322, Centurion, 0046

Title: Chief Executive Officer

Tel: 012 671 2853

Fax: 012 671 2751

E-mail: zwelakhen@denel.co.za

10.2 No right or obligation under this Agreement shall be transferable or assigned to any third party without the express agreement in writing of the other Party.

10.3 No modification or amendment of this Agreement shall be valid without such amendment being in writing and signed by both Parties.

10.4 If any provision contained in this Agreement is or becomes ineffective or is held to be invalid by a competent authority or court having final jurisdiction thereover, or

the competent authorities find a provision to be invalid or request modifications, all other provisions of this Agreement shall remain in full force and effect and there shall be substituted for the said invalid provision a valid provision having an economic effect as similar as possible to the original provision.

10.5 This Agreement and any documents attached hereto constitute the entire agreement between the Parties with respect to the transactions contemplated hereby and, except as otherwise expressly set forth herein, supersedes all prior discussions, understandings, agreements and negotiations between the Parties with respect to such subject matter

THIS DONE AND SIGNED AT CENTURION ON THIS 27TH DAY OF OCTOBER 2015.

WITNESSES:

1. _____

2. _____

MR ZWELAKHE NTSHEPE OBO DENEL

(Duly authorised)

THIS DONE AND SIGNED AT CENTURION ON THIS 27TH DAY OF OCTOBER 2015.

WITNESSES:

1. _____

2. _____

MR PIETER VAN DER MERWE obo VR ASIA

(Duly authorised)

COMMISSION OF INQUIRY
STATE CAPTURE

MARKET OPPORTUNI

Country	Products	USD'm Order Intake Opportunities							
		2016	2017	2018	2019	2020	TOTAL	2015	
INDIA (10 year market presence)	Turrets/Vehicles (Infantry Fighting Vehicle Program)	-	2,000,000	-	-	-	2,000,000	-	
	T5-52 Truck Mounted Artillery Gun	-	-	2,849,000	-	-	2,849,000	-	
	35mm Air Defence Cannon	-	100,000	-	-	-	100,000	-	
	Automatic Grenade Launcher	135,000	-	-	-	-	135,000	-	
	NTW20 Anti-Material Rifle	28,700	-	-	-	-	28,700	-	
	Unmanned Aerial Vehicle	-	-	-	-	-	-	-	
	155mm Ammo	-	-	-	-	-	-	-	
	Bi-Modular Charges	-	-	-	-	-	-	-	
	Total	163,700	2,100,000	2,849,000	-	-	5,112,700	-	
BANGLADESH	105mm Towed Artillery Gun	-	64,800	-	-	-	64,800	-	
	155mm Towed Artillery Gun	-	90,000	-	-	-	90,000	-	
	105mm Ammo	-	-	-	-	-	-	-	
	155mm Ammo	-	-	-	-	-	-	-	
	Bi-Modular Charges	-	-	-	-	-	-	-	
	Total	-	154,800	-	-	-	154,800	-	
SINGAPORE	GI2 Naval Cannon Systems	24,100	-	-	-	-	24,100	-	
	Total	24,100	-	-	-	-	24,100	-	
THAILAND	GI2 Naval Cannon Systems	6,000	-	-	-	-	6,000	-	
	GI30 Naval Cannon	75,000	-	-	-	-	75,000	-	
	105mm Towed Howitzer	-	-	165,600	-	-	165,600	-	
	155mm Towed Howitzer	-	-	-	-	45,000	45,000	-	
	155mm Self-Propelled Howitzer	-	-	-	-	42,000	42,000	-	
	35mm DPG Naval Cannon	50,000	-	-	-	-	50,000	-	
	Total	133,000	-	165,600	-	87,000	385,600	-	
IND[illegible]SIA	PK-20 Turret	89,460	-	-	-	-	89,460	-	
	Total	89,460	-	-	-	-	89,460	-	
PHILIPPINES	GI2 Naval Cannons	-	17,010	-	-	-	17,010	-	
	GI30 Naval Cannon	-	-	36,000	-	-	36,000	-	
	Total	-	17,010	36,000	-	-	53,010	-	
VIETNAM	35mm DPG Naval Cannon	-	50,000	-	-	-	50,000	-	
	Total	-	50,000	-	-	-	50,000	-	
MYANMAR	35mm DPG Naval Cannon: Manufacturing licence	10,000	-	-	-	-	10,000	-	
	Total	10,000	-	-	-	-	10,000	-	
	TOTAL USD	$ 420,260	$ 2,321,810	$ 3,050,600	$ -	$ 87,000	$ 5,879,670	$ -	$
	TOTAL RAND	R 5,253,250.00	R 29,022,625.00	R 38,132,500.00	R -	R 1,087,500.00	R 73,495,875.00	R -	R

INFO STATE CAPTURE

ANNEXURE “KT8”

DENEL GROUP

Tel: +27 12 671 2938
Fax: +27 12 671 2944
Email: zwelakhen@denel.co.za
Ref: Ltr/NT/Denel Asia/2015

10 December 2015

The Honourable Minister D Van Rooyen (MP)
Minister of Finance
Department of National Treasury
Private Bag X115
PRETORIA
0001

PER HAND

Dear Honourable Minister

FORMAL APPLICATION FOR APPROVAL IN TERMS OF SECTION 51(1)(g) OF THE PUBLIC FINANCE MANAGEMENT ACT 1 OF 1999 – PROPOSED ESTABLISHMENT OF DENEL ASIA SOC LIMITED

We refer to the pre-notification letter dated 29 October 2015, addressed to the Honourable Minister Nene, which pre-notification served to inform the Department of Finance in terms of Section 51(1)(g) of the Public Finance Management Act 1 of 1999 ("PFMA") of the proposed establishment of a joint venture company in Hong Kong.

We hereby submit the formal application required in terms of the PFMA. In this regard, we shall simultaneously herewith advise the Department of Public Enterprises of the proposed establishment of a joint venture company in Hong Kong and its limited financial impact on Denel SOC Limited.

Should any further information be required, please do not hesitate to contact either the Denel Executive Management or myself.

Yours faithfully

Mr L. D. Mantsha
CHAIRMAN OF THE DENEL BOARD
11/12/2015

cc. Honourable Minister L. Brown (MP) — Minister of Public Enterprises
Mr Richard Seleke — Director-General: Department of Public Enterprises
Mr Lungisa Fuzile — Director General: National Treasury
Mr Zwelakhe Ntshepe — Acting GCEO: Denel

Denel SOC Ltd, Reg No 1992/001337/30, Nellmapius Drive, Irene
P O Box 8322, Centurion, 0046, South Africa. Tel: +27 (0)12 671 2700, Fax: +27 (0)12 671 2751
Directors: Mr L D Mantsha (Chairman), Mr R Saloojee[1] (Group Chief Executive Officer), Ms M Kgomongoe, Mr T D Mahumapelo, Ms P M Mahlangu, Ms N Mandindi, Mr Z Mhlontlo[1], Ms R Mokoena, Mr N J Molseki, Mr T J Msomi, Lt Gen T M Nkabinde (rtd), Ms K P S Ntshavheni.

[1]Executive Director
Group Company Secretary: Ms E M Africa


COMMISSION OF INQUIRY
INTO STATE CAPTURE

APPLICATION IN TERMS OF SECTION 54(1), 54(2)(a), 54(2)(b) and 54(2)(e) OF THE PFMA

1. EXECUTIVE SUMMARY

This document has been prepared in terms of Sections 54(1), 54(2)(a), 54(2)(b) and 54(2)(e) of the Public Finance Management Act No. 1 of 1999 ("**PFMA**"), as the intention of Denel SOC Ltd ("**Denel**") is to increase its international footprint and capabilities in line with its growth strategy.

The said application seeks to, inter alia, present a comprehensive business case for the establishment of "Denel Asia SOC Limited" ("**Denel Asia**") which would be a new subsidiary limited liability company in Hong Kong, with a view to exploiting opportunities in the Asia Pacific defence market.

It is intended that Denel Asia itself will, subject to applicable local legal requirements, in the future also establish further subsidiaries and/or joint venture companies in the Asia region.

2. BACKGROUND

Denel's growth strategy is based on, inter alia, making inroads into global target markets. The current Denel strategy, based on the internal strengths and weaknesses as well as a regional analysis, is to actively pursue opportunities in the Asia-Pacific market in which Denel has been active since the early 1990's.

2.1. Reasons why this transaction is not proposed in the 2015/2016 Corporate Plan

The proposed establishment of Denel Asia was not included in the 2015-2016 Corporate Plan, for inter alia, the following reasons:

(i) The Asia Pacific market did not play a significant role in Denel's order cover for the 2015/2016 financial year because Denel was excluded from business in India, one of Asia Pacific's largest markets. The reasons for Denel's exclusion from India are fully detailed in **paragraph 5.4** below. The opportunity to re-enter Asia-Pacific presented itself when the Indian Ministry of Defence (MOD) lifted its blacklisting against Denel as prior to the upliftment of the blacklisting, Denel could not contemplate the opportunity for doing business in India.

(ii) Further, the new Board of Directors of Denel, which was appointed only in July 2015, sought to extend Denel's participation in the Asia Pacific market as a way of increasing the order book. This emanated from the fact that there are immediate opportunities that Denel can take advantage of.

2.2. Governance Process: Denel Internal Approvals

ACTION	TIMELINE
Approval by Denel Board to explore a suitable equity partner for the Asia Pacific region	10 September 2015
Final approval by the Denel Board of the identified equity partner together with the draft PFMA application subject to, inter alia, Denel obtaining the requisite regulatory approvals and subject to certain conditions, which conditions have been dealt with in **paragraph 10.1** below.	7 December 2015

2.3. The reasons for Continent Specific vs Country Specific Arrangement and preference for Hong Kong

(i) Hong Kong is strategically located for business in Asia and can really be seen as the best gateway for doing business in that jurisdiction.

(ii) Conducting general business in Hong Kong is simple and setting up offices and structures are quick and inexpensive.

(iii) Foreigners can own 100% of a Hong Kong company and are free to be the sole directors and shareholders of a Hong Kong company. There are no local resident requirements and there are no restrictions on nationality.

(iv) A Hong Kong company offers global recognition and is very stable. Hong Kong is one of the world's major trading, finance and service centres.

(v) To open a Hong Kong company, you don't need a physical address in Hong Kong and your physical presence in Hong Kong is not required

(vi) Hong Kong adopts a territorial source principle of taxation meaning that all profits generated outside of Hong Kong are tax free and profits generated inside Hong Kong are taxed at 16.5%.

(vii) The legal system in Hong Kong is still ruled by British law.

3. REGIONAL STRATEGY

3.1. Studies Undertaken

Rapid and uneven economic development across 25 countries and regions of the Asia-Pacific region both enables and demands new approaches to national defence. By 2018, as global defence spending increases by 5.5 percent, defence budgets across the Asia-Pacific (excluding the US) are expected to grow by over 19 percent (Asia Pacific Defence Outlook 2015 – Deloitte report).

Rapid economic development has also created new sources of vulnerability. While the advancements are essential for developed economies, they require governments to plan for their defence, driving defence budgets and technical requirements upwards and increasing security threats have led to substantial increases in defence spending.

Increasing Global terrorism is also playing a major role in this region. Five Asia-Pacific countries – Pakistan, Philippines, India, Thailand and Bangladesh – accounted for 36 percent of the rise in global terrorist incidents between 2004 and 2013, and 97 percent of the increase within Asia-Pacific. While actual incidents of terrorism remain concentrated in a few nations, regional concerns about terrorism are increasing as Islamic State-related attacks and propaganda proliferate. This also leads to increased defence spending.

Asia-Pacific defence budgets increasingly emphasize procurement and research and development, as nations develop indigenous defence industrial bases and pursue advanced defence technology. Procurement and R&D are projected to grow by 29 and 28 percent respectively from 2014 to 2018, reflecting plans for major new acquisitions in most countries in the region.

Procurement Budget Increases by country

Country	% Increase (2014-2018)	Growth Focus
India	25	Develop Industrial base. Land Based systems Artillery and Infantry weapon systems. Air Defence programs
Singapore	18+	Technology Partners
Cambodia	18+	R&D and Industry development focus.
Indonesia	18+	R&D and Industry development focus. Land Based systems
Pakistan	11	Not Publicly published. Based on current requests. Air Defence and Artillery focus
Vietnam	18+	R&D and Industry development focus. Land Based systems and Air Defence
Philippines	85	R&D and Industry development focus. Land Based systems and Air Defence.

By 2018, rapidly-developing Asia-Pacific nations will command more than half of non-US global defence procurement and two-thirds of non-US defence research and development, making the region a key defence market, and a potent force in defence technology innovation and advancement. Therefore, Denel needs to be in this space.

3.2. Strategic Relevance of Asia

Countries such as India, Indonesia, Singapore, Thailand, Vietnam and China are considered to be primary target markets for Denel whilst markets such as the Philippines, Myanmar, Sri Lanka and Bangladesh form secondary target markets.

In analysing the Denel business in the Asia Pacific region, the following emerged to Denel management as barriers to entry into this fast growing market:

- lack of multilateral defence relationships;
- inability to provide funding solutions;
- inability to source local production and development partners (particularly in India);
- frequent engagement with end user and industry from a distance not feasible;
- company visibility in the market place/region from a distance not possible;
- need for a lawful conduit for developing/Aligning with local business networks; and
- active participation in regional initiatives from a distance are not feasible.

3.3. Hong Kong as the Country of Incorporation for a Private Limited Company

The salient business requirements for Hong Kong particularly with respect to undertaking business in this jurisdiction is set out in **paragraph 4** below. In essence, the financial, regulatory and legal requirements are substantially similar to that applicable to companies in South Africa.

4. COMPREHENSIVE DUE DILIGENCE REPORT ON THE FINANCIAL REGULATORY LEGAL REQUIREMENTS AND REGULATORY LAWS GOVERNING FOREIGN OWNED ENTITIES IN HONG KONG

Denel has been advised that:

- Hong Kong is situated in the south-eastern coast of China. With a total area of 1104km^2. The territory comprises Hong Kong Island, Kowloon Peninsula, and the New Territories, which also includes 262 outlying islands.

- Hong Kong became a Special Administration Region of the People's Republic of China on 1 July 1997, after a century and a half of British colonial administration. Under the "one country, two system" policy and constitutional documents, the Basic Law, Hong Kong's existing economic, legal and social systems will be maintained for at least 50 years. Hong Kong does however enjoy a high degree of autonomy except in defence and foreign affairs.

- While the People's Republic of China follows a civil law system, Hong Kong's legal system is based on the traditions of its former colonial master, England. As such, English common law continues to have sway. As in the British system, lawyers are either solicitors (handling paperwork, negotiations, and settlements) or barristers (who can appear in court). The Hong Kong "Basic Law" functions as Hong Kong's constitution, subject to interpretation by the Standing Committee of the National People's Congress.

- The Basic Law of Hong Kong ensures Hong Kong's autonomy in its executive, legislative, and judicial systems, as well as certain foreign relations. It protects freedom of expression, assembly, and religion, forbids torture and unwarranted searches, seizures, and arrest. Furthermore, Hong Kong is ardently capitalist, in spite of Mainland China's (nominal) adherence to socialism.

- Every year since 1995 to about 2013, Hong Kong was voted the world's most free economy by the Heritage Foundation and the Wall Street Journal's Index of Economic Freedom. It also has one of the lowest tax rates in the world. According to studies conducted by PricewaterhouseCoopers and the World Bank Group, Hong Kong is the fourth-easiest place in the world to pay taxes, just behind three countries in the Middle East.

- Hong Kong is ideally located in the heart of Asia and serves as a gateway to and from Mainland China amongst others. These advantages make Hong Kong an attractive place for foreign investors.

- The Companies Ordinance (the "CO") is the main piece of legislation governing companies in Hong Kong.

- Types of Permitted Operations in Hong Kong

  Depending on the scope of operations, foreign companies seeking to operate in Hong Kong have **three** alternative permitted forms of business presence:

  - Representative Office
    A representative office is suitable for a foreign company that intends to conduct only minimal activities in Hong Kong. A representative office cannot conduct any trade, professional, or business activities or transactions in Hong Kong and cannot enter into any contracts in Hong Kong. A representative office is appropriate, for example, for acting as a liaison office without creating any binding business obligations.

  - Branch Office
    If a foreign company establishes a place of business in Hong Kong, it will require registration as a foreign company under the CO. A "place of business" includes a place used by a company to transact any business that creates legal obligations. The foreign company is liable for the debts and liabilities of its Hong Kong branch, and a branch office cannot take full advantage of Hong Kong's tax benefits.

  - Hong Kong Subsidiary
    Due to the limitations of a representative office and branch office as described above, foreign companies usually favour establishing a Hong Kong–incorporated company as a subsidiary to operate in Hong Kong. **This is generally the preferred type of business structure because the entity may be sued only to the extent of the limited assets of the Hong Kong subsidiary**.

- Classification of a Company

  - Under the CO, a "private company" is a company that restricts the right to transfer its shares, prohibits public subscription for its shares or debentures, and limits the number of shareholders to 50. Any company which cannot satisfy all three requirements is a public company. A public company can be listed on a stock exchange or unlisted.

  - A company can also be classified by whether it is limited by shares or by guarantee, or is an unlimited company. We have limited our discussion to a company limited by shares, which is the most common type and is usually referred to as a "limited company." A company limited by guarantee in Hong Kong is usually a non-profit organization.

- The CO makes it clear that there are five types of companies that can be set up under the CO:
  - a public company limited by shares;
  - a private company limited by shares;
  - a public unlimited company with a share capital;
  - a private unlimited company with a share capital; and
  - a company limited by guarantee without a share capital.

- Requirements for a Hong Kong Private Company

  At a minimum, a Hong Kong private limited company must have the following:
  - one shareholder;
  - one director;
  - a company secretary;
  - a registered office address in Hong Kong;
  - an auditor; and
  - a business registration certificate.

- Director
  - A director must be at least 18 years of age, must not be an undischarged bankrupt, must not be subject to a disqualification order, must comply with any share qualification requirement, and must consent to act. There is no restriction on the nationality of a director.
  - A private company can have a director that is a corporation but at least one director must be a natural person.

- Company Secretary

  A company secretary must either be an individual resident in Hong Kong or a company with a registered office or place of business in Hong Kong.

  - Business Registration Certificate
    - A one-stop Company and Business Registration Service has been launched by the Companies Registry and the Inland Revenue Department. Applications for both incorporation and business registration are undertaken simultaneously.
    - In addition to the business registration certificate, certain types of businesses may need additional forms of licensing. For example, a company conducting regulated financial services activity (such as asset management, dealing in securities, or advising on securities) in Hong Kong requires licenses from the Securities and Futures Commission.

  - Generally
    - There is no prescribed minimum paid-up capital. Under the CO, the concept of nominal or authorized share capital and nominal or par value was abolished. Instead, the articles of the company with a share capital must include a statement of capital containing some prescribed information and the initial shareholdings.
    - The same person can be the secretary, director, and shareholder of a company, except that the sole director of a company cannot also be the secretary of the company.

- A company's statutory records must be kept at its registered office. If they are kept at a different place, a notice must be filed with the Companies Registry.
- Under the CO, the articles of association are the sole constitutional document of the company.

- Information Available to the Public
  Compared to other jurisdictions (e.g., the British Virgin Islands and the Cayman Islands), Hong Kong companies are much more transparent in terms of information that is available to the public. In addition to basic information, one can search for all the documents filed with the Companies Registry in relation to a particular company. One can also search for the registered charges (securities in favour of third parties) of a company and disqualification orders made. Moreover, one can search for all the companies in which an individual has directorships and the particulars of that director, such as his or her identity number and residential address.

- Establishing a Private Company

  There are two ways of establishing a private company in Hong Kong which is either by incorporating a new company or buying a shelf (or existing) company.
  - Incorporation involves applying to the Companies Registry, which then issues a certificate of incorporation within four working days after submission of the application by post (online applications may be processed within an hour). The newly incorporated company then needs to be activated by holding its first board meeting and a shareholders' meeting, if necessary.
  - Buying a shelf company is useful when a company is urgently needed. One just needs to acquire a shelf company and then activate it by effecting a change of shareholders and directors and holding a board meeting (and a shareholders' meeting, if necessary).

- Continuing Compliance Requirements
  - A company should hold an annual general meeting (AGM) each year, and not more than 15 months from the previous AGM, unless everything that is required to be done at the meeting is done by written resolution and the relevant documents are provided to each member.
  - The following matters are usually dealt with at the AGM:
    - adoption of audited accounts comprised of the balance sheets, directors' report, and auditors' report;
    - declaration of dividends;
    - election of directors; and
    - appointment of auditors.

  - The CO provides that a company is not required to hold an AGM if it has only one member or the AGM is dispensed with by unanimous members' consent.

  - Other compliance requirements include, among others, the following:
    - a company should keep a register of members and a register of directors and secretaries;
    - various returns have to be filed with the Companies Registry within stipulated deadlines for changes in relation to the company, such as changes in directorship and secretary, registered office, share capital, etc.;
    - a company must file an annual return;
    - a company must have annual audited accounts. The CO prescribes detailed requirements regarding the types of accounts to be prepared. A directors' report must also be prepared in conjunction with the annual accounts;

- shareholders' or board meetings should be held as may be necessary or required under the CO. The minutes or written resolutions should be filed in a minute book and resolutions or notices should be filed with the Companies Registry as required under the CO; and
- a company also needs to renew its business registration certificate before it expires and file profit tax returns for the company and the employer's return for its employees with the Inland Revenue Department.
- If a company fails to comply with these requirements, the company and every officer of the company who is in default may be liable for a fine and/or imprisonment.

- Tax Issues

  - Profits Tax
    - Hong Kong adopts a territorial corporate tax system. Corporations are taxed on profits at a rate of 16.5% percent. Profits tax is charged on Hong Kong–sourced profits and is collected by the Inland Revenue Department. The tax rate on profit derived in Hong Kong is the same for Hong Kong and foreign companies.
    - Specifically, domestic and foreign entities meeting the following three criteria are subject to profits tax:
      - the entity carries on a trade, profession, or business in Hong Kong;
      - the profits are from such trade, profession, or business carried on by the entity in Hong Kong; and
      - the profits arose in, or were derived from, Hong Kong.
    - A Hong Kong resident may derive profits from abroad that are not subject to Hong Kong profits tax; conversely, a non-resident may be liable for tax on profits arising in Hong Kong. The question of whether a business is carried on in Hong Kong and whether profits are derived from Hong Kong is largely one of fact. Profits arising from activities conducted abroad, even if they are remitted into Hong Kong, are not subject to profits tax.

  - General Tax Benefits
    - Dividends or overseas branch profits repatriated to Hong Kong are not subject to Hong Kong tax. In addition, dividends paid by a Hong Kong company to its shareholders are not subject to Hong Kong tax in the hands of shareholders (tax already having been paid by the company on the profits underlying those dividends), nor is there any withholding tax on dividends paid to shareholders outside Hong Kong.
    - Capital gains are also tax-exempt. A stamp duty is imposed on certain documents such as share transfers, leases of real property, and sale of real property. There is no sales tax, value-added tax, or estate tax in Hong Kong.

5. SELECTION OF PARTNERS

With a focus on Asia, Denel's approach is to immediately re-enter the India market through Denel Asia as a way of building a business profile in the region. The details of the India strategy and its rationale are discussed below. The choice of partner has mainly been influenced by the plan to use India as an entry point into the Asia market.

5.1. Denel's History in India

Denel entered the India market during 1994 with a wide range of products. During the period 1998 and 2005, Denel participated in tenders issued by the Indian MOD and was

successfully awarded contracts for various products including ammunition and land systems products.

These contracts were for the supply of ammunition, explosives, anti-materiel rifles, fuses and other munitions components such as base bleeds and modular charge systems totaling circa US$ 282 623 768.00.

Some of these transactions included the transfer of technology for the relevant products sold to the Government of India.

A contract for a significant artillery program for a tracked self-propelled gun resulted in a successful trial being concluded during July 1999 to February 2000 which included the introduction of the G6. The costs of these trials exceeded R500 million. Contract negotiations commenced in February 2003 and were concluded in December 2003 with a contract value of US$ 1,180,744,682.

On 17 April 2005, an article appeared in the Cape Argus newspaper alleging that Denel had contravened specific Indian legislation. Notwithstanding the lack of proof thereof and Denel's denial that it was in breach of the MOD contracts, the MOD issued a notice of termination of the defence programs and instituted legal proceedings against Denel which resulted in, inter alia, protracted arbitrations. Contracts to the value of US$ 77,3 million were adversely affected by these actions. Denel was effectively treated in India as if it were blacklisted notwithstanding no formal blacklisting being in force.

In 2007 Denel sought to re-enter the India market as a subcontractor on a tracked gun program where Rheinmetall was the prime contractor. Successful trials for the gun took place during July 2010 and March 2011. However, in 2012, Rheinmetall was recommended for blacklisting which resulted in a termination of the said program. Denel incurred a further loss of a R11 million as a result of this termination.

This confirmed that Denel competing on its own in India on major programs is very high risk.

Since Denel's absence from the market, the procurement rules changed significantly on major programs. In particular, it introduced the requirement for a local Indian Industry partner/s based on the "Buy Make India" procurement program. This mandatory requirement combined with Denel's previous unsuccessful attempts to access and remain successful in the Indian market reconfirmed the need for Denel to identify and rather proceed with a local partner in India as opposed to its own.

5.2. Buy Make India

The India "Buy Make Program" requires that local content should be more than 50% as well as inclusion of technology transfer from the foreign Original Equipment Manufacturer (OEM).

Denel is positioning itself for major programs in India which programs are premised on the 'Buy Make India' concept. This means that only Indian Companies that can prove that they have partnered with "foreign technology companies" are allowed to bid as prime contractors.

The Indian procurement process demands a strenuous and protracted product evaluation process which can become extremely costly (as detailed in **paragraph 5.1** above and experienced first-hand by Denel).

5.3. India Remains a Lucrative Market

Despite Denel's previous lack of success in the India market, due largely to circumstances outside its control, the Asia Pacific region and specifically the Indian market remains a lucrative market as more fully set out in **paragraph 3.1** above.

5.4. Possible Partners Explored

As detailed in **paragraph 5.1** above, Denel was inactive in the India market for a significant length of time until verbal notification was received late in 2014 from the Indian Embassy in South Africa informing Denel that the investigation was completed and that we may proceed to conduct business in India.

It must be pointed out that the defence industry is a niche market and the norm in this industry is that a competitor can easily become a strategic partner and vice versa depending on the type of opportunity being explored by the parties.

As Denel needed to finalise a partner in light of a Request for Information (RFI) to be issued on the mounted artillery gun program, an industry visit took place during February 2015 wherein Denel visited the following potential business partners. Securing a suitable partner proved to be unsuccessful as most of the potential business partners that Denel considered were already aligned to other companies. For example, Denel considered the following companies:

a) *Bharat Forge*
They have a large forging capability and are a well-established defence contractor. They were however already committed to ELBIT (Israel Company) on artillery programs.

b) *Larsen and Toubro*
They are a well-established defence contractor but were already committed to NEXTER (French company) on artillery programs.

Given the significant changes in the procurement process as well as Denel's previous unsuccessful experiences coupled with our own internal strengths and weaknesses, a decision was taken not to participate in major programs in India unless there was a distinct advantage that presented itself and which would increase the possibility of us successfully participating in the Indian market.

VR Laser presented to Denel, on an unsolicited basis, a value proposition that was worth considering. The value proposition, more fully set out in **paragraph 5.2** below, was attractive to Denel as it was based on VR Laser Asias' experience as well as market studies conducted during the planning phase of re-entry into India. VR Laser Asia's value proposition allows for Denel to enter into the India market as well as the wider Asia Pacific market.

In the past, Denel has incorporated similar joint venture companies in other countries with some of its suppliers as in the case of Tawuzan Dynamics, a joint venture company incorporated in the UAE. Denel has seen and continues to see significant benefits in the incorporation of this joint venture.

Key aspects of the Tawazun Dynamics Joint Venture are, inter alia:

- It is a risk sharing model; and
- Intellectual Property (IP) is licenced in Tawazun Dynamics in order to discharge offset obligations.

5.5. Value proposition of VR Asia

As previously indicated, a decision was initially taken (prior to VR Laser Asias approach) not to re-enter the India market given the informal blacklisting and having not been in the market for a significant length of time.

It is evident that, in order to be successful on any major defence program in the world, there needs to be a balanced strategy which encompasses, inter alia, the following:

(i) A defence solution that supports national objectives
The VR Asia proposition brought an understanding on national objectives at an industry level and industry knowledge in the form of a well-established, highly respected and highly successful India partners being PIPAVAV and the Adani Group. The Adani Group is an Indian multinational conglomerate company. It has a diversified business portfolio covering resources, logistics, agribusiness and energy supply. The company was founded in 1988 as a commodity trading business. The founder and Chairman, Mr Gautam Adani is a well established business man and has vast knowledge of setting up significant programs. Similarly, PIPAVAV is a reputable Indian company which operates in the armament industry with knowledge of the Indian market.

(ii) Compliance to the user specification with a competitive value proposition
The VR Asia proposition at this level is again Industry knowledge, setting up the not so obvious contenders in a business venture. As indicated above, Denel's initial evaluation of possible partners was unsuccessful as the main contenders were already committed or not willing to share the risk. Through, for example, the Adani business partners in India as well as risk sharing by Indian partners such as PIPAVAV during the pre-contracting phase of the program, participation will be possible. The value proposition in the bidding process will be an Indian solution with local content growing new contenders and establishing new technologies as directed by policy.

(iii) A competitive technical solution
The VR Asia proposition at this level is technical skills in VR South Africa as well as operational funding.

5.6. VR Laser Asia as a partner of choice

Denel has thus concluded that VR Laser Asia Limited, a company incorporated in Hong Kong (**"VR Asia"**), and aligned with one of Denel's local fabrication specialists (VR Laser South Africa Proprietary Limited (**"VR RSA"**)), as a suitable partner to form a joint venture company. VR RSA, on behalf of VR Asia has presented a suitable business model to Denel for consideration. VR RSA has also undertaken to fund VR Asia in order to enable VR Asia to meet its funding commitments to Denel Asia.

Denel's traditional strength lies in the areas of concept, design, prototyping and weapons integration. In partnering with VR Asia, Denel obtains access to VR RSA's strong capability in industrialisation, production and support of armoured and specialised vehicles.

The advantages of Denel entering the Asia market with VR Asia includes:

- the provision of design, manufacturing and fabrication skills
- a deeper understanding of the local market and industrial landscape
- the ability to align with local business networks
- the provision of quick access to local potential production and development partners
- the ability to increase visibility in the market/region
- access to operational funding

- the ability to grow the business in a sustainable manner
- the ability to share all demonstration costs proportionately to its shareholding

For the above reasons the partnership with VR Asia, who has satisfied Denel that it is familiar with the landscape of Denel's primary and secondary target markets, makes commercial sense.

Further, it makes commercial sense for Denel to establish a footprint in the market. In order to mitigate the costs and risk of a new market entry, Denel management are of the view that a risk sharing model be adopted. This entails that Denel enter into a joint venture with VR Asia to form Denel Asia.

It is reiterated that VR Asia is a partner of choice for Denel for reasons, which include, details as set out in this **paragraph 5**, the unsolicited approach made by VR Asia together with, inter alia, its value proposition and the commercial relationship enjoyed between VR Laser RSA and Denel Land Systems (a Denel entity) which has resulted in mutual trust and recognition between the respective parties.

6. ADVANTAGES OF PARTNERING WITH VR LASER ASIA

6.1. Registration Details and shareholding of VR Laser Asia

The registration details of VR Laser Asia are: **VR LASER ASIA LIMITED**, (Company No. 2111273) whose registered office is at Block A, 15/F, Hillier Comm Building, 65-67 Bonham Strand East, Sheung Wan, Hong Kong.

The sole shareholder of VR Laser Asia Limited is Mr Salim Aziz Essa, a South African national with passport no. M00073786. Mr Essa is via the entity Elgasolve Proprietary Limited, the controlling shareholder of VR Laser South Africa Proprietary Limited.

6.2. Networking Capability Expanded

As mentioned in **paragraph 5.2** above, VR Laser Asia's network includes, but is not limited to, the following reputable Indian businesses:

6.2.1 Adani's Profile

Mr Gautam Adani, the Chairman and Founder of the Adani Group, has more than 33 years of business experience. Under his leadership, Adani Group has emerged as a global integrated infrastructure player with interests across Resources, Logistics and Energy verticals.

Mr Adani's success story is extraordinary in many ways. His journey has been marked by his ambitious and entrepreneurial vision, coupled with great vigour and hard work. This has not only enabled the Group to achieve numerous milestones but also resulted in creation of a robust business model which is contributing towards building sound infrastructure in India.

Quoted from the Chairman message:

"The government's call for 'Make in India' shall get a fillip with a robust infrastructure that is world class and facilitates the manufacturing industry. It is our endeavour to narrow the energy demand and supply gap, build world class ports so that India becomes a shipping hub and operates mines across the globe with environmental concerns addressed most optimally.

We look forward to make inroads into new sectors of infrastructure and aim to excel in all our initiatives."

Adani's Vision

As part of preparing the Group for the next phase of our growth, we have re-formulated our 2020 vision:
"To be a globally admired leader in integrated infrastructure businesses with a deep commitment to nation building. We shall be known for the scale of our ambition, speed of execution and quality of operation."

(Source: Adani website)

6.2.2 PIPAVAV's Profile

Reliance Infrastructure, together with its wholly owned subsidiary Reliance Defence Systems Private Limited, acquired in March 2015, a controlling share from the promoters of Pipavav Defence.

Reliance Infrastructure Limited (RInfra) is amongst the largest Infrastructure Companies in India, developing Special Purpose Vehicles (SPVs) in several high growth sectors within the Infrastructure space.

PIPAVAV Defence is India's first world class company integrated Defence production company. PIPAVAV was the first private sector company to get a license and contracts to build frontline warships for the Indian Navy.

PIPAVAV has strong partnerships with Global players such as:

- SAAB Technology AG, Sweden on technology transfer for the manufacturing of missiles, underwater systems and Aero-structures for fighter jets
- DCNS (France) Government owned company on Naval programs
- Rosoboron Export Russia on Naval programs
- Atlas Electronica on torpedoes and Sonars for the Indian Navy
- Sagem Defence Securite, part of the Sagem Group on long range air borne multi sensor multi spectral electro optical systems

PIPAVAV has been participating in several land system projects such as:

- Upgrade of several vehicle programs such as BMP2 and tank projects
- Manufacturing and supply of Armour Personnel Carriers
- Several UAV programs

Having regard to the fact that Denel has come in as a late entry competitor on the main programs in India, our partnering options were very limited as the traditional partners that Denel could have considered were in most instances already paired with other major industry players (See **paragraph 5.1** above).

In support of Indias' national objective of developing local privately owned defence companies, partnering with (either one or both) Adani and PIPAVAV will bring major advantages in terms of Industry knowledge, manufacturing capability, setting up manufacturing partners, business knowledge and investment capital on major programs. Expanding into the Defence Business forms part of both companies growth vision and both have a history of success.

6.3. Financial Commitment

VR Laser Asia via VR Laser RSA has committed R100 million in terms of a shareholder loan on an arms-length basis with interest (being at normal market rates).

Denel intends to negotiate a higher amount to be paid at the outset and should this be unsuccessful, it will be referred back to the Denel Board.

Should the joint venture be unsuccessful within the first 5 years of incorporation of the company, VR Asia will not have recourse to Denel to repay the loan but shall bear this risk in totality. This is articulated in the Shareholders Agreement.

7. BUSINESS MODELS

As indicated in **paragraph 5,2** above, Denel can best position itself for programs based on the 'Buy Make India' concept. In addition, if there are any similar requirements within the Asia Pacific region, it will be easier to leverage on these opportunities from the India base.

Set out in **paragraph 8** below are the 2 main business / contracting models that may arise from identified opportunities in the Asia Pacific region hereafter referred to as Scenario 1 (No Production Scenario) and Scenario 2 (Production Scenario) respectively.

8. CONTRACTING MODEL

8.1. Joint Venture Governance

In order to implement Denel's chosen risk mitigation strategy, Denel has elected that a new limited liability company be registered in Hong Kong (Denel Asia). This ensures that Denel does not inherit any legacy concerns and ensures a speedier due diligence process.

Notwithstanding the fact that Denel Asia will be incorporated in Hong Kong, Denel has to ensure that Denel Asia will be established and managed in line with its status as a state owned company, reflecting Denel's own corporate governance best practices and standards. In this regard, Denel has negotiated a favourable shareholders' agreement entrenching its rights and providing a contractual framework which will ensure Denel Asia's effective governance.

8.2. Contributions by the Parties

Denel management have recognised that the intended shareholders of Denel Asia have differing strengths and capabilities. In this regard, it is envisaged (and the Denel Asia shareholders' agreement provides) that:

- Denel, will be the technology partner and will hold 51% of the issued share capital and control of Denel Asia. The remaining 49% minority is to be held by VR Asia who will be the networking and industrial partner.
- Other than standard minority protections, Denel as majority shareholder will be able to influence the strategic direction of Denel Asia at a shareholder level as shareholder matters require approval by a simple majority.
- Denel Asia will pursue opportunities in Asia, and, specifically in India using the network of VR Asia. Once an opportunity translates into a firm order:

- Denel Asia may establish a subsidiary in India in order to satisfy Indian legal requirements;
- Denel Asia will pursuant to a preferential supply agreement with Denel, procure product for delivery to an Indian end-consumer; and
- If and to the extent required, VR RSA will contract, manufacture, and produce for Denel Asia for delivery to an Indian end-user.

Subject to relevant approvals, a Shareholders agreement in relation to Denel Asia has been negotiated. The current draft of the shareholders' agreement is attached hereto as **Appendix A**. The Denel Board has considered the same and taken advice thereon. They are satisfied that Denel has adequately protected itself in relation to Denel Asia.

8.3. Transaction Structure

The cooperation agreement referenced in the pre-notification letter to Minister Brown dated 29 October 2015 is to be superseded by the shareholders' agreement. In addition, Denel, VR RSA and VR Asia are to conclude:

- A standard form Denel supply agreement in relation to the supply of product by Denel to Denel Asia, which will entitle Denel Asia (as a subsidiary of Denel) to preferential pricing and procurement status; and
- A contract manufacturing agreement between Denel Asia (as customer) and VR RSA (as supplier) in terms whereof, amongst other things:
  - Denel Asia will appoint VR RSA as its preferred contract manufacturer for specialized vehicles and related products in India;
  - VR RSA will supply specialized vehicles and related products at a preferential price, given its indirect interest via VR Asia; and
  - Denel will make available to VR RSA, certain IP on a limited licensed use basis, to enable VR RSA to manufacture/fabricate product.

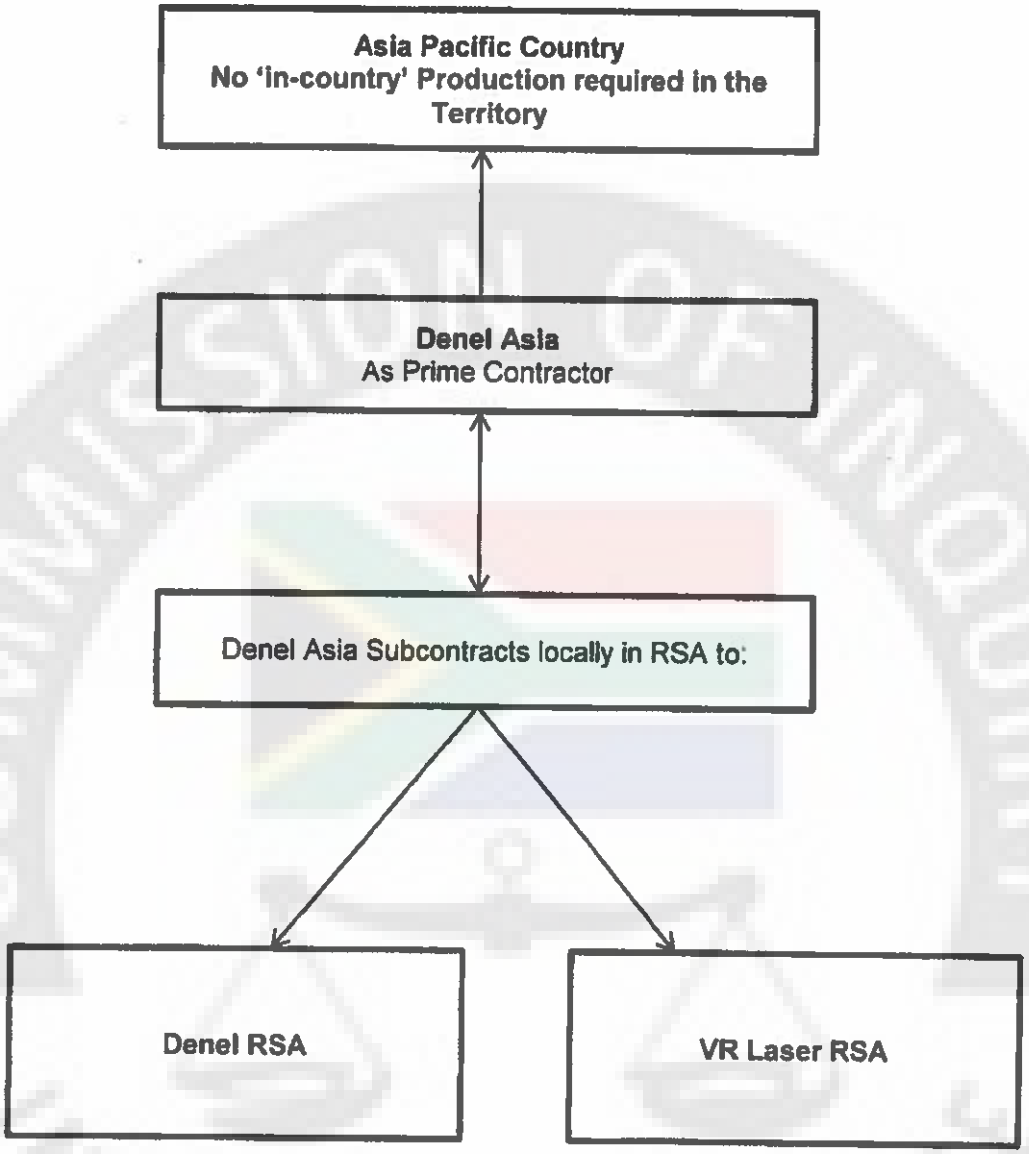
  See **paragraph 12.7** below.

8.4. Schematic representation of the contracting models

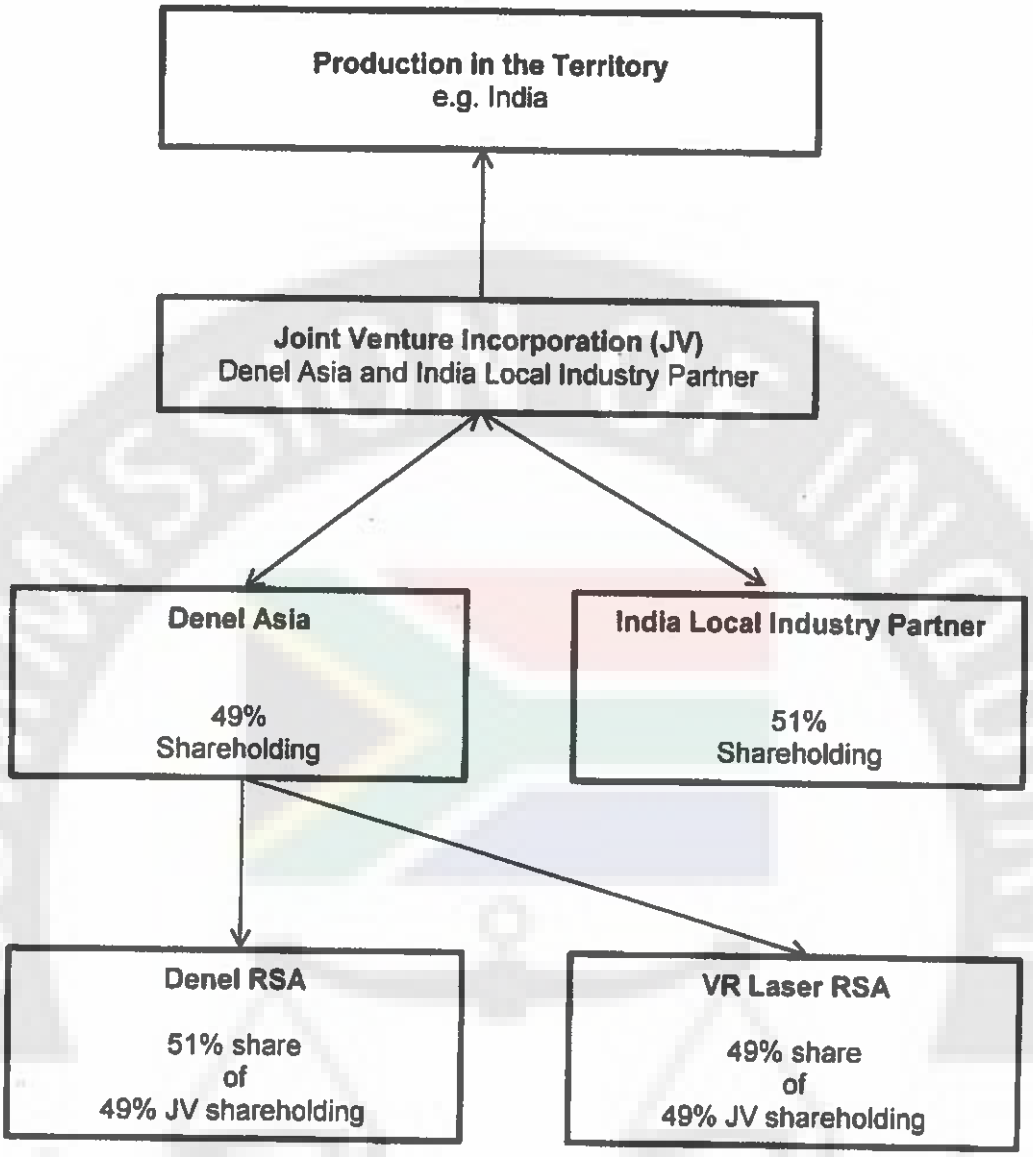
8.4.1 Scenario 1 – No Production envisaged in country

8.4.2 Scenario 2 – In country Production is envisaged

Scenario 1:


Asia Pacific Country
No 'in-country' Production required in the Territory
Denel Asia
As Prime Contractor
Denel Asia Subcontracts locally in RSA to:
Denel RSA
VR Laser RSA

Scenario 2:



(i) It is not envisaged that any production will take place in Hong Kong as this office is essentially a marketing office.

(ii) Tawazun Dynamics conducts business in accordance with Scenario 2 above.

8.5. Financing

One of the key supporting drivers for the formation of Denel Asia, is Denel's limited finance obligations. VR Asia has undertaken to invest an amount of R100 million (One Hundred Million Rand) into Denel Asia for operational costs, payable in amounts of R20 million a year for a period of five years.

Thereafter, Denel Asia will, to the extent that external funding is required, source such funding from third party funders. The shareholders (Denel and VR Asia) will also be able to provide funding by way of shareholder loans pro-rated according to their respective shareholding but they are not obliged to provide funding. Denel does not have any definitive finance obligations or exposure to Denel Asia (save for ordinary supply arrangements).

9. INTELLECTUAL PROPERTY (IP) AND LICENCING

9.1. Technology transfer and protection of Denel's IP

(i) Denel will not alienate its Intellectual Property and technology transfer will be done by way of an applicable licencing agreement between relevant parties.

(ii) Requisite approvals from Armscor and/or a third party will be obtained prior to licencing this IP.

(iii) To the extent that royalties are payable to Armscor and/or any third party, Denel Asia will be required to effect such payment.

(iv) Where Denel is the owner of the IP, there will be no royalty payable by Denel Asia as Denel is the technology partner bringing with it the technology to the joint venture subject to **paragraph 9.1 (i)** above. This is consistent with the Tawazun Dynamics joint venture model referred to in **paragraph 5.7** above.

(v) In instances where Denel cannot be subcontracted by Denel Asia for technology transfer to a local industry company in a specific jurisdiction, Denel Asia will instead be licenced with a right to extend such licence to an identified local industry company.

10. RISKS AND MITIGATION

Key risks were considered during the assessment of the business and relevant risks taken into account in the negotiation process and contractual framework. Appropriate financial and legal due diligence reviews were performed to identify and mitigate any further risks and the recommendations emanating therefrom have and/or will be adopted and implemented. **Appendix B**, **Appendix C** and **Appendix D** refers.

10.1. Transaction risks and its mitigation

	Risks	Mitigation/Remarks
1.	Reputational	• Denel has undertaken a due diligence investigation and the recommendations thereof will be implemented. • No agents will be involved. • Denel has a controlling share and thus can

Risks		Mitigation/Remarks
		control the direction of Denel Asia.
2.	Guarantees/ Finance Risk	• VR Asia is funding Denel Asia in the amount of R100 Million (R20 million a year for 5 years). Denel is to engage with VR Asia to secure a greater cash injection in the first 2 years. Denel previously unsuccessfully engaged with VR Asia on this issue. The Board has requested that a re-engagement with VR Asia on this issue is to take place. • Reduced balance sheet exposure due to partnering. • Denel has limited credit exposure to its subsidiary for normal supply arrangements on preferential terms.
3.	Penalties	• Both Denel and VR Asia, have the skill, expertise and experience to minimise the possibility of penalties being incurred.
4.	Legal Exposure	• Denel exposure is seen by the Denel board as limited.
5.	PFMA Conditions	• Denel will ensure that Denel Asia abides, to the extent applicable to the PFMA, the Denel Shareholder Compact and the Denel Risk and Compliance Frameworks. • Adherence to all shareholder conditions prior to Shareholders Agreement and ancillary agreements.
6.	Cooperation Agreement	• The Shareholders Agreement, once signed, will supersede the Cooperation Agreement (**Appendix E**).
7.	Protection afforded in terms of the Shareholder Agreement	• The agreement only becomes effective upon the fulfilment of the suspensive conditions (Clause 4). • Control vests in Denel which has a 51% shareholding (Clause 5). • There are certain reserved matters which require a 75% majority vote with other

Risks		Mitigation/Remarks
		matters requiring a simple majority of 51% in order for the resolution to be passed (Annexure B for reserved matters). • There is specific provision for the implementation of anti-bribery, anti-money laundering and anti-corruption policies in the joint venture (Clause 6). • In the event of the joint venture being wound up/dissolved prior to full repayment of the shareholders loan, no liability will accrue to Denel to settle the loan (Clause 16.2). • Denel has the right to investigate the directors and ultimate beneficiaries and shareholders of VR Asia to ensure that such persons have sufficient standing and if not satisfied, Denel has the right to demand that VR Asia repurchases the shares from that person thereby removing the person from being a shareholder of VR Asia (Clause 18.3). • The termination clause (Clause 21) relates to termination on material breach (as opposed to termination for convenience). • Provision is made for termination in circumstances where the Government directs that Denel ceases to be a shareholder for reasons of national security or otherwise (Clause 25.1) • Termination can take place by mutual agreement (Clause 25.1.3). • Termination can also take place where a party frustrates the performance of the other party by making performance impossible or unreasonably expensive or difficult, materially alters the rights and obligations of the parties or materially interferes with the benefits (Clause 25.1.4).
8.	Exit Clause: Termination for convenience	• Initial discussions with VR Asia resulted in a rejection of a clause for termination for convenience. • Denel is to engage with VR Asia and address the Board's requirement that such a clause is to be included in the agreement.
9.	Due Diligence	• The key risk identified is the potential for bribery and corruption. This is alleviated in the shareholders agreement by the obligation to abide by anti-money laundering (AML) and anti-bribery and anti-corruption (ABC) policies. • Financial viability of VR Laser Asia raising the loan – in the absence of the loan being furnished by VR Asia to the joint venture, it

Risks		Mitigation/Remarks
		will constitute a material breach and is a ground for termination. • Denel is satisfied that the loan can be legitimately be raised by VR Laser Asia via its shareholders.
10.	Double Taxation Agreement	• There are currently discussions between India and Hong Kong re a double tax agreement. • The risk of the lack of a double taxation agreement is outweighed by the lucrative opportunities that can be realised in India.

11. DUE DILIGENCE

Denel had procured that a due diligence investigation be undertaken in respect of each of the following areas, which due diligence reports are attached hereto as follows:

1. Regulatory Due Diligence – **Appendix B**
2. Legal Due Diligence – **Appendix B and Appendix C**
3. Financial Due Diligence – **Appendix D**

There were some findings of concern that was raised by the due diligence which are acknowledged. Denel management is however confident that it is able to incorporate the recommendations of the report and will adopt corrective measures in particular related to an anti-corruption policy and compliance framework coupled with rigorous monitoring thereto. See **paragraph 10.1** above.

In addition, Denel is satisfied that the shareholder loan can be legitimately raised by VR Laser Asia via its shareholders failing which the breach provision in the Shareholder Agreement will be invoked.

12. FINANCIALS

12.1. Capital Contribution

There will be a capital contribution of 1000 shares issued at USD 1 with Denel taking up 590 shares and VR Laser Asia taking up 490 shares.

12.2. Financial viability

The formation of Denel Asia in the region is opportune as it resolves many challenges that prevent Denel taking advantage of the current regional opportunities. It will also provide solutions to challenges that Denel faces at the moment i.e. to provide funding solutions.

Initially potential business amounting to USD 9,2 billion was identified. This has been tested and evaluated again and based on a realistic probability matrix on the latest marketing intelligence, the potential business is approximately USD 5.8 billion over the next 5 years which Denel could take advantage of (See **paragraph 12.3** below).

12.3. Markets and Opportunities

Denel Asia's forecasted capabilities and market interests are promising.

The business opportunity at a reduced risk via partnering constitutes a logical next step by Denel for entry into a new market. See **Appendix F** which sets out markets and opportunities.

12.4. Income Statement

R'm	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25
Sales	0	587	900	1,543	3,087	4,372	6,013	7,025	7,500
Gross Profit	0	117	180	309	617	874	1,203	1,405	1,500
Gross Profit %	0	20	20	20	20	20	20	20	20
Operational Cost	11	14	19	22	27	35	35	35	35
Labour	6	8	12	15	20	25	25	25	25
Marketing	3	4	4	4	4	5	5	5	5
Overheads	2	2	3	3	3	5	5	5	5
Additional Operating Cost to Cover Business Growth	50	46	54	55	127	184	266	316	340
Profit before Interest / Tax / Dividends	(61)	57	107	232	463	655	902	1,054	1,125

Notes

[1] The rate of exchange used was R12.50/USD.

[2] The normal yearly operational costs consist mainly of salaries for the office personnel and will increase as more resources are needed to do project management and marketing.

The marketing costs would mainly be for travel and accommodation and direct marketing in the different countries where the opportunities lies.

The operational overheads will be to rent space and equipped the office with the necessary resources to operate effectively. The IT costs will be typically be part of this.

This calculation is based on foreign offices cost structures that are managed by Denel over a very long term.

[3] The additional operating costs would mainly be used to do big system demonstrations to the potential clients. Any one big full in client country demonstrations could cost between R10m – R20m. This is based on various system demonstrations done in foreign countries.

12.5. Business Funding

Denel is satisfied that it has limited financial exposure in terms of Denel Asia due to the fact that VR Asia will be assuming the primary finance obligations of Denel Asia. Forecasted cash flows are in the view of Denel management sufficient to meet Denel Asia's obligation to VR Asia, which is without recourse to Denel.

(i) The R100m investment from the Denel partner will fund the basic office operational costs for the first few years until sales are realised. The sales from operations will cover the direct cost and increased operational costs associated with the business case.

(ii) The R100m investment will be a preferential and secured loan, which will be re-paid to the partner before any future profit sharing takes place.

(iii) No substantial capital spend will be incurred before an order is obtained and the capital investment will be recovered on the orders obtained.

12.6. Cash Flow Impact

(i) The cash shortfall in the first year would have to be financed from either a 12 month short term loan at reasonable international rates negotiate with the partner. Subsequently, the business would be self-funding and sustainable over the medium to long term.

R'm	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25
Nett Operating Cash	(61)	57	107	232	463	655	902	1,054	1,125
Investment Capital	20	20	20	20	20				
Nett	(41)	77	127	252	483	655	902	1,054	1,125

12.7. Pricing Policy

(i) There is currently a Memorandum of Agreement that specifies rates which were negotiated and agreed between VR Laser RSA and Denel Land Systems (a trading division of Denel) which provides a basis to the pricing.

(ii) **Paragraph 8.3** above refers.

13. BENEFITS

13.1. Local Manufacturing Development

By concluding a contract manufacturing agreement with VR RSA (an established provider to Denel), Denel Asia ensures the sustainability of local manufacturing expertise.

13.2. Skills Development

Due to the technological partnering between Denel, Denel Asia and VR RSA, Denel serves its obligation and desire of fostering the development of core skills and technology competencies with black owned and/or black controlled South African entities. A proposition that satisfies a number of key Denel policies.

13.3. Job Creation

By facilitating a black owned and/or controlled South African company (VR RSA), Denel Asia seeks to maintain South African jobs in the skilled and semi-skilled industry sectors. In addition, based on the projected income, significant work will result from Denel Asia contracting with both Denel and VR RSA.

13.4. Human Capital Development / Transformation

We refer the Honourable Minister to our comments contained in **paragraphs 13.1**13.1 and **13.2** above.

14. CONCLUSION

Asia is one of the fastest growing defence markets. Of the top ten worldwide defence importers in 2014, four were from Asia (India, China, Indonesia and Vietnam) with Singapore and Pakistan making 11 and 12 slots respectively. (Stockholm International Peace Research).

The formation of Denel Asia in the region is opportune as it resolves many challenges that prevent Denel taking advantage of the current regional opportunities. It will also provide solutions to challenges that Denel faces at the moment i.e. provide funding solutions.

15. IMPLEMENTATION PLAN

The following activities will take place towards contract implementation and the establishment of Denel Asia:

Action	Timeline
Negotiation and conclusion of the shareholders agreement	Draft shareholder agreement has been agreed to in principle and awaits Ministerial approval.
Establishment of the Joint Venture Company • PFMA pre-notification	Delivered on 30 October 2015
• Draft Shareholders Agreement	Circulated herewith
• Regulatory due diligence, Legal and Financial due diligence	Completed as at 27 November 2015
• Denel Board Approval	7 December 2015
• PFMA submission	10 December 2015
• PFMA Approval expected	January 2016
Approval from the financial surveillance department of the RSA Reserve Bank for establishing a subsidiary outside the common monetary jurisdiction	January 2016
Conclusion of final shareholders agreement and adoption of memorandum of incorporation.	January 2016
Joint Venture Company business activation and procuring all relevant approvals and/or registrations	January / February 2016

RECOMMENDATION

It is requested that the Honourable Minister notes and approves of Denel's intention to:

1. establish Denel Asia as joint venture company in Hong Kong which company will facilitate the legitimate securing of contracts in the Asia-Pacific region; and

2. establish any further joint ventures, particularly within the India market, to ensure the successful execution of the contracts placed on Denel Asia.

The Denel Board has approved of such establishment subject to the receipt of Ministerial approval in terms of section 51(1)(g), section 54(1) and 54 (2) of the PFMA.

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COMMISSION OF INQUIRY INTO STATE CAPTURE

LIST OF QUERIES RE PRE-NOTIFICATION LETTER

Denel's responses to the specific queries raised by the Honourable Minister has been addressed in the preceding business case. For the sake of completeness, the queries and the paragraph references in the business case to our responses are set out below.

RESPONSES TO SPECIFIC QUERIES

In response to the Honourable Minister Brown's specific queries as contained in her letter to Denel SOC Limited ("Denel"), dated 23 November 2015, we advise as follows:

1. **Comprehensive detailed business case:**
   Paragraphs 1 to 14 refers.

2. **Comprehensive due diligence report on the financial regulatory legal requirements and regulatory laws governing foreign owned entities in Hong Kong:**
   Paragraph 4 refers.

3. **Funding Plans and Transaction Documents:**
   Paragraph 12 refers.

4. **Process followed to select VR Laser as partner of choice:**
   Paragraph 5 refers.

5. **Proposed structure of new subsidiary limited liability company in Hong Kong, to be known as "Denel Asia SOC Limited" ("Denel Asia"):**
   Paragraph 8.2 above refers.

6. **Comprehensive Due Diligence of VR Laser:**
   Paragraph 11 refers.

7. **Registration Details of the company and shareholding of VR Laser Asia:**
   Paragraph 6.1 refers.

8. **The reasons for Continent Specific vs Country Specific Arrangement and preference for Hong Kong:**
   Paragraph 2.3 refers.

9. **Studies undertaken by Denel to establish VR Laser as a suitable Partner:**
   Paragraphs 5 and 6 refers.

10. **Reasons why this transaction is not proposed in the 2015/2016 Corporate Plan:**
    Paragraph 2.1 refers.

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ANNEXURE “KT9”

Mr Lungisani Daniel Mantsha
Chairperson
Denel SOC Limited
P O Box 8322
Centurion
0046

Tel: (011) 781 0099 / (012) 671 2896
Email: Dan@lungisanimanthsaattorneys.co.za / Fortunel@denel.co.za / Yvonne@lungisanimanthsattorneys.co.za

Dear Mr Mantsha

Approval in Terms of the Public Finance Management Act (PFMA): Proposed Establishment of Denel Asia SOC Limited

Your letter dated 11 December 2015 regarding the above subject matter has reference.

Before considering your application, I wish to bring the following issues to your attention:

1. The Department is unable to consider Denel's Section 54 application in the absence of Section 51 (1) (g) approval by Minister of Finance.

2. In terms of the R1.85 billion Government Guarantee, the Minister of Finance must co-approve all Denel's PFMA applications. This then requires the Department to engage and reach consensus with National Treasury (NT) before recommendations could be made to both the Executive Authority and the Minister of Finance;

3. In terms of the final submission made by Denel, the business case is not clear and the Department would like to request Denel to present the business case to the Department and National Treasury.

4. The response to the questions raised in the pre-notification letter were not sufficient due to the following reasons:

    a. Whether the business case for Denel Asia and VR Laser Asia as a partner is solid;

b. The unsuitability of VR Laser as a partner based on the due diligence. The company is technically insolvent;

c. Political considerations or support not exhausted;

d. The primary intention in setting business in Asia seems to be mainly brokering services. The application does not seem to support otherwise;

e. The inadequate financial plan, only financial projections provided.

f. The breakdown of the cost structure as well as alternatives to address the R61 million shortfall. The proposed structure provides two options with no preferred option chosen by Denel;

g. There was a request to furnish studies relating to the choice of partner. No studies undertaken by SOC which indicates the partner is viable; and

h. The reason that proposed partner not included in 2015/16 Corporate Plan is vague. The change in board does not interrupt trajectory of the business. In the formal submission, Denel indicated engagements started in February 2015.

I request that Denel addresses these issues comprehensively so as to allow myself and the Department to make a fully informed decision on this application.

Yours sincerely

MS LYNNE BROWN, MP
MINISTER OF PUBLIC ENTERPRISES
DATE:

cc.: Mr Zwelakhe Ntshepe, Acting Group Chief Executive Officer
Tel: (012) 671-2938 Email: ZwelakheN@denel.co.za / CharleneT@denel.co.za

ANNEXURE “KT10”

Charmaine Yssel

Subject: FW: DENEL_ASIA_(PFMA_§54(1)_AND_§54(2)_APPLICATION)
Attachments: MEMO_DENEL_ASIA_(PFMA_§54(1)_AND_§54(2)_APPLICATION) [partially signed].pdf; MEMO_DENEL_ASIA_(PFMA_§54(1)_AND_§54(2)_APPLICATION).DOCX; LETTER_TO_DENEL_CHAIR_DENEL_ASIA_(PFMA_§54(1)_AND_§54(2)_APPLICATION).DOCX; LETTER_TO_DENEL_CHAIR_DENEL_ASIA_(PFMA_§54(1)_AND_§54(2)_APPLICATION) [draft].pdf

Importance: High

From: Charmaine Yssel
Sent: Thursday, 24 December 2015 12:27
To: Annelize Van Wyk; Daniel Plaatjies; Phillip Mbanyana; Mogokare Seleke
Cc: Kgathatso Tlhakudi; Matsietsi Mokholo; Orateng Motsoai; Keromamang Mhlongo; Neriath Kgomongwe
Subject: RE: DENEL_ASIA_(PFMA_§54(1)_AND_§54(2)_APPLICATION)
Importance: High

Dear Colleagues,

On behalf of DDG: Tlhakudi, kindly receive soft copies of the partially signed memo and draft letter in response to Denel's formal PFMA application seeking approval to establish Denel Asia SOC Limited, in terms of Section 54(1) and 54 (2) of the Public Finance Management Act 1 (PFMA) of 1999 to establish Denel Asia SOC Limited dated 10 December 2015.

The hard copy will be submitted as per the norm.

Regards,

Ms. Charmainé Yssel:
Operations Coordinator to Mr Kgathatso Tlhakudi, DDG: MANUFACTURING ENTERPRISES (Denel, Alexkor & SAFCOL)
+27 (0)12 431 1019 +27 (0)86 763 2674 charmaine.yssel@dpe.gov.za
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Department:
Public Enterprises
REPUBLIC OF SOUTH AFRICA

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Department:
Public Enterprises
REPUBLIC OF SOUTH AFRICA

DECISION MEMORANDUM

TO	:	MS LYNNE BROWN, MP MINISTER
FROM	:	MR KGATHATSO TLHAKUDI DDG: MANUFACTURING ENTERPRISES
FILE REF	:	14/1/12/1
IDMS	:	186054
SUBJECT	:	DENEL: FORMAL APPLICATION FOR APPROVAL IN TERMS OF SECTIONS 54(1) AND 54(2) OF THE PFMA OF 1999, RE-PROPOSED ESTABLISHMENT OF DENEL ASIA SOC LTD
DATE	:	24 DECEMBER 2015

1. PURPOSE

1.1. To provide Minister with the assessment of Denel's formal application for the approval in terms of Sections 54(1) and 54 (2) of the Public Finance Management Act 1 of 1999 (PFMA) regarding the proposed establishment of Denel Asia SOC Ltd. A copy of the full application dated 10 December 2015 is attached hereto and marked as **Annexure "B"** and

1.2. To request Minister to sign the attached letter to Denel, if she is in agreement with the contents thereof. The letter is attached hereto and marked as **Annexure "A"**.

2. SUMMARY

2.1 Denel on 10 December 2015 applied to the Minister of Public Enterprises ("Minister") seeking approval to establish Denel Asia SOC Limited, in terms of Section 54(1) and 54 (2) of the Public Finance Management Act 1 (PFMA) of 1999.

- Confidential -

2.2 The formal application by Denel dated 10 December 2015 was preceded by an approval by the Minister on 23 November 2015 to grant an in principle approval to Denel to proceed with discussions with VR Laser Asia in preparation for the PFMA application. The Minister directed the Board to consider the following in preparing the PFMA application. Copies of the memorandum and letter with subject "DENEL: PFMA PRE-NOTIFICATION – PROPOSED FORMATION OF DENEL ASIA", IDMS number 185375 dated 16 October 2015 is attached hereto and marked as **Annexure "C"**.

2.2.1 Denel to obtain approval from the Minister of Finance in terms of section 51(g) of the PFMA, towards establishing a new entity.

2.2.2 Denel to submit section 54(2) PFMA application once the Minister of Finance has granted approval in terms of section 51(g).

2.2.3 The Denel section 54(2) PFMA application to include the following among other things:

2.2.3.1 Funding plans, all the transaction documents (including MOU and Cooperation agreements);

2.2.3.2 A comprehensive detailed business case to enable the Minister to express an opinion on the joint venture transaction; and

2.2.3.3 A comprehensive due diligence report on the financial regulatory legal requirements and regulatory laws governing foreign owned entities in Hong Kong;

2.3 Furthermore, the Minister indicated that the Denel Board would need to obtain the Minister of Finance's approval for the transaction in terms of PFMA Section 51 (1) (g), and that the PFMA application to Minister (section 54(2)) should only be submitted once the Minister of Finance has approved the PFMA Section 51 (g) application.

2.4 Therefore, in order for the Department to be in a position to advise the Minister the expectation was that Denel would provide the Minister with the following critical supporting documents on the proposed venture:

2.4.1 The business case, which should provide the logic for the transaction such that Minister is placed in a position to appreciate the value of the transaction to Denel;

2.4.2 The business plan indicating the revenue and expenditure lines movements expected in the short to medium term;

2.4.3 The funding plan, which should show how the venture is to be funded and where the funding sources will emanate from;

2.4.4 Concluded and proposed agreements between Denel and VR Laser. These would include any memoranda of understanding or cooperation that have been are intended to be concluded if the Minister approves the transaction;

2.4.5 A comprehensive due diligence report on the financial, regulatory, and legal requirements in all jurisdictions that will have a direct and indirect interest in the transaction. The preliminary list of jurisdictions that the Department believe would require consideration consists of South Africa, Hong Kong, India, OECD and Malaysia. However, the Asia continental reach of the transaction suggests that there are more jurisdictions that require consideration;

2.5 The Department has reviewed the PFMA application and it is not in a position to advise the Minister on the position she should take with regard to the transaction as:

2.5.1 The detailed information expected, as per paragraph 2.2 to 2.4, has not been provided by Denel;

2.5.2 The following issues will require engagement with Denel executives as the information provided is either not comprehensive or raises further questions:

2.6 The Department wishes to alert the Minister to political ramifications of the transaction as pointed out in the ENS due diligence report (Annexure "B"). The Special Advisors are best positioned to advise the Minister on the report and the adequacy of Denel's response.

3. DISCUSSION

3.1 The Department in reviewing the application first checked whether Denel had addressed the conditions of Minister's approval of the pre-notification in the letter dated 23 November 2015. The analysis reveals the following:

3.1.1 Denel is still awaiting section 51(g) PFMA approval from the Minister of Finance

3.1.2 Funding plans are not included and operational costs are not clear following the two options provided with no clear indication on which is best suited for the proposed joint venture.

3.1.3 The business case has been provided by Denel, however it raises the following lack of detail and rigour in the information provided and has raised further concerns:

3.1.3.1 The entity, Denel Asia is essentially a marketing company seeking to leverage the regional market expertise and knowledge of VR Laser Asia to secure orders in the region, with India a priority market. The reasons provided for opting for the partnership:

3.1.3.1.1 Denel has been out of the India market for over 10 years due to "blacklisting" and therefore does not have adequate recent knowledge of the market nor the necessary networks. This is surprising as Denel has been developing the market for long time as seen by previous success in the market, before it was blacklisted.

3.1.3.1.2 The Made in India demands that Denel partner with an Indian entity in order to be considered for armaments purchase bids. The Department is of the opinion that Denel should instead be directing its efforts to create strategic partnerships with Indian entities.

3.1.3.1.3 Instead of Denel going it alone during the business development stages are inadequate, especially in view of Denel having been successful so far in securing order in what Denel has identified as a key market.

3.1.3.2 The business case provided gives a high level analysis of the Asian market, market drivers and its outlook. This kind of information is freely available and lacks the depth (which would be derived from a professional market study) that what would have been expected considering the risks associated with the venture. The business case submitted is in power point format, the Department would like the document which informed the presentation.

3.1.3.3 The application relies heavily on the opportunities in India though the application is for the entity to represent Denel in the Asian market as a whole. A region of forty nine (49) diverse countries (4.5 billion people and nominal GDP of USD 18.5 trillion) with competing interests. The Departmental analysis suggests that a regional (Mid East, South Asia and Asia Pacific) strategy would be more suitable if the country to country approach was deemed to be suboptimal.

3.1.4 The Department would need an engagement with Denel executives to glean out the gaps identified:

3.1.4.1 The essence of having a marketing company based in Hong Kong despite being questioned in the legal due diligence report. Although Hong Kong is regarded as the Asia's business capital and transport hub across Asia, the due diligence report advices that this may not be the most optimal option.

3.1.4.2 From a tax saving point of view, there could be no benefits for the new entity. In fact there could be tax leakages by doing business with India from Hong Kong as the two jurisdictions do not have double tax agreement jurisdiction

between them. The due diligence report proposes other alternatives such as establishing operations in Dubai which has a dual tax arrangement with India. Denel makes no attempt to consider the proposal from the due diligence.

3.1.4.3 Furthermore, conducting business in India could result in a duplication of plant facilities. The new defence procurement regime in India requires that some of the products and systems acquired should be made in India as part of India's own strategy to grow its defence manufacturing capabilities.

3.1.5 Suitability of VR Laser based on due diligence reports:

3.1.5.1 Due diligence is not adequate as it does not give tangible evidence of VR Laser's networks in the Asia pacific region. The due diligence points to the fact that VR Laser Asia has one shareholder and is a shell company registered in Hong Kong. Only VR Laser South Africa has some level of operational and technical expertise. The concern is that the parent company VR Laser SA itself does not have a significant international footprint and previously received unfavourable publicity in the USA through its another subsidiary which involved bribery which resulted in prosecution. This kind of information does not bode well for the proposed joint venture.

3.1.6 Due diligence on the shareholders of VR Laser Political implications (Annexure B):

3.1.6.1 The due diligence report points to the fact VR Laser SA has a number of high-profiled political exposed persons who will ultimately fund the trading operations of Denel Asia.

3.1.6.2 The fact that VR Laser Asia was established in 2015 and is a dormant company which has no proven global exposure is a huge risk.

3.1.7 The funding for the establishment of Denel Asia is also not well articulated in the PFMA submission. According to the due diligence, VR Laser SA should be the source of funding. However, the company was found to be factually insolvent and it has been funding its operations from loan finance advanced to it by its shareholders. The transaction is not clear on how VR Laser SA plans to fund R100 million it undertakes to put down to establish Denel Asia. In light of this, the due diligence highlights a serious potential risk that the future source of financing of Denel Asia will be sourced from loans held in VR Laser RSA and these loans will be due and payable to politically exposes persons. Therefore in its current form, the transaction structure poses numerous political risk for Minister and the Government as well as Denel.

3.2 Guarantee Conditions:

3.2.1 In terms of the R1.85 billion Government Guaranteed, the approval of any PFMA Section 54 applications requires not only approval by Executive Authority alone but that of the Minister of Finance as well.

3.2.2 It is therefore critical that the Department should first engage the National Treasury regarding this transaction in order to reach consensus which will inform recommendations to Minister and the Minister of Finance.

3.3 Risk Mitigation Plan:

3.3.1 The risk mitigations plans that are proposed against the identified threats to the proposed joint venture are scantly informed by the due diligence reports that the SOC commissioned. It would appear that Denel only did the due diligence reports to fulfil the conditions set by Minister in response to the PFMA pre-notification and not necessarily to strengthen the PFMA submission. The amount of time it took Denel to respond from the pre-notification feedback from Minister suggests that not much time was given to the critical elements that have wider implications.

3.3.2 The Department cannot establish a reason for the urgency of the application. Denel has not fully engaged Minister for political support which could facilitate entry into some of the markets on a standalone basis. Minister has assisted Denel's marketing efforts in a number of countries in the current financial year. Apart from Vietnam in 2014, neither Minister nor Deputy Minister has been called upon to assist in the marketing effort with regard to the Asian market.

4. CONCLUSION:

4.1 The Department remains cautious on the proposed joint venture as a number of issues raised in the letter to the Chairperson are not clearly addressed in the application. These issues, unless they are attended to, pose political and reputational risks to Minister, the Department, Denel and wider Government.

4.2 The Department still has to engage National Treasury on the application. The National Treasury still has to give consideration and decision regarding the joint venture in terms of Section 51(g) of the PFMA.

4.3 Overall, the rationale to enter into a joint venture to establish Denel Asia is not compelling. It is a preponderance to believe that the shareholders of VR Laser SA will put in their money and give Denel majority shareholding.

5. CONSULTATION/PROJECT TEAM

The assessment process has been led by the Manufacturing Enterprises Branch. Inputs from Legal, Governance and Risk (LGR) on cross-cutting matters were received.

6. RECOMMENDATION

It is recommended that the Minister:

5.1 notes the contents of this memorandum;

5.2 sign the attached letter to Denel, if she is in agreement with the contents thereof. The letter is attached hereto and marked as **Annexure "A"**.

DENEL: FORMAL APPLICATION FOR APPROVAL IN TERMS OF SECTIONS 54(1) AND 54(2) OF THE PFMA OF 1999, RE-PROPOSED ESTABLISHMENT OF DENEL ASIA SOC LTD

Memorandum prepared by:	REVIEW AND SUPPORTED:	
MS GLORIA MABINDISA DD: DEFENCE&AEROSPACE DATE: 24/12/2015	MR WEEKEND BANGANE CD: DEFENCE & AEROSPACE DATE: 24 December 2015	P.P MS VUYO TLALE CD: FINANCIAL ANALYSIS DATE: 24/12/2015

REVIEW AND SUPPORTED:

MR KGATHATSO TLHAKUDI
DDG: ME
DATE: 24/12/2015

MS ORATENG MOTSOAI
ACTING DDG: LGR
DATE:

MR MOGOKARE RICHARD SELEKE DIRECTOR-GENERAL DATE:	RECOMMENDED / NOT RECOMMENDED / COMMENTS
MS LYNNE BROWN, MP MINISTER DATE:	APPROVED / NOT APPROVED / COMMENTS
MR BULELANI GRATITUDE MAGWANISHE, MP MINISTER DATE:	NOTED / COMMENTS

Mr Lungisani Daniel Mantsha
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Dear Mr Mantsha

Approval in Terms of the Public Finance Management Act (PFMA): Proposed Establishment of Denel Asia SOC Limited

Your letter dated 11 December 2015 regarding the above subject matter has reference.

Before considering your application, I wish to bring the following issues to your attention:

1. The Department is unable to consider Denel's Section 54 application in the absence of Section 51 (1) (g) approval by Minister of Finance.

2. In terms of the R1.85 billion Government Guarantee, the Minister of Finance must co-approve all Denel's PFMA applications. This then requires the Department to engage and reach consensus with National Treasury (NT) before recommendations could be made to both the Executive Authority and the Minister of Finance;

3. In terms of the final submission made by Denel, the business case is not clear and the Department would like to request Denel to present the business case to the Department and National Treasury.

4. The response to the questions raised in the pre-notification letter were not sufficient due to the following reasons:

    a. Whether the business case for Denel Asia and VR Laser Asia as a partner is solid;

b. The unsuitability of VR Laser as a partner based on the due diligence. The company is technically insolvent;

c. Political considerations or support not exhausted;

d. The primary intention in setting business in Asia seems to be mainly brokering services. The application does not seem to support otherwise;

e. The inadequate financial plan, only financial projections provided.

f. The breakdown of the cost structure as well as alternatives to address the R61 million shortfall. The proposed structure provides two options with no preferred option chosen by Denel;

g. There was a request to furnish studies relating to the choice of partner. No studies undertaken by SOC which indicates the partner is viable; and

h. The reason that proposed partner not included in 2015/16 Corporate Plan is vague. The change in board does not interrupt trajectory of the business. In the formal submission, Denel indicated engagements started in February 2015.

I request that Denel addresses these issues comprehensively so as to allow myself and the Department to make a fully informed decision on this application.

Yours sincerely

MS LYNNE BROWN, MP
MINISTER OF PUBLIC ENTERPRISES
DATE:

cc.: Mr Zwelakhe Ntshepe, Acting Group Chief Executive Officer
Tel: (012) 671-2938 Email: ZwelakheN@denel.co.za / CharleneT@denel.co.za

CONFIDENTIAL

ANNEXURE "KT11"

public enterprises
Department:
Public Enterprises
REPUBLIC OF SOUTH AFRICA

DECISION MEMORANDUM

TO	:	**MS LYNNE BROWN, MP** **MINISTER**
FROM	:	**MR KGATHATSO TLHAKUDI** **DDG: MANUFACTURING ENTERPRISES**
FILE REF	:	**14/1/12/1**
IDMS	:	**186078**
SUBJECT	:	**DENEL: FORMAL APPLICATION FOR APPROVAL IN TERMS OF SECTIONS 54(1) AND 54(2) OF THE PFMA OF 1999, RE-PROPOSED ESTABLISHMENT OF DENEL ASIA SOC LTD**
DATE	:	**24 DECEMBER 2015**

1. PURPOSE

1.1. To provide Minister with the assessment of Denel's formal application for the approval in terms of Sections 54 (1) and 54 (2) of the Public Finance Management Act 1 of 1999 (PFMA) regarding the proposed establishment of Denel Asia SOC Ltd. A copy of the full application dated 10 December 2015 is attached hereto and marked as **Annexure "B"**; and

1.2. To request Minister to sign the attached letter to Denel, if she is in agreement with the contents thereof. The letter is attached hereto and marked as **Annexure "A"**.

2. SUMMARY

2.1 Denel on 10 December 2015 applied to the Minister of Public Enterprises ("Minister") seeking approval to establish Denel Asia SOC Limited, in terms of Section 54 (1) and 54 (2) of the Public Finance Management Act 1 (PFMA) of 1999.

2.2 The formal application by Denel dated 10 December 2015 was preceded by an approval by the Minister on 23 November 2015 to grant an in principle approval to Denel to proceed with discussions with VR Laser Asia in preparation for the PFMA application. The Minister directed the Board to consider the following in preparing the PFMA application. Copies of the memorandum and letter with the subject "DENEL: PFMA PRE-NOTIFICATION – PROPOSED FORMATION OF DENEL ASIA", IDMS number 185375 dated 16 October 2015 is attached hereto and marked as **Annexure "C"**.

2.2.1 Denel to obtain approval from the Minister of Finance in terms of section 51 (g) of the PFMA, towards establishing a new entity.

2.2.2 Denel to submit section 54 (2) PFMA application once the Minister of Finance has granted approval in terms of section 51(g).

2.2.3 The Denel section 54 (2) PFMA application to include the following among other things:

2.2.3.1 Funding plans, all the transaction documents (including MOU and Cooperation agreements);

2.2.3.2 A comprehensive detailed business case to enable the Minister to express an opinion on the joint venture transaction; and

2.2.3.3 A comprehensive due diligence report on the financial regulatory and legal requirements of the applicable jurisdictions.

2.3 Furthermore, the Minister indicated that the Denel Board should only submit the application for her consideration once the Minister of Finance has approved the PFMA Section 51 (1) (g) application.

2.4 Therefore, in order for the Department to be in a position to advise Minister, the expectation was that Denel would provide Minister with the following critical supporting documents on the proposed venture:

2.4.1 The business case, which should provide the logic for the transaction such that Minister is placed in a position to appreciate the value of the transaction to Denel;

2.4.2 The business plan indicating the revenue and expenditure lines movements expected in the short to medium term;

2.4.3 The funding plan, which should show how the venture is to be funded and where the funding sources will emanate from;

2.4.4 Concluded and proposed agreements between Denel and VR Laser. These would include any memoranda of understanding or cooperation that have been intended to be concluded if the Minister approves the transaction;

2.4.5 A comprehensive due diligence report on the financial, regulatory, and legal requirements in all jurisdictions that will have a direct and indirect interest in the transaction. The preliminary list of jurisdictions that the Department believe would require consideration consists of South Africa, Hong Kong, India, OECD and Malaysia. However, the Asia continental reach of the transaction suggests that there are more jurisdictions that require consideration.

2.5 The Department has reviewed the PFMA application and it is not in a position to advise Minister on the position she should take with regard to the transaction as:

2.5.1 The detailed information expected, as per paragraph 2.2 to 2.4, has not been provided by Denel;

2.5.2 The following issues will require engagement with Denel executives as the information provided is either not comprehensive enough or raises further questions.

2.6 The Department wishes to alert Minister to political ramifications of the transaction as pointed out in the ENS due diligence report **(Annexure "B4")**. The Special Advisors are best positioned to advise the Minister on the report and the adequacy of Denel's response.

3. DISCUSSION

3.1 The Department in reviewing the application first checked whether Denel had addressed the conditions of Minister's approval of the pre-notification in the letter dated 23 November 2015. The analysis reveals the following:

3.1.1 Denel is still awaiting section 51 (g) PFMA approval from the Minister of Finance

3.1.2 Funding plans are not included and operational costs are not spelt out. The two transaction options provided do not clearly indicate preference or the best suited option for the proposed joint venture.

3.1.3 The business case has been provided by Denel, the following lack of detail and rigour in the information provided and raised further concerns:

3.1.3.1 The entity, Denel Asia is essentially a marketing company seeking to leverage the regional market expertise and knowledge of VR Laser Asia to secure orders in the region, with India a priority market. The reasons provided for opting for the partnership:

3.1.3.1.1 Denel has been out of the India market for over 10 years due to "blacklisting" and therefore does not have adequate recent knowledge of the market nor the necessary networks. This is surprising as Denel has been developing the market even during the blacklisting period and Denel has successfully entered virgin markets with minimal local partnership, therefore in view of this background and Denel's previous success in this market, it is difficult to understand how it can be said that Denel does not have a good understanding of the market.

3.1.3.1.2 South Africa and India enjoy good diplomatic, political and economic relationships through IBSA and BRICS – would it not have been better to leverage these relationships through DIRCO and Minister of Public Enterprises

before opting for the venture with VR Laser Asia?

3.1.3.1.3 The Made in India demands that Denel partner with an Indian entity in order to be considered for armaments purchase bids. The Department is of the opinion that Denel should instead be directing its efforts towards creating strategic partnerships with Indian entities.

3.1.3.2 The business case provided gives a high level analysis of the Asian market, market drivers and its outlook. This kind of information is freely available and lacks the depth (which would be derived from a professional market study) that what would have been expected considering the risks associated with the venture. The business case submitted is in power point format, the Department would like the document which informed the presentation.

3.1.3.3 The application relies heavily on the opportunities in India, though the application is for the entity to represent Denel in the Asian market as a whole. A region of forty nine (49) diverse countries (4.5 billion people and nominal GDP of USD 18.5 trillion) with competing interests. The Departmental analysis suggests that a regional (Mid East, South Asia and Asia Pacific) strategy would be more suitable if the country to country approach was deemed to be suboptimal.

3.1.4 The Department would need an engagement with Denel executives to glean out the gaps identified:

3.1.4.1 The essence of having a marketing company based in Hong Kong despite this being questioned in the legal due diligence report. Although Hong Kong is regarded as Asia's business capital and transport hub across Asia, the due diligence report advises that this may not be the most optimal option.

3.1.4.2 From a tax saving point of view, there could be no benefits for the new entity. In fact there could be tax leakages by doing business with India from Hong Kong as the two jurisdictions do not have double tax agreement jurisdiction between them.

The due diligence report proposes other alternatives such as establishing operations in Dubai, which has a dual tax arrangement with India. Denel makes no attempt to consider the proposal from the due diligence.

3.1.4.3 Furthermore, conducting business in India investing in plant facilities. The new defence procurement regime in India requires that some of the products and systems acquired should be made in India as part of India's own strategy to grow its defence manufacturing capabilities. Invariably intellectual property will need to be shared with the joint venture – it is not clear how the risk of possible competition with the new venture will be mitigated.

3.1.5 Suitability of VR Laser based on due diligence reports:

3.1.5.1 Due diligence is not adequate as it does not give tangible evidence of VR Laser's networks in the Asia pacific region. The due diligence points to the fact that VR Laser Asia has one shareholder and is a shell company registered in Hong Kong. Only VR Laser South Africa has some level of operational and technical expertise. The concern is that the parent company VR Laser SA itself does not have a significant international footprint and previously received unfavourable publicity in the USA through one of its subsidiaries which involved bribery, which resulted in prosecution; especially since Denel has just untangled itself of a blacklisting in India due to questionable marketing arrangements.

3.1.6 Due diligence on the shareholders of VR Laser Political implications **(Annexure B4)**:

3.1.6.1 The due diligence report points to the fact VR Laser SA has a number of high-profiled political exposed persons who will ultimately fund the trading operations of Denel Asia; and

3.1.6.2 The fact that VR Laser Asia was established in 2015 and is a dormant company which has no proven global exposure is a huge risk.

3.1.7 The funding for the establishment of Denel Asia is also not well articulated in the PFMA submission. According to the due diligence, VR Laser SA should be the source of funding. However, the company was found to be factually insolvent and it has been funding its operations from loan finance advanced to it by its shareholders. The transaction is not clear on how VR Laser SA plans to fund R100 million it undertakes to put down to establish Denel Asia. In light of this, the due diligence highlights a serious potential risk that the future source of financing of Denel Asia will be sourced from loans held in VR Laser RSA and these loans will be due and payable to politically exposed persons. Therefore in its current form, the transaction structure poses numerous political risks for Minister and the Government as well as Denel.

3.2 Guarantee Conditions:

3.2.1 In terms of the R1.85 billion Government Guaranteed, the approval of any PFMA Section 54 applications requires not only approval by Executive Authority alone, but that of the Minister of Finance as well.

3.2.2 It is therefore critical that the Department should first engage the National Treasury regarding this transaction in order to reach consensus which will inform recommendations to Minister and the Minister of Finance.

3.3 Risk Mitigation Plan:

3.3.1 The risk mitigations plans that are proposed against the identified threats to the proposed joint venture, as detailed in PFMA application are scantly informed by the due diligence reports that the SOC commissioned, are not provided. It would appear that Denel only did the due diligence reports to fulfil the conditions set by Minister in response to the PFMA pre-notification and not necessarily to strengthen the PFMA submission. The amount of time it took Denel to respond from the pre-notification feedback from Minister suggests that not much time was given to the critical elements that have wider implications.

3.3.2 The Department cannot establish a reason for the urgency of the application. Denel has not fully engaged Minister for political support which could facilitate entry into some of the markets on a standalone basis. Minister has assisted Denel's marketing efforts in a number of

countries in the current financial year. Apart from Vietnam in 2014, neither Minister nor Deputy Minister has been called upon to assist in the marketing effort with regard to the Asian market.

4. CONCLUSION:

4.1 The Department remains cautious on the proposed joint venture as a number of issues raised in the letter to the Chairperson are not clearly addressed in the application. These issues, unless they are attended to, pose political and reputational risks to Minister, the Department, Denel and wider Government.

4.2 The Department still has to engage National Treasury on the application. The National Treasury still has to give consideration and decision regarding the joint venture in terms of Section 51 (g) of the PFMA.

4.3 Overall, the rationale to enter into a joint venture to establish Denel Asia is not compelling. It is a preponderance to believe that the shareholders of VR Laser SA will put in their money and give Denel majority shareholding.

5. CONSULTATION/PROJECT TEAM

The assessment process has been led by the Manufacturing Enterprises Branch. Inputs from Legal, Governance and Risk (LGR) on cross-cutting matters were received.

6. RECOMMENDATION

It is recommended that the Minister:

5.1 notes the contents of this memorandum; and

5.2 sign the attached letter to Denel, if she is in agreement with the contents thereof. The letter is attached hereto and marked as **Annexure "A"**.

DENEL: FORMAL APPLICATION FOR APPROVAL IN TERMS OF SECTIONS 54(1) AND 54(2) OF THE PFMA OF 1999, RE-PROPOSED ESTABLISHMENT OF DENEL ASIA SOC LTD

Memorandum prepared by:

MS GLORIA MABINDISA
DD: DEFENCE&AEROSPACE
DATE: 24/12/2015

REVIEW AND SUPPORTED:

MR WEEKEND BANGANE
CD: DEFENCE & AEROSPACE
DATE: 24 December 2015

REVIEW AND SUPPORTED:

P.P

MS VUYO TLALE
CD: FINANCIAL ANALYSIS
DATE: 24/12/2015

REVIEW AND SUPPORTED:

MR KGATHATSO TLHAKUDI
DDG: ME
DATE: 24/12/2015

MS ORATENG MOTSOAI
ACTING DDG: LGR
DATE: 06/01/2015

MR MOOOKARE RICHARD SELEKE
DIRECTOR-GENERAL
DATE: 13/01/2016

RECOMMENDED / NOT RECOMMENDED / COMMENTS

Discussed the report with Programme Manager Please return to the Branch. Keep reports

83
84

APPROVED / NOT APPROVED / COMMENTS

MS LYNNE BROWN, MP
MINISTER
DATE:

NOTED / COMMENTS

MR BULELANI GRATITUDE MAGWANISHE, MP
MINISTER
DATE:

ANNEXURE "KT12"

MINISTRY
PUBLIC ENTERPRISES
REPUBLIC OF SOUTH AFRICA

Private Bag X15, Hatfield, 0028 Tel: (012) 431 1118/1150 Fax: (012) 431 1039
Private Bag X9079, CAPE TOWN, 8000 Tel: (021) 461 6376/7/469 6760 Fax: (021) 465 2381/461 1741

Mr Lugisani Daniel Mantsha
Chairperson
Denel SOC Limited
P.O Box 8322
Centurion
0046

Tel: (011) 781 0099 / (012) 671 2896
Email: dan@lugisanimantshaattorneys.co.za / info@lugisanimantshaattorneys.co.za
yvonne@lugisanimantshaattorneys.co.za

Dear Mr Mantsha

Re: Establishment of Denel Asia in Terms of Section 54 And 51(1)(g) of the Public Finance Management Act ("PFMA")

Your letter dated 28 June 2016 regarding the above subject matter has reference.

I am now convinced that Denel did make adequate consultation with the Department and the National Treasury and followed the necessary steps required by the PFMA when undertaking a transaction of this nature.

My considered view is that both the DPE and National Treasury were slow in reviewing the application despite Denel indicating the urgency of the application. Both the pre-notification and the actual full PFMA applications emphasised the urgency of the transaction. The least both Departments could have done was to ask Denel for additional time to review the transaction within the prescribed PFMA timeframe.

In the meantime, I have proposed a bilateral engagement with the Minister of Finance in order to in order to properly conclude this to undo the adverse impact that might have been caused by the negative public exchanges concerning this matter.

I trust that you find the above reasonable.

Kind Regards

MS LYNNE BROWN, MP
MINISTER OF PUBLIC ENTERPRISES
DATE: 15/07/2016

Mr Zwelakhe Ntshepe, Acting Group Chief Executive Officer
Tel: (012) 671-2938
Email: zwelakhen@denel.co.za / charlenet@denel.co.za

COMMISSION OF INQUIRY INTO STATE CAPTURE

Masenya Selatswa

From:	Masenya Selatswa
Sent:	Thursday, July 21, 2016 2:12 PM
To:	'dan@lugisanimantshaattorneys.co.za'; 'info@lugisanimantshaattorneys.co.za'; 'Yvonne@lungisanimantshattorneys.co.za'
Cc:	'zwelakhen@denel.co.za'; Keromamang Mhlongo; Nkuna Freedom; Weekend Bangane; Vuyo Tlale; Orateng Motsoai
Subject:	Re: Establishment of Denel Asia in terms of Section 54 and 51(1)(g) of the PFMA
Attachments:	SMinistry16072113521.pdf

Good day Chair

On behalf of Minister Lynne Brown the Minister of Public Enterprises, kindly find attached letter on the above mentioned subject for your attention.

Please acknowledge receipt.

Thank you,

Kind regards,

Mr Selatswa Masenya
Registry
Ministry of Public Enterprises

+27 (0)12 431 1158 | +27 (0) 21 469 6760 +27 (0) 12 431 1039 | ministry.registry@dpe.gov.za

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Mr Pravin Gordhan, MP
Minister of Finance
National Treasury
Pretoria
0001

Tel: 012 315 5070/5799
Fax: 012 326 5445
Email: minreg@treasury.gov.za

Dear Colleague

Re: Establishment of Denel Asia in Terms of Section 54 And 51(1)(g) of the Public Finance Management Act ("PFMA")

Your letter of 10 June 2016 regarding the above subject matter has reference.

Thank you for updating me on the engagements that your department has been having with Denel. Ideally, I would have preferred that such engagement be directed through the Director-General of my department. It is my considered view that some of the challenges that you alluded to in your letter could have been avoided if these protocols had been followed.

In order to respond to your letter, I met with the Denel Board on 23 June 2016 to obtain their response to the concerns that you raised regarding the process followed by Denel in the establishment of Denel Asia, as well as the South African Reserve Bank ("SARB") application. The summary of the discussion is as follows:

1. The Board reiterated that it is of the view that it had followed all the necessary steps required by the PFMA when undertaking a transaction of this nature. This is formally captured in the letter of 28 June 2016 the Denel Board has written to the two of us.

2. With regard to the interpretation of sections 51(1)g and 54(3) of the PFMA, The Board explained its interpretation and indicated that this is supported by a legal advice.

3. Furthermore, the Board indicated that the SOC operates in a highly competitive industry which is extremely time sensitive which could be assisted by a more agile support from the shareholder and other authorities of

government to enable them to take advantage of business opportunities that emerge from time to time.

4. With regard to the SARB application, the application was completely aligned to the PFMA application, as Denel had indicated that it intends to establish further joint ventures with India being a key market. The entity reiterated that Denel India does not as yet exist, and that such an application shall be submitted at an appropriate time. The approval by SARB recognised this requirement as it stated: *"...thank you for the information furnished and advise that the Financial Surveillance Department should, from an exchange control point of view and provided that the matter has been cleared with all appropriate authorities, have no objection to the applicants acquiring 51% interest in Denel Asia, domiciled in Hong Kong, and a 49% interest in Denel India, domiciled in India..."* Therefore, it was and it remains Denel's intention to ensure that it complies with all legal requirements in conducting its business activities in both the local and overseas markets.

It was apparent during the engagement that the conduct of my department and yours in managing PFMA applications can be improved upon, with Denel Asia as the case in point:

1. The time it took for the departments in responding to the PFMA application, despite the holiday period impact, could have been better. The application was received on 11 December 2015, and the first formal response that Denel received from either department on their application was on 5 February 2016 from the NT Office of Chief Procurement Officer, which communication was not addressing the substance of the application.

2. Denel had sent a pre-notification to both departments on 29 October 2015, which was only responded to by the Department of Public Enterprises on 23 November 2015 indicating approval to the SOC to proceed with the intent to set up the Denel Asia subsidiary.

3. In both the pre-notification and the PFMA application, Denel had emphasised the urgency of the transaction. The least both Departments could have done was to ask the entity for additional time to review the transaction within the prescribed PFMA timeframe.

4. I further understand that our departments (NT team was led by Mr Mogorosi Lebethe) and Denel executives had a discussion on the application on 27 January 2016, which provided both departments with an opportunity to seek clarity on any issues relating to the application.

I must indicate at this point that I am inclined to support the position taken by Denel on this matter. I, however propose, in order to properly conclude this matter, a bilateral engagement between us.

We should jointly seek to reconcile the relationship between our respective departments and Denel and undo the adverse impact that might have been caused by the negative public media exchanges.

I trust that you find my suggestion to close on this matter reasonable.

Yours Sincerely

MS LYNNE BROWN, MP
MINISTER OF PUBLIC ENTERPRISES
DATE: 15/07/2016

COMMISSION OF INQUIRY INTO STATE CAPTURE

Masenya Selatswa

From: Masenya Selatswa
Sent: Thursday, July 21, 2016 2:38 PM
To: 'Ministry Registry'
Cc: Weekend Bangane; Vuyo Tlale; Orateng Motsoai; Keromamang Mhlongo; Nkuna Freedom
Subject: Re: Establishment of Denel Asia in terms of Section 54 and 51 (1)(g) of the PFMA
Attachments: SMinistry16072113520.pdf

Dear Ministry Registry

On behalf of Minister Lynne Brown the Minister of Public Enterprises, kindly find attached letter on the above mentioned subject for the attention of Minister Pravin Gordhan, Minister of Finance.

Please acknowledge receipt.

Thank you,

Kind regards,

Mr Selatswa Masenya
Registry
Ministry of Public Enterprises

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COMMISSION OF INQUIRY INTO STATE CAPTURE

ANNEXURE “KT13”

public enterprises
Department:
Public Enterprises
REPUBLIC OF SOUTH AFRICA

Suite 301, Infotech Building1090 Acadia Street Hatfield, 0083 Private Bag X15 Hatfield 0028
Ref.: Mr Kgathatso Tlhakudi Tel: 012 431 1282 Email: Kgathatso.Tlhakudi@dpe.gov.za

Mr Lungisa Fuzile
Director-General
National Treasury
Private Bag
0001

T: 012 315 5904
Email: Felicitas.Mogase@treasury.gov.za

Dear Mr Fuzile

Finalisation of Denel Asia Joint Venture Public Finance Management Act (PFMA) Application

The above matter and your letter dated 02 September 2016, of which a copy is attached hereto as Annexure "1", refers.

Denel has, from the onset, expressly indicated the urgency of the application. Time and timing are some of the critical factors in the competitive global defence market. The delays in providing feedback by both our departments are putting the company on a disadvantage. The Asia-Pacific defence market relies strongly on partnerships and strategic alliances with domicile and regional entities.

Despite registering the Denel Asia on 29 January 2016, Denel Asia is yet to be a trading entity due to the outstanding formal response from the Minister of Finance in terms of section 51(1)(g) of the PFMA. Since registration of the joint venture, Denel risks to lose out on a number of potential opportunities and this will continue as long as this matter remains unresolved. The DPE has accepted that, in terms of section 54(3) of the PFMA, Denel is within its right to consider the application as "deemed" approved after the lapse of the stipulated thirty (30) day period. As such, the Minister of Public Enterprises and the Department considers this matter regularised and closed from our perspective.

I wish to bring to your attention that further delays in finalising the section 51(1)(g) approval would, in all likelihood, see Denel being crowded out of the Pacific-Asia market; given the aggressive business model of the large

global original equipment manufacturers (OEMs) in relation to that market. In light of this, I wish to request the National Treasury to provide the DPE and Denel with reasonable timelines on when a formal response in terms of section 51(1)(g) of the PFMA will be provided.

I wish also to suggest that yourself and I meet to engage further on this and other matters related to Denel. I share your concern, as expressed in your letter dated 2 September 2016, about the potential adverse impact the public spats over the Denel Asia matter. Our meeting could be used to reach an alignment and formulate a communication protocol around Denel matters. This would be fundamental in creating certainty among our different stakeholders about coordination between our two departments, thereby help reverse the negative public discourse that is beginning to take root. Ideally, the meeting should happen before the proposed meeting between our two Ministers and our appearance before Parliament over the Denel Asia matter.

I trust you find my both request and proposal reasonable.

Yours sincerely

Mr Mogokare Richard Seleke
Director-General

Date: 20 | 09 | 2016

Cc: Ms Lynne Brown, MP
Minister of Public Enterprises
Email: Nonhlanhla.Mokoena@dpe.gov.za

Mr Pravin Gordhan, MP
Minister of Finance
Email: minreg@treasury.gov.za

national treasury
Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

Mr M R Seleke
Director-General
Department of Public Enterprises
Private Bag X15
Hatfield
0028

Dear DG Seleke

REPORTED DENEL REACTION TO ARTICLES THAT NATIONAL TREASURY TAKING DENEL TO COURT

Our discussion of 30 August 2016 and your letter of 9 May 2016 have reference.

On 29 August 2016, the Sunday Times Article reported in its article entitled "Treasury 'taking Denel to court' to halt Gupta deal" that National Treasury had sent letters to Denel demanding that it dissolve the Denel Asia joint venture or face legal action. Pursuant to our discussion of 30 August 2016, the National Treasury has undertaken a due diligence and there is no record of any such letter. I have written to Denel to have the company provide us with a copy of the letter, should they have such a letter in their possession, or provide an explanation for their press statement, in the event that they do not. You have been copied on this correspondence.

More fundamentally, as we agreed, it is unacceptable that any state-owned entity launch a public attack (and in this case, a vicious attack) on any Minister. Not only is such an attack out of line with the spirit of cooperative governance and good faith, but in transgression of the President's statement of 11 December 2015 that "no state-owned entity will dictate to Government how it should be assisted". All state-owned companies (SOCs) must be accountable. Moreover, they must seek to work together with other parts of government to resolve differences constructively rather than dealing with such matters legally or through the media.

Denel currently has in place a R1.85 billion government guarantee which has been fully utilised to raise debt financing. When government has issued guarantees to SOCs, conditions were attached precisely with the aim of providing government with the tools to strengthen its oversight and manage the fiscal risks that can arise from such guarantees. The way in which a number of the SOCs, including Denel, are conducting themselves, demonstrating poor governance and taking up matters in the press rather than trying to resolve these matters in mutual trust and good faith directly with government, is damaging to the SOC, government and public sector in general, undermining confidence and contributing directly to an increase in fiscal risk. In line with

our discussion, I would like to propose that we meet during the course of next week to look at how the entities in the Department of Public Enterprises (DPE) portfolio can be held to account in line with the legislative provisions.

I have noted that in your letter of 9 May 2016, you indicated that any information requested from the SOCs within the DPE portfolio must be channeled through your office. National Treasury strives to ensure that DPE is involved in any interactions it has with the entities for which you are the Executive Authority, as we have done in the most recent correspondence. We do so even though the National Treasury does have original powers to interact with all organs of state over fiscal and financial matters. However, from time to time, circumstances do require direct engagement with the SOCs which is also contemplated and provided for in the PFMA.

I would like to also bring you attention to the legal advice that National Treasury has received with respect to the Denel Asia transaction, as was detail in correspondence from the Minister of Finance to your Minister dated 10 June 2016 and 1 August 2016, Specifically:

- The conditions attached in terms of Section 70(1) of the PFMA to the R1.85 billion guarantee that has been issued to Denel included a requirement that "Any transactions undertaken in terms of Section 54 of the PFMA are subject to approval of the Minister [of Finance] as well as the Minister of Public Enterprises". The conditions create a distinct legal obligation on Denel to obtain both Ministers' approval prior to entering into the types of transactions envisaged in Section 54(2) of the PFMA. Moreover, the deeming provision contained in Section 54(3) of the PFMA is not imported.
- In terms of Section 51(1)(g), a reasonable period could not be assumed to be the 30-day period envisaged in Section 54 of the PFMA. and that the period that constitutes a reasonable time depends on the circumstances of each case, which in this case included, amongst others, the following:
  - On 10 December 2015, a new Minister was appointed;
  - By 13 December 2015, that Minister was replaced by another;
  - As a result thereof, the markets were affected and the Minister and National Treasury had to concentrate its efforts on restoring market confidence;
  - The National Treasury closed during the Christmas and New Year period and its staff were on holiday; and
  - January and February are the busiest months for the Minister and National Treasury because of the budget preparations.
- There is no assumption of deemed approval incorporated into Section 51 as is provided for in Section 54: a decision from the National Treasury is required prior to the formal establishment of a company.

Based on this legal advice, contrary to Denel's assertion that the approval process has been concluded as allowed for by the PFMA, decisions are still required from both Ministers. I have noted that your Minister has indicated that she has not as yet granted approval for the transaction. Similarly the Minister of Finance has also not given his approval. It would assist if you can furnish us with any correspondence from your Minister to Denel outlining that she has not approved the Denel Asia transaction.

National Treasury has proceeded with evaluating the application that had been made by Denel. Both the original submission and the supplementary information provided by Denel relating to the establishment of Denel Asia has been carefully reviewed. A number of issues have been

identified which have the potential to negatively impact on Denel. As I have already highlighted, Denel currently has in place a R1.85 billion government guarantee. Several rating agencies have highlighted government's contingent liability exposure to state owned companies as a risk for the sovereign credit rating. A call or an increase in the exposure could negatively impact on the sovereign rating and could have negative repercussions for government's capacity to deliver on its objectives to promote growth, development and job creation.

I trust that you will find the above in order.

Kind regards

LUNGISA FUZILE
Acting **DIRECTOR-GENERAL: NATIONAL TREASURY**
Date: 2/9/2014

COMMISSION OF INQUIRY INTO STATE CAPTURE

Sarah Setshedi

From:	DGOffice@dpe.gov.za
Sent:	21 September 2016 05:15 PM
To:	'Felicitas Mogase'
Cc:	Charmaine Yssel; Matsietsi Mokholo; Kgathatso Tlhakudi; DGOffice@dpe.gov.za; Nonhlanhla Mokoena; 'minreg@treasury.gov.za'
Subject:	FINALISATION OF DENEL ASIA JOINT VENTURE PUBLIC FINANCE MANAGEMENT ACT (PFMA) APPLICATION
Attachments:	Scanned from a Xerox Multifunction Printer.pdf; Scanned from a Xerox Multifunction Printer.pdf

Dear Felicitas,

On behalf of the Director-General of Public Enterprises, Mr. Mogokare Richard Seleke please find the above-mentioned letter with attachment for the attention of Mr Lungisa Fuzile

Please acknowledge receipt

Kind regards

Sarah Setshedi |
Office of the Director General
+27 (0)12 431 1043 | +27 (0)12 431 1040 sarah.setshedi@dpe.gov.za
1090 Arcadia Street | InfoTech Building | Hatfield | Pretoria | Switchboard: +27 12 431 1000

public enterprises
Department:
Public Enterprises
REPUBLIC OF SOUTH AFRICA

Click on the following link to view DPE website & email disclaimer http://www.dpe.gov.za/home.asp?id=10
Click on the following link to view directions to DPE http://www.dpe.gov.za/home.asp?id=1053

ANNEXURE “KT14”

KT 14 replaces KT 14

public enterprises
Department:
Public Enterprises
REPUBLIC OF SOUTH AFRICA

DECISION MEMORANDUM

TO	:	**MS LYNNE BROWN, MP** **MINISTER**
FROM	:	**MR KGATHATSO TLHAKUDI** **DDG: MANUFACTURING ENTERPRISES**
FILE REF	:	**14/1/12/1**
IDMS	:	**186078**
SUBJECT	:	**DENEL: FORMAL APPLICATION FOR APPROVAL IN TERMS OF SECTIONS 54(1) AND 54(2) OF THE PFMA OF 1999, RE-PROPOSED ESTABLISHMENT OF DENEL ASIA SOC LTD**
DATE	:	**24 DECEMBER 2015**

1. PURPOSE

1.1. To provide Minister with the assessment of Denel's formal application for the approval in terms of Sections 54 (1) and 54 (2) of the Public Finance Management Act 1 of 1999 (PFMA) regarding the proposed establishment of Denel Asia SOC Ltd. A copy of the full application dated 10 December 2015 is attached hereto and marked as **Annexure "B"**; and

1.2. To request Minister to sign the attached letter to Denel, if she is in agreement with the contents thereof. The letter is attached hereto and marked as **Annexure "A"**.

2. SUMMARY

2.1 Denel on 10 December 2015 applied to the Minister of Public Enterprises ("Minister") seeking approval to establish Denel Asia SOC Limited, in terms of Section 54 (1) and 54 (2) of the Public Finance Management Act 1 (PFMA) of 1999.

2.2 The formal application by Denel dated 10 December 2015 was preceded by an approval by the Minister on 23 November 2015 to grant an in-principle approval to Denel to proceed with discussions with VR Laser Asia in preparation for the PFMA application.

2.3 The Minister directed the Board to consider the following in preparing the PFMA application. Copies of the memorandum and letter with the subject "DENEL: PFMA PRE-NOTIFICATION – PROPOSED FORMATION OF DENEL ASIA", IDMS number 185375 dated 16 October 2015 is attached hereto and marked as **Annexure "C"**.

2.3.1 The Denel section 54 (2) PFMA application to include the following among other things:

2.3.1.1 Funding plans, all the transaction documents (including MOU and Cooperation agreements);

2.3.1.2 A comprehensive detailed business case to enable the Minister to express an opinion on the joint venture transaction;

2.3.1.3 A comprehensive due diligence report on the financial regulatory and legal requirements of the applicable jurisdictions; and.

2.4 Denel has not fully complied with the conditions of the PFMA Pre-Notification approval referred to in Paragraph 2.3.

2.5 Denel has performed a due diligence on VR Laser Asia through Edward Nathan Sonnenburg (ENS) as directed by the Minister. The due diligence report is attached as **(Annexure "D")**. Denel has indicated that adequate measures will be put in place to manage the risks identified.

3. DISCUSSION

3.1 Denel has motivated for the partnership on the basis that it has been out of the India market for over 10 years due to "blacklisting" and therefore does not have adequate recent knowledge of the market nor the necessary networks. According to Denel, VR Laser possesses the valuable expertise and presence in the market, which Denel does not have.

3.2 South Africa and India enjoy good diplomatic, political and economic relationships through IBSA and BRICS, including continental Asia and Asia Pacific region through other multilateral forums. Denel should be encouraged to leverage these relationships in view of armaments sales being on the main government-to-government transactions. In this regard, the Ministers of Public Enterprises and International Relations and Cooperation good offices should be explored.

3.3 VR Laser Asia has pledged to capitalise Denel Asia with R100 million. Denel will need to secure the funding at establishment of the Denel Asia entity. The ENS due diligence suggests that VR Laser Asia may have difficulties in raising the funds as the parent company VR Laser RSA has been kept afloat by shareholder loans.

3.4 The 2012 recapitalisation of Denel and approval of the turnaround plan, gave the Minister of Finance cosignatory powers over the PFMA Section 54 applications of Denel. Therefore, the Minister of Finance has to concur with the Minister of Public Enterprises, who is the Executive Authority of Denel, on the establishment of Denel Asia.

4. CONCLUSION

4.1. The Department is of the opinion that there is an opportunity to mature the business case and that Denel as it concludes local production agreements should use local partner(s) knowledge to enhance the business case. The Department concurs with Denel that a significant presence in the Continental Asia and Asia Pacific is critical to successful placement of product in the region.

4.2. The SOC will need to ensure that adequate measures are put in place to mitigate against the risks identified. Current performance reporting channels should be used to keep the Minister appraised on the

5. CONSULTATION/PROJECT TEAM

The assessment process has been led by the Manufacturing Enterprises Branch. Inputs from Legal, Governance and Risk (LGR) on cross-cutting matters were received.

6. RECOMMENDATIONS

It is recommended that the Minister:

5.1 Notes the contents of this memorandum its annexures;

5.2 Grants Denel conditional approval to enter into a strategic relationship with VR Laser to establish Denel Asia subject to the fulfilment of the following conditions:

5.2.1 Denel secures an irrevocable commitment by VR Laser to make all the required funding to establish and run the affairs of Denel Asia;

5.2.2 Denel should implement a comprehensive risk mitigation plan to address the risks raised in the due diligence reports and report progress on the effectiveness of the mitigation actions in the agreed performance reports; and

5.2.3 For the transaction, Denel has to receive the following approval from the Minister of Finance: Sections 51(1) (g) and 54(2)(a) as required by R1.85 billion government guarantee conditions;

5.3 Signs the attached letter to Denel, if she is in agreement with the contents thereof. The letter is attached hereto and marked as **Annexure "A"**.

DENEL: FORMAL APPLICATION FOR APPROVAL IN TERMS OF SECTIONS 54(1) AND 54(2) OF THE PFMA OF 1999, RE-PROPOSED ESTABLISHMENT OF DENEL ASIA SOC LTD

MEMORANDUM PREPARED BY:

KGATHATSO TLHAKUDI
DEPUTY DIRECTOR GENERAL
DATE:

REVIEW AND SUPPORTED:

MATSIETSI MOKHOLO
DEPUTY DIRECTOR GENERAL
DATE:

MR MOGOKARE RICHARD SELEKE DIRECTOR-GENERAL DATE:	RECOMMENDED / NOT RECOMMENDED / COMMENTS
MS LYNNE BROWN, MP MINISTER DATE:	APPROVED / NOT APPROVED / COMMENTS
MR BULELANI GRATITUDE MAGWANISHE, MP MINISTER DATE:	NOTED / COMMENTS

Mr Lungisani Daniel Mantsha
Chairperson
Denel SOC Limited
P O Box 8322
Centurion
0046

Tel: (011) 781 0099 / (012) 671 2896
Email: Dan@lungisanimanthsaattorneys.co.za / Fortunel@denel.co.za /
Yvonne@lungisanimanthsattorneys.co.za /

Dear Mr Mantsha

Approval in Terms of the Public Finance Management Act (PFMA): Proposed Establishment of Denel Asia SOC Limited

Your letter dated 11 December 2015 regarding the above subject matter has reference.

On consideration of your application, the Department grants Denel conditional approval to enter into a strategic relationship with VR Laser to establish Denel Asia subject to the fulfilment of the following conditions:

1. Denel secures an irrevocable commitment by VR Laser to make all the required funding to establish and run the affairs of Denel Asia;

2. Denel should implement a comprehensive risk mitigation plan to address the risks raised in the due diligence reports and report on the effectiveness of the mitigation action in the agreed performance reports; and

I would also like to highlight the importance of duty and care to be exercised in transactions of this nature as stipulated in the PFMA's Chapter 5, part 2: "Responsibilities of Accounting Offices".

Yours sincerely

MS LYNNE BROWN, MP
MINISTER OF PUBLIC ENTERPRISES
DATE:

cc.: Mr Zwelakhe Ntshepe, Acting Group Chief Executive Officer
Tel: (012) 671-2938 Email: ZwelakheN@denel.co.za / CharleneT@denel.co.za

CONFIDENTIAL

ANNEXURE “KT15”

Ngidi Business Advisory
ADVISORY•FORENSICS•TAX

Denel SOC Ltd

Independent Review of the process followed in concluding the Memorandum of Agreement between Denel SOC Ltd and VR Laser Services (Pty) Ltd



Ngidi Business Advisory
ADVISORY•FORENSICS•TAX

Draft Report

Strictly private and confidential

March 2018

Ngidi Business Advisory

Strictly private and confidential

Privileged

Mr T Kleynhans
Group Executive: Strategy
Denel SOC Ltd
Nellmapius Drive
Centurion
0046

09 March 2018

Dear Mr Kleynhans,

Independent Review of the Process Followed in Concluding the Memorandum of Agreement between Denel SOC Ltd and VR Laser Servicers (Pty) Ltd

1. In accordance with our letter of engagement dated 21 July 2017, you required us to conduct an independent review into the process followed in concluding the Memorandum of Agreement between Denel SOC Ltd ("Denel") and VR Laser Services (Pty) Ltd ("VR Laser").

2. Pursuant to the aforesaid mandate, we now have pleasure in presenting our draft report. This report is provided to you as a draft in order to afford you an opportunity to comment on our findings to date and to provide us with any outstanding information to enable us to finalise our report.

3. Should you have any comments, please do not hesitate to contact me on 012 752 7655 or 071 889 2245 or vusmuzim@ngid.co.za.

Yours faithfully,



Vusmuzi Masilela CA (SA)
Managing Director & Head of Forensics

210 Amarand Avenue, Cnr January Masilela & Amarand, Menlyn Maine, Pretoria, 0181, Tel: +27 (0) 12 752 7655
Directors and Associate Directors: Vusmuzi Masilela CA (SA), Solomon Sikhosana CA (SA), Jabu Masilela BCom(Hons)
Company registration number: 2015/166965/07

Ngidi Business Advisory

Denel SOC Ltd

Draft Report: Independent Review of the Process Followed in Concluding the Memorandum of Agreement between Denel SOC Ltd and VR Laser Servicers (Pty) Ltd

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List of Annexure

1	Copy of our letter of engagement dated 21 July 2017
2	Copy of relevant extracts from the Public Finance Management Act, 1 of 1999
3	Copy of the relevant extract from the Constitution of the Republic of South Africa, Act 108 of 1996
4	Copy of Treasury Regulations 16A6.4
5	Copy of the relevant extract from the Gauteng Provincial Government Supply Chain management policy model
6	Copy of Denel SOC LTD Procurement Policy
7	Copy of the unsigned Denel SOC LTD Delegation of Authority
8	Copy of an email dated 17 July 2014 addressed by Mr Wessels to Mr Burger titled "*DLS recent request to contract VR Laser*"
9	Copy of an email dated 18 July 2014 addressed by Mr Burger to RE_EXCO1 titled "*Round robin on VR Laser*"
10	Copy of an email dated 18 July 2014 addressed by Mr Burger to Mr Wessels and Mr Mhlontlo and copied to Mr Saloojee, Ms Tribelhorn and Mr Ntshepe titled "*DLS recent request to contract VR Laser*"
11	Copy of a submission dated 15 October 2014 addressed by DLS EXCO to Group EXCO titled "*Industrialisation and Production of 183 Vehicle Platform Hulls at VR Laser*"
12	Copy of a report referenced "*D117051_0*" and dated 03 March 2014 that indicates that it was issued by Patria
13	Mr Mlambo's interview notes
14	Copy of an email dated 10 March 2015 addressed by Mr Drevin to Ms Malahlela titled "*Motivation for single source supply of Hoefyster Turret armour steel fabrications and components.docx*"
15	Copy of an unsigned memorandum dated 9 March 2015 addressed by Mr

	Drevin to the Executive Manager: Supply Chain titled "*Supplier for Hoefyster turret armour steel components and fabrication*"
16	Mr Burger's interview notes
17	Mr Teubes' interview notes
18	Mr Drevin's interview notes
19	Ms Govender's interview notes
20	Copy of an email dated 11 March 2015 addressed by Mr Teubes to Ms Malahlela titled "*Motivation for single source supply of Hoefyster Turret armour steel fabrications and components.docx*
21	Copy of an email dated 11 March 2015 addressed by Ms Malahlela to Mr Teubes in response to his email
22	Copy of an email dated 11 March 2015 from Mr Teubes responding to Ms Malahlela
23	Copy of an email dated 11 March 2015 from Ms Malahlela responding to Mr Teubes
24	Copy of an email dated 12 March 2015 addressed by Ms Malahlela to Mr Teubes titled "*GROUP CEO Submission*"
25	Copy of an unsigned submission dated March 2015 (actual date not specified) titled "*GROUP CHIEF EXECUTIVE OFFICER'S SUPPLY CHAIN SUBMISSION*"
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27	Copy of an email dated 20 March 2015 addressed by Mr Teubes to Ms Malahlela
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29	Copy of the recommendation made by the UN regarding the use of Proprietary Limited

30	Copy of an email dated 23 March 2015 addressed by Ms Malahlela to Mr Teubes in response to his email dated 20 March 2015
31	Copy of a letter dated 16 April 2015 addressed by Mr Burger to Mr Salojee titled "*MOU WITH VR LASERFOR SUPPLY OF FABRICATED STRUCTURES*"
32	Copy of a letter dated 22 April 2015 addressed by Mr Burger to Mr Salojee also titled "*MOU WITH VR LASERFOR SUPPLY OF FABRICATED STRUCTURES*"
33	Copy of unsigned minutes of special DLS EXCO meeting held on 3 March 2015
34	Copy of a Memorandum of Agreement entered into between VR Laser and Denel
35	Copy of an email dated 05 June 2015 addressed by Ms Govender to EXCO and copied to Ms Malahlela titled "*VR LASER – APPROVAL FROM DCO AS SINGLE SOURCE SUPPLIER*"
36	Copy of the minutes of DLS EXCO meeting held on 07 August 2015
37	Copy of minutes of DLS Special Procurement EXCO meeting held on 29 October 2015
38	Copy of a memorandum dated 29 October 2015 addressed by Ms Malahlela to Mr Mlambo titled "*Conflict between policy and signed MOU*"
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40	Copy of DLS EXCO minutes of meeting held on 21 April 2016
41	Copy of an email dated 20 April 2016 addressed by Ms Malahlela to Mr Burger
42	Copy of an email dated 20 April 2016 addressed by Mr Burger to Ms Malahlela in response to her email
43	Copy of an email dated 20 April 2016 addressed by Ms Malahlela to Mr Burger in response
44	Copy of a letter dated 29 April 2016 addressed by Mr Burger to Mr Mlambo

	titled *"VR LASER: SUPPLY OF FABRICATED STRUCTURES"*
45	Copy of minutes of DLS EXCO meeting held on 04 July 2016
46	Copy of Denel's response to Parliament relating to question number 1569 that was asked of the Minister by a specified MP on 06 June 2017

TERMS AND ABBREVIATIONS

Throughout this document, unless otherwise stated, the words in the first column have the meanings stated opposite them in the second column.

Terms

Armscor	Armaments Corporation of South Africa
B-BBEE	Broad-Based Black Economic Empowerment
BD	Business Development
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CHR	Chief of Human Resources
COO	Chief Operations Officer
DCD	DCD Protected Mobility
DCO	Denel Corporate Office
Denel	Denel SOC Ltd
DLS	Denel Land Systems
DoA	Delegation of Authority
DVS	Denel Vehicle Systems
EM	Executive Manager
EXCO	Executive Committee
FCM	Fighting Compartment Module
GCEO	Group Chief Executive Officer
GCOO	Group Chief Operations Officer

Ngidi Business Advisory
ADVISORY | FORENSICS | TAX

Denel SOC Ltd

Draft Report: Independent Review of the Process Followed in Concluding the Memorandum of Agreement between Denel SOC Ltd and VR Laser Servicers (Pty) Ltd

GDF	Gauteng Department of Finance
GSCE	Group Supply Chain Executive
GM	General Manager
JV	Joint Venture
LMT	LMT Holdings SOC Ltd
MOA	Memorandum of Agreement
MOU	Memorandum of Understanding
OEM	Original Equipment Manufacturer
PATRIA	Patria Plc
RFP	Request for Proposal
RFQ	Request for Quotation
SANDF	South African National Defence Force
SCM	Supply Chain Management
SOE's	State-owned Enterprises
UN	United Nations
UNOPS	United Nations Office for Project Services
VAT	Value Added Tax
Wrt	With respect to

Individuals

Mr Africa	Mr Albert Africa: Business Development Executive Manager, DLS
Mr Burger	Mr A Stephan Burger: Divisional CEO, DLS
Mr Drevin	Mr Martin Drevin: Programme Manager, Hoefyster Phase 2, DLS
Mr Khoza	Mr Innocent Khoza: Acting CFO, DLS
Mr Mahlinza	Mr Thulani Mahlinza: CHR, DLS
Mr Makhatini	Mr Mxolisi Makhatini: Deputy CEO, DLS
Mr Masuku	Mr Douglas Masuku: Acting SCM Executive, DLS
Mr Mhlonto	Mr Mhlonto: Former Group CFO, Denel Group
Mr Mlambo	Mr Denisse Mlambo: SCM Executive, Denel Group
Mr Ntshepe	Mr Zwelakhe Ntshepe: Group CEO and former Business Development and Corporate Affairs Manager, Denel Group
Mr Salojee	Mr Riaz Salojee: Former Group CEO, Denel Group
Mr Teubes	Mr Reenen Teubes: COO, DLS
Ms Tribelhorn	Ms Charlene Tribelhorn: Former Personal Assistant to Mr Teubes, DLS
Mr Van Heerden	Mr Hank Van Heerden: SCM Category specialist, DLS
Mr Wessels	Mr Jan M Wessels: Former Group COO, Denel Group
Mr Williams	Mr Williams: Former GM: Mechem
Ms Govender	Ms Denise Govender: Chief Legal Officer, DLS
Ms Malahlela	Ms Celia Malahlela: Acting GM Operations, Denel Group and former DLS Supply Chain Executive Manager
Mr Mhlwana	Mr Odwa Mhlwana: Group Chief Financial Officer, Denel

Denel SOC Ltd

Draft Report: Independent Review of the Process Followed in Concluding the Memorandum of Agreement between Denel SOC Ltd and VR Laser Servicers (Pty) Ltd

	Group
Ms Qinga	Ms Qinga: Group Executive, Communications & Public Affairs, Denel Group

COMMISSION OF INQUIRY INTO STATE CAPTURE

I BACKGROUND AND MANDATE

1. Based on the State Capture Report by the previous public protector, a judicial commission of inquiry will be established to probe allegations of state capture to look into claims against state-owned enterprises ("SOE's") including Denel.

2. The report touched on allegations against Denel and it was said that a full investigation was to ensue at a later stage. Amongst other matters, specifically the State Capture Report questioned the formation of joint venture Denel Asia with Gupta-linked VR Laser Asia and the Denel relationship with VR Laser SA as a supplier. The Denel Board is of the opinion that it would be in the interest of good governance, given the public protector report, to request an independent review. Such review would, inter alia, provide Denel with information that would be required for a potential judicial commission and ensure that we act responsibly to the public protector reports.

3. We understood the following to be the scope of the review:

   3.1 Review all Supply Chain contracts between Denel and VR Laser for the period of three years ending August 2016 (date around which Denel submitted documents to the Public Protector) and provide an independent report;

   3.2 Determine if there was competitive process followed for the placement of contracts found; and

3.3 Based on the contracts reviewed, provide findings on whether the allegations of state capture are founded or not.

4. The scope specifically excludes the formation of the Denel Asia JV which we understand was already reviewed by the management of the Denel Group.

5. Our mandate was subsequently clarified and we were requested to instead perform an independent review of the process followed in concluding the Memorandum of Agreement ("MOA") between Denel SOC Ltd and VR Laser. Consequently, this draft report contains our factual findings and conclusions on our review of the said MOA.

6. Although we conducted a preliminary review of the contract entered into between DLS and VR Laser in respect of the Hoefyster hulls, this was purely for background purpose as part of our independent review of the process followed in concluding the MOA with VR Laser. The said contract awarded to VR Laser in respect of the Hoefyster platform hulls will be reviewed in the second phase of our investigation.

II NATURE AND SCOPE OF THE REVIEW

1. Our review was based mainly on consultations held with various parties and documentary evidence provided by Denel and other external parties.

2. We were not required nor did we undertake an audit in terms of the International Standards on Auditing. The scope of our work was limited to a review of relevant documentation and information secured as well as consultations conducted with various parties within Denel.

3. The findings contained herein are based on the work performed to the date of this report. We have taken reasonable steps to ensure that the information obtained is authentic and complete. Though we have performed sufficient procedures based on evidence obtained, we cannot provide absolute assurance that the work was exhaustive.

4. We will not accept any responsibility should this draft report or any part thereof, be disclosed or released to any other party without our prior written consent.

5. We were not required to, nor do we express any legal opinion in this document, nor should anything stated herein be regarded as such.

6. The review findings are based on facts, documentary review and other procedures. The review is not a pronouncement of guilt or lack thereof by any party.

7. The draft report contains evidence based on consultations conducted with several parties. We deem the afore-mentioned evidence appropriate to corroborate our findings. We have however, endeavoured not to base our

findings on such evidence alone. Factual findings in this draft report are mainly based on documentation reviewed.

8. It is the prerogative of management to act on any of the recommendations made in this draft report. These are based on our findings to date and take into account, inter alia, remedies available to you as per legislative prescripts. As the recommendations are of an advisory nature, we may not be held responsible for actions emanating from the implementation thereof.

III PROCEDURES PERFORMED

1. We obtained and reviewed copies of the following legislative prescripts and policies/procedures:

   1.1. The Constitution of the Republic of South Africa, Act 108 of 1996;

   1.2. Public Finance Management Act, Act 1 of 1999;

   1.3. Treasury Regulations 16A6.4;

   1.4. Gauteng Provincial Government Supply Chain Management Policy model;

   1.5. Denel SOC LTD Procurement Policy; and

   1.6. Unsigned Denel SOC LTD Delegation of Authority.

2. We obtained and reviewed, *inter alia*, copies of the following documents from DLS:

   2.1. Email dated 17 July 2014 addressed by Mr Wessels to Mr Burger titled "*DLS recent request to contract VR Laser*";

   2.2. Email dated 18 July 2014 addressed by Mr Burger to RE_EXCO1 titled "*Round robin on VR Laser*";

   2.3. Email dated 18 July 2014 addressed by Mr Burger to Mr Wessels and Mr Mhlontlo and copied to Mr Saloojee, Ms Tribelhorn and Mr Ntshepe titled "*DLS recent request to contract VR Laser*";

   2.4. Submission dated 15 October 2014 addressed by DLS EXCO to Group EXCO titled "*Industrialisation and Production of 183 Vehicle Platform Hulls at VR Laser*";

2.5. Report referenced "*D117051_0*" and dated 03 March 2014 that indicates that it was issued by Patria;

2.6. Email dated 10 March 2015 addressed by Mr Drevin to Ms Malahlela titled "*Motivation for single source supply of Hoefyster Turret armour steel fabrications and components.docx*";

2.7. Unsigned memorandum dated 9 March 2015 addressed by Mr Drevin to the Executive Manager: Supply Chain titled "*Supplier for Hoefyster turret armour steel components and fabrication*";

2.8. Email dated 11 March 2015 addressed by Mr Teubes to Ms Malahlela titled "Motivation for single source supply of Hoefyster Turret armour steel fabrications and components.docx;

2.9. Email dated 11 March 2015 addressed by Ms Malahlela to Mr Teubes in response to his email;

2.10. Email dated 11 March 2015 from Mr Teubes responding to Ms Malahlela;

2.11. Email dated 11 March 2015 from Ms Malahlela responding to Mr Teubes;

2.12. Email dated 12 March 2015 addressed by Ms Malahlela to Mr Teubes titled "*GROUP CEO Submission*";

2.13. Unsigned submission dated March 2015 (actual date not specified) titled "*GROUP CHIEF EXECUTIVE OFFICER'S SUPPLY CHAIN SUBMISSION*"

2.14. Email dated 20 March 2015 addressed by Mr Teubes to Ms Malahlela;

2.15. Another unsigned submission dated March 2015 (actual date not specified) titled "*GROUP CHIEF EXECUTIVE OFFICER'S SUPPLY*

CHAIN SUBMISSION";

2.16. Recommendation made by the UN regarding the use of VR Laser;

2.17. Email dated 23 March 2015 addressed by Ms Malahlela to Mr Teubes in response to his email dated 20 March 2015;

2.18. Letter dated 16 April 2015 addressed by Mr Burger to Mr Salojee titled "*MOU WITH VR LASERFOR SUPPLY OF FABRICATED STRUCTURES*";

2.19. Letter dated 22 April 2015 addressed by Mr Burger to Mr Salojee also titled "*MOU WITH VR LASERFOR SUPPLY OF FABRICATED STRUCTURES.*";

2.20. Unsigned minutes of special DLS EXCO meeting dated 3 March 2015;

2.21. Memorandum of Agreement entered into between VR Laser and Denel;

2.22. Email dated 05 June 2015 addressed by Ms Govender to EXCO and copied to Ms Malahlela titled "VR Laser– *APPROVAL FROM DCO AS SINGLE SOURCE SUPPLIER*";

2.23. Minutes of DLS EXCO meeting held on 07 August 2015;

2.24. Minutes of DLS Special Procurement EXCO meeting held on 29 October 2015;

2.25. Memorandum dated 29 October 2015 addressed by Ms Malahlela to Mr Mlambo titled "*Conflict between policy and signed MOU*";

2.26. DLS Procurement EXCO minutes of meeting held on 22 March 2016;

2.27. DLS EXCO minutes of meeting held on 21 April 2016;

2.28. Email dated 20 April 206 addressed by Ms Malahlela to Mr Burger;

2.29. Email dated 20 April 2017 addressed by Mr Burger to Ms Malahlela in response to her email;

2.30. Email dated 20 April 2016 addressed by Ms Malahlela to Mr Burger in response;

2.31. Letter dated 29 April 2016 addressed by Mr Burger to Mr Mlambo titled "VR LASER: *SUPPLY OF FABRICATED STRUCTURES*";

2.32. Minutes of DLS EXCO meeting held on 04 July 2016; and

2.33. Denel's response to Parliament relating to question number 1569 that was asked of the Minister by a specified MP on 06 June 2017.

3. We consulted with the following relevant parties amongst others for purposes of our review:

3.1. Mr Africa;

3.2. Mr Burger;

3.3. Mr Drevin;

3.4. Ms Govender;

3.5. Ms Malahlela;

3.6. Mr Masuku;

3.7. Mr Ntshepe;

3.8. Mr Teubes;

3.9. Mr Van Heerden; and

3.10. Mr Mlambo.

IV Findings

1. Our findings are based on the review of the relevant documentation obtained and consultations conducted. For ease of reference, we set out our findings under the following sections:

Section 1:	Review of relevant legislative framework
Section 2:	Review of the relevant Denel Policies and Procedures
Section 3:	Review of the process followed in concluding the Memorandum of Agreement between Denel and VR Laser

Section 1: Review of relevant legislative framework

1. Chapter 1 of the PFMA (***Annexure 2***) defines unauthorized expenditure, irregular expenditure, fruitless and wasteful expenditure as follows:

   "unauthorised expenditure' means-

   (a) overspending of a vote or a main division within a vote;

   (b) expenditure not in accordance with the purpose of a vote or, in the case of a main division, not in accordance with the purpose of the main division"

   ***"irregular expenditure** means 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

   (b) the State Tender Board Act, 1968 (Act 86 of 1968), or any regulations made in terms of that Act"

   ***"fruitless and wasteful** expenditure' means expenditure which was made in vain and would have been avoided had reasonable care been exercised"*

2. Paragraph 38(1)(a)(iii) of the PFMA (***Annexure 2***) states that: "*The accounting officer for a department, trading entity or constitutional institution must ensure that the department, trading entity or constitutional institution has and maintains an appropriate procurement and provisioning system which is fair, equitable, transparent, competitive and cost-effective.*"

3. Paragraph 38(1)(c)(ii) of the PFMA (**Annexure 2**) states that "*The accounting officer for a department, trading entity or constitutional institution*

must take effective and appropriate steps to prevent unauthorised, irregular and fruitless and wasteful expenditure and losses resulting from criminal conduct."

4. Paragraph 38(1)(g) of the PFMA (***Annexure 2***) states that "*The accounting officer for a department, trading entity or constitutional institution on discovery of any unauthorised, irregular or fruitless and wasteful expenditure, must immediately report, in writing, particulars of the expenditure to the treasury and in the case of irregular expenditure involving the procurement of goods or services, also to the relevant tender board*".

5. Paragraph 38(1)(h)(iii) of the PFMA (**Annexure 2**) states that *"The accounting officer for a department, trading entity or constitutional institution must take effective and appropriate disciplinary steps against any official in the service of the department, trading entity or constitutional institution who makes or permits an unauthorised expenditure, irregular expenditure or fruitless and wasteful expenditure".*

6. Paragraph 45(c) of the PFMA (***Annexure 2***) states that "*An official in a department, trading entity or constitutional institution must take effective and appropriate steps to prevent, within that official's area of responsibility, any unauthorised expenditure, irregular expenditure and fruitless and wasteful expenditure and any under collection of revenue due."*

7. Paragraph 51(1)(b)(ii) of the PFMA (***Annexure 2***) states that "*An accounting authority for a public entity must take effective and appropriate steps to prevent irregular expenditure, fruitless and wasteful expenditure, losses resulting from criminal conduct, and expenditure not complying with the operational policies of the public entity."*

8. Paragraph 51*(1)(e)(iii)* of the PFMA (***Annexure 2***) states that "*An accounting authority for a public entity must take effective and appropriate disciplinary steps against any employee of the public entity who makes or permits an irregular expenditure or a fruitless and wasteful expenditure".*

9. Paragraph 57(c) of the PFMA (***Annexure 2***) states *that "An official in a public entity must take effective and appropriate steps to prevent, within that official's area of responsibility, any irregular expenditure and fruitless and wasteful expenditure and any under collection of revenue due."*

10. Section 217 of the Constitution (***Annexure 3***) states that: *"(1) When an organ of state in the national, provincial or local sphere of government, or any other institution identified in national legislation, contracts for goods or services, it must do so in accordance with a system which is fair, equitable, transparent. competitive and cost-effective.*

11. Paragraph 16A6.4 of the Schedule to Treasury Regulations (***Annexure 4***) states that "*If in a specific case it is impractical to invite competitive bids, the accounting officer or accounting authority may procure the required goods or services by other means, provided that the reasons for deviating from inviting competitive bids must be recorded and approved by the accounting officer or accounting authority."*

12. Paragraph 9.10 of the Gauteng Provincial Government supply chain management policy model (***Annexure 5***) states that "*If in a specific case it is impractical to invite competitive bids, the department / entity may procure the required goods or services by other means, provided that the reasons for deviating from inviting competitive bids must be recorded and approved by the Accounting Officer /Authority (Treasury Regulations 16A6.4). The*

Accounting Officer / Authority may dispense with the normal procurement processes only if the following conditions exist:

- *In cases of emergency where immediate action is necessary to avoid a dangerous or risky situation or misery or disaster such as floods and fires.*
- *When the goods and services required are produced or available from a sole service provider.*
- *For the acquisition of special works of art or historical objects where specifications are difficult to compile.*
- *Acquisition of animals for zoos.*
- *When procuring water from Department of Water Affairs, municipality, municipal entity, or public entity.*
- *When procuring electricity from Eskom, municipality, municipal Entity, or public entity.*

The Accounting Officer / Authority cannot allow lack of proper planning to constitute a reason for dispensing with prescribed bidding processes.

The Accounting Officer / Authority will report within ten (10) working days before the award of the contract to GDF: Treasury Division and the Auditor General, all cases where goods and services above the value of R500 000 (VAT inclusive) were procured in terms of Treasury Regulation 16A6.4. The Accounting Officer / Authority will put measures in place to avoid unauthorized expenditure, irregular expenditure, fruitless and wasteful expenditure. In instances where irregular expenditure occurred and is not considered relevant for condonation, or where the Accounting Officer / Authority does not condone the irregular expenditure, immediate steps must

be taken to recover the irregular expenditure from the responsible employee, if he / she is liable in law."

COMMISSION OF INQUIRY INTO STATE CAPTURE

Section 2: Review of the relevant Denel Policies and Procedures

13. Paragraph 6.3.2 of the Denel SOC LTD Procurement Policy (***Annexure 6***) states that "*In instances where the value is above five hundred thousand rand (R500k) and there are many potential suppliers, an open tender process must be followed unless there are compelling good business reasons to follow a closed tender process. In the case of the latter example, approval must still be obtained from Group Supply Chain Executive. Closed tenders are ideal if the number of potential Suppliers is well known and there is documentary proof. That could also have the effect of containing advertising costs for Denel.*"

14. In terms of paragraph 6.4.1 of the policy (***Annexure 6***) "*The approval of any transaction, depending on the value of the transaction shall be in accordance with the Group Delegation of Authority.* "

15. In terms of paragraph 6.9.1 of the policy (***Annexure 6***) "*The requirement is that only Suppliers that meet Denel's qualifying criteria be contracted for a maximum period of three years unless a longer period is properly motivated and approved as per the Denel Delegation of Authority.*"

16. Paragraph 6.10.1 of the policy (***Annexure 6***) provides that "*Under no circumstances shall products or services that can be procured from a Group Entity or Division be procured from an external Supplier or non-Denel company unless there is approval by the Group Supply Chain Executive based on sound business reasons.*"

17. Paragraph 10.2.2 of the unsigned Denel SOC LTD Delegation of Authority ("DoA") policy (***Annexure 7***) dated 11 February 2015 states that "*It is mandatory that any agreement creating an obligation for Denel should follow*

due process and be approved at the appropriate level of authority. Amendments to or transaction relating to the same agreement must be approved at the same level of the original approval."

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18. The following tables are abstracts of paragraph 13 of the DoA policy (***Annexure 7***)

SH	-	*SHAREHOLDER (DPE)*	*A*	-	*APPROVAL*
DBD	-	*DENEL BOARD OF DIRECTORS*	*PR*	-	*PRIMARY RESPONSIBILITY*
GCE	-	*GROUP CHIEF EXECUTIVE OFFICER*	*CR*	-	*CO-RESPONSIBILITY*
DEX	-	*DENEL EXCO*	*C*	-	*CONSULTATION/INPUT SUPPLIED*
GFD	-	*GROUP FINANCIAL DIRECTOR*	*I*	-	*INITIATE*
GEX	-	*FUNCTIONAL GROUP EXECUTIVE*	*FI*	-	*FOR INFORMATION/RECEIVE REPORT*

No.	*Description*	*SH*	*DBD*	*DEX*	*GCE*	*GFD*	*GEX*	*CEO*	*Remarks*

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No.	Description	SH	DBD	DEX	GCE	GFD	GEX	CEO	Remarks
5	Procurement								Procurement of >R1m per transaction from suppliers with BEE rating >5 (excluding transactions in the approved MPS) to be discussed with the Group Supply Chain Manager for approval. Policy and normal tender requirements to be followed.
5.1	Standard procurement of products and services other than items specified in 5.2 and 5.3.								All procurement transactions for the approval of the GCEO to be counter signed by the Group Supply Chain Manager.
	• ≤R50m				C		C	A	Group Supply Chain Manager

No.	Description	SH	DBD	DEX	GCE	GFD	GEX	CEO	Remarks
									prior consultation on procurement above R20m for process compliance approval.
	• >R50m – R200m			FI	A			I	*Group Supply Chain Manager prior consultation for process compliance approval.* *A report outlining the process followed to invite and shortlist suppliers and evaluation and scores of the shortlisted suppliers and recommendations of the Tender Committee to be tabled at Denel Exco information.*

No.	Description	SH	DBD	DEX	GCE	GFD	GEX	CEO	Remarks
	• >R200m		A		PR			I	To be tabled at Denel Exco first including a report outlining the process followed to invite and shortlist suppliers and evaluation and scores of the shortlisted suppliers and recommendations of the Tender Committee to be tabled at the Board for approval.

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Section 3: Review of the process followed in concluding the Memorandum of Agreement between Denel and VR Laser

Hoefyster platform hulls contract awarded by DLS to VR Laser, reviewed for background purposes

19. We noted a copy of an email (***Annexure 8***) dated 17 July 2014 addressed by Mr Wessels to Mr Burger titled "*DLS recent request to contract VR Laser*". The email (***Annexure 8***) states "*Fikile and I have been considering the submission to contract* VR Laser *for Hoefyster received last Thursday. Based on our discussion of Monday I am not ready to recommend it. My rationale is as follows:*

    - *Like all comparable defence groups we as Denel also have to operate as group companies/divisions encouraging more entity to entity business. The industry is not of less importance, but the internal group business comes first before doing business with the outside industry. This is a universal principle.*
    - *We would like to see a sincere effort to keep this work within the group – exactly the same logic we followed when we encouraged LMT to appoint DLS as main contractor for KSA turrets 5 weeks or so ago.*
    - *We recognise & support the BEE & general RSA supplier development priorities – perhaps DLS could find a compromise (again like we did the turrets & Commenius?) where LMT commits to sub more specific packages to VR Laser and other legitimate black-owned companies for example?*

Lastly, I fully recognise DLS well expressed & valid concerns about the family member – LMT – not being up to standard in certain functional & operational areas. That is the subject of a specific engagement process to strengthen the core at LMT. But as in all these instances DLS should rather please be sharing what it would want to see happening operationally and/or changes that LMT should make, and normal "collaboration forums & steering committees" should please be re-established between DLS & LMT management as discussed on Monday – despite the formal governance directives which talks (sic) *about a different level of relationship."*

20. A copy of an email (***Annexure 9***) dated 18 July 2014 addressed by Mr Burger to RE_EXCO1 titled "*Round robin on VR Laser*" states "*Our discussion this morning at the EXCO meeting wrt the placement* (sic) *the Hoefyster Hull contract on VR Laser, refers.*" The email (***Annexure 9***) further states "*Hereunder is my proposed email to DCO. Your urgent support, or lack thereof is required. I need to send it off to Raiz and team this morning. Sould* (sic) *you want to also propose changes to the email, please feel free to do so. But unfortunately, time is limited."*

21. The email (***Annexure 9***) states "*Dear Jan and Fikile, Thank you for your commitment and support in this regards* (sic)*; it really is appreciated. Your email of 15 July is noted and I fully commit to an improved relationship with LMT. In this regard I intend to reinstitute a Steercom that looks at program performance, business opportunities, marketing intelligence, and the likes. It would have been ideal if a LMT board could chair this meeting, but in the possible absence thereof, I will chair the meeting and determine the direction within a cooperative framework."*

22. According to the email (***Annexure 9***) "*I would also like to reiterate that it is in the best interest of everybody that LMT does well, and I still believe that the product portfolio of LMT, and its knowledge of vehicles and its design, and in particular ballistic protection and vehicle design, is a huge asset to the strategic vison of DLS. We also recognise that LMT is very good at prototyping, but having a repeatable vehicle production capacity, remains their biggest challenge. I also acknowledge that LMT cannot be sustainable by just selling engineering hours, and it is of importance that they also sell products.*"

23. The email (***Annexure 9***) states "*As stated in Monday's meeting, I believe that the primary focus of DLS should be to the best landward prime contractor/system integrator in SA, whilst also being a product supplier/designer of subsystems in certain strategic markets. And in the exception, also do production, but that should be driven by strategic requirements. If the vision of DLS was to insource everything, it will not only kill the local industry, DLS itself will run the risk of not being sustainable of a long period. LMT, however, I see focussing on being a product supplier/design house. And in the exception being a level 5 prime contractor (in line with an agreed product strategy to ensure alignment between DLS and LMT), and also supporting local industry by only manufacturing those strategic components at LMT. The leadership role of Denel in the local industry should not be underestimated.*"

24. The email (**Annexure 9**) further states that "*With regards to the choice of supplier for the Hoefyster vehicle hull, it is true that the original intent of DLS was to support the sustainability of LMT by placing various contracts, including the vehicle hull, on LMT. Unfortunately, regardless of all the good*

discussions and undertaking to support each other, I believe it will be irresponsible to disregard the recommendations of the procurement committee and place the contract on LMT. My humble recommendation remains that it is placed on VR Laser and for the following reasons:" The email (***Annexure 9***) then states the following eight (8) reasons and a brief discussion of each:

24.1. Criticality of the vehicle hull;

24.2. Performance of LMT as a supplier of production equipment;

24.3. Capacity at LMT;

24.4. Business culture of LMT;

24.5. Impact on the Saudi turret contract on DLS;

24.6. Expectation of industry to benefit from Hoefyster;

24.7. Previous decisions taken on promises; and

24.8. Compromise to support LMT.

25. We made various requests, including in our consultation with Mr Burger, for the said recommendations of the procurement committee presumably against the award of the contract concerned to LTM. The said recommendations have, however, not been made available to us. According to Mr Burger, these recommendations, which recommended the award of the Hoefyster hulls contract to VR Laser, should be somewhere in the files at the DLS's offices.

26. "*Therefore, and unfortunately, from a business and operational perspective, my recommendation remains unchanged for this opportunity. But clearly this contract is beyond my delegation and the decision lies with DCO...*", the email (***Annexure 9***) concludes.

27. We further noted a copy of an email (***Annexure 10***) dated 18 July 2014 addressed by Mr Burger to Mr Wessels and Mr Mhlontlo and copied to Mr Saloojee, Ms Tribelhorn and Mr Ntshepe titled "*DLS recent request to contract VR Laser*". The contents of this email (***Annexure 10***) are similar to those of the email (***Annexure 9***) dated 18 July 2014 addressed by Mr Burger to RE_EXCO1 titled "*Round robin on VR Laser* and have, therefore, not been repeated here. We have not been provided with any email responding to the said email (***Annexure 9***) dated 18 July 2014 addressed by Mr Burger to Mr Wessels and Mr Mhlontlo.

28. We noted a copy of a submission (***Annexure 11***) dated 15 October 2014 addressed by DLS EXCO to Group EXCO titled "*Industrialisation and Production of 183 Vehicle Platform Hulls at VR Laser*. The submission (***Annexure 11***) indicates that it was signed by the following parties, who made a recommendation to Mr Saloojee, on the specified dates:

DLS EXCO RECOMMENDATION:

C Mahlalela – Executive: Supply Chain Management	16 October 2014
A Afrika – Executive Manager: Infantry Systems	16 January 2014
FR Teubes – COO: Denel Land Systems	16 October 2014
AS Burger – CEO: Denel Land Systems	16 October 2014

DCO RECOMMENDATION:

JM Wessels – Group COO: Denel	16 October 2014
Z Mhlontlo – Group CFO: Denel	16 October 2014

29. The submission (***Annexure 11***) also indicates that it was signed by Mr Saloojee on 16 October 2014. However, Mr Saloojee did not indicate on the submission whether he was approving or rejecting the recommendation. However, the logical conclusion to draw in this instance would be that he signed as he was approving the recommendation as it would not make sense to sign while one is rejecting the recommendation.

30. The submission (***Annexure 11***) indicates that its objective was "*To obtain approval from Denel Group Executive Officer to*

(a) *enter into contract negotiations for the manufacturing and supply of the HOEFYSTER platform hulls for 183 armoured vehicles to ensure that the total contract price fits within the DLS budget and*

(b) *sign the contract for the manufacturing and supply of the HOEFYSTER platform hulls for the 183 armoured vehicles and place the associated Purchase Order.*"

31. The submission (***Annexure 11***) states the following, *inter alia*, as part of the background:

"In 2013 the board of DENEL authorized the signing of the production Contract for the 238 (Including 34 new variants/new requirement by SANDF) Badger vehicle systems with ARMSCOR. In order to execute the ARMSCOR contract, DENEL Land Systems (DLS) now wishes to sign the Contract and accordingly place an Order for the manufacturing and supply of the armoured hulls for these vehicles. 16 of these vehicles are manufactured in Finland and 217 will be manufactured in South Africa. At this stage DLS has not finalized the baselines for the 34 new variants. We therefore cannot

place an order on the full 217. The intention at this stage is to place an order for only 183 platform hulls. The procurement for the new variants platform hulls will only be made once the baselines have been firmed up with frozen data-packs."

In 2012 DLS obtained quotations from the local industry to benchmark the prices with PATRIA budget prices. LMT, VR Laser and DCD Dorbyl (name changed to DCD protected mobility) were invited to participate in this process. Three quotations obtained from these 3 companies in 2012 were as follows;

SUPPLIER	***PRICE PER UNIT***
LMT	*R1,738,694.00*
VR Laser	*R865,010.00*
DCD Dorbyl	*R896,000.00*

As part of the contract between DLS and PATRIA, PATRIA has an obligation to transfer hull manufacturing and fabrication technology to the local South African supplier that will be contracted for this work. The transfer of Technology between DLS and PATRIA has already begun and various DLS departments must be trained on how to incorporate the processes and date into the DLS systems."

32. The submission (***Annexure 11***) further states, *inter alia*, the following as part of the motivation:

"In June 2014, DLS went out on RFQ to obtain revised prices from all the suppliers that initially quoted in 2012. The tender closing date was 25 June 2014, after which clarification sessions were held (sic) *26th June 2014 with each supplier. They all had 7 days in which to submit additional information. Any information received after this drop dead date was not considered. A cross functional team of representatives from Supply Chain, Infantry Systems and Business Excellence was constituted to evaluate the proposals submitted and make a final recommendation on the supplier that will be manufacturing the platform Hull. The team evaluated the proposals on the following criteria technical, commercial and B-BBEE. The percentage split implemented in the criteria used is accordingly aligned with the mandated Denel criteria communicated throughout the group."*

"In February 2014, PATRIA visited the three suppliers for facility/capacity assessment. The outcomes of this assessment were captured in the final report ref: D117051_.3.2014 submitted to DLS. The outcomes can be summarised as follows:

(a) PATRIA is of the opinion that VR Laser is capable of manufacturing the whole hull from parts to delivery. The possibility of information leakage at VR Laser is slight/minimal. And lastly, the references given for VR Laser are impressive/good.

(b) PATRIA is concerned about the possibility of information leakage at DCD protected mobility. PATRIA relayed the concern that DCD protected mobility has substantial risk for information leak especially for mine protection package. Furthermore, PATRIA is of the opinion that DCD protected mobility has not capacity for the manufacturing

of hull plate sets due to lack of machinery and would have to outsource components or buy new machinery. That said, the PATRIA team felt that DCD protected mobility has all the necessary quality requirements in place and has the capacity to machine turrets ring at one of their other division (sic).

(c) *PATRIA is of the opinion that LMT has poor level of welding quality and it needs to be improved in order to be able to manufacture AMV hulls. However PATRIA also articulated that LMT might still be suitable for the manufacturing of other AMV components."*

33. The above visits by Patria at the said premises of the specified services providers was corroborated through our review of a copy of a report (***Annexure 12***) referenced "D117051_0" and dated 03 March 2014 that indicates that it was issued by Patria. Furthermore, during our consultations with various parties including Mr Burger, Mr Teubes and Mr Drevin, they confirmed that Patria visited the premises of the specified service providers and conducted an inspection thereof as part of the process leading to the conclusion of a contract with VR Laser in respect of Hoefyster platform hulls.

34. Under Discussion/Other Relevant Facts section, the submission (***Annexure 11***) states that "*The evaluation committee noted that the price submitted by LMT is unreasonably too low*", that "*The price submitted by VR Laser seem* (sic) *to be realistic and more acceptable, however this price exceeds DLS's current budget/input price*" and that "*the price offered by DCD protected mobility seem* (sic) *to be extremely higher than the estimated cost above.*"

35. Under the price section, the submission (***Annexure 11***) indicates the revised prices quoted by the aforesaid service providers as summarised hereunder:

SUPPLIER	PRICE PER UNIT
LMT	R768,191.00
VR Laser	R1 209,247.00
DCD	R1 391,319.00

36. During our consultation with Mr Mlambo, he informed us that subsequent to the award of the Hoefyster hulls contract to VR Laser, he spoke to the then Divisional CEO of LMT and made enquiries on the reasonableness of the price that had been quoted by LMT that was, according to the DLS's evaluation committee, unreasonably too low. According to Mr Mlambo, LMT Divisional CEO informed him that the price quoted by LMT was more than enough for LMT to recover the costs and still make a reasonable profit as LMT had a good understanding of the extent and nature of the work required to deliver the project in that they had done the prototype of the vehicle concerned.

37. During our consultation with Mr Burger, he also confirmed that LMT had indeed done the prototype of the Hoefyster vehicle.

38. The submission (***Annexure 11***) further states that *VR Laser has demonstrated the willingness to support DLS on several occasions in the past delivering on time, quality products". VR Laser submitted an unsolicited*

proposal for a lower price as well as submitting a new BBBEE certificate with a new improved level from 4 to 3, but as in the case of the BBBEE Certificate of LMT this could not be considered for the evaluation. We strongly believe that they will be willing to negotiate the prices in order to fit within our budget."

39. We have not performed any necessary additional procedures relating to the said submission by VR Laser of an unsolicited proposal for a lower price as well as a new BBBEE certificate in that, as indicated in the Background and Mandate Section above, the award of the contract to VR Laser for the provision of Hoefyster platform hulls was not part of our mandate but was rather reviewed as part of the background leading to the conclusion of the MOA with VR Laser which is a subject of our review. The review of the contract concluded with VR Laser for the provision of Hoefyster platform hulls will form part of the second phase of our investigation. It is not clear why VR Laser would, during the bid/quotation evaluation process, submit an unsolicited additional information in a form of a revised proposal reflecting a lower price, especially since their initially quoted price was, according to the submission (***Annexure 11***), in excess of the "*DLS's current budget/input price*".

40. Allowing VR Laser an opportunity to resubmit a proposal with a lower amount, without affording the same opportunity to the other participating service providers, would not be fair. This would also potentially compromise the transparency and competitiveness of the process. We have, however, not further investigated this potential transgression as, as indicated above, the review of the Hoefyster platform hulls contract will form part of the second phase of our investigation.

41. Furthermore, it is not clear how VR Laser would have known that their quoted price was in excess of the "*DLS's current budget/input price*" and that there was, consequently, a need to resubmit their proposal with a lower amount.

42. During our consultation with Mr Mlambo (***Annexure 13***), he informed us that he refused to approve the above contract with VR Laser as, in terms of the Denel Group Supply Chain Management Policy (***Annexure 6***), under no circumstances shall products or services that can be procured from a Group entity or division be procured from an external service provider or non-Denel company, unless there is approval by the Group Supply Chain Executive based on sound business reasons. We confirmed that this was indeed a requirement through our review of the of the said Denel Group Supply Chain Management Policy (***Annexure 6***). We will review the aforesaid contract and confirm whether this contract was indeed not approved by Mr Mlambo as part of the second phase of our investigation.

43. According to Mr Mlambo (***Annexure 13***), LMT, one of the divisions of Denel, was capable of providing the required Hoefyster platform hulls and this contract should have, therefore, not been awarded to VR Laser or any other external entity. This was contrary to the views expressed by certain parties we consulted with, including Mr Burger, Mr Teubes, Mr Drevin and Ms Govender, who stated that DLS had previously experienced various challenges relating to LMT's capabilities and the quality of work they had provided and that this is an issue that had to be considered in deciding on whether LMT could successfully deliver on the Hoefyster hulls contract. The said challenges previously experienced were apparently, amongst others, in relation to the supply of vehicles named Caspers to the UN.

44. During our consultation with Mr Burger, he informed us that LMT provided the best mobility protection in South Africa and beyond and that they had exceptional experience in ballistic and mine protection for vehicles. He further stated that, although LMT was brilliant in prototyping and design work, their ability to do production was non-existent. According to Mr Burger, LMT was a design house trying to do production and he was simply not willing to put a programme as complex as Hoefyster at risk by placing same on LMT. He stated that, although the above capabilities of LMT and the fact that they had done the prototype of the vehicle concerned were taken into account, these were totally outweighed by the project failures stated above.

45. Mr Burger further stated that he was previously a member of LMT Board of Directors until Mr Saloojee advised him to relinquish his membership as it was apparently a conflict for him to be a member of the said Board while all orders placed with LMT came from DLS at the time. He stated that, after his termination of the LMT Board membership as advised by Mr Saloojee, the Board did not put appropriate mechanism in place and instead left LMT to the same CEO that had previously bankrupted the organisation. According to Mr Burger, every single programme that DLS contracted to LMT failed and DLS had to go through frustrations and heartaches to resolve these project failures, until it became clear to him that he would not risk any of his programmes by placing same on LMT.

46. Mr Burger further stated that at the time when DLS considered placing the Hoefyster hulls contract on LMT, LMT had just been awarded a contract to deliver certain vehicles to Saudi Arabia and that this, according to him, would have invariably further put a strain on their capacity to deliver.

47. According to Mr Mlambo (***Annexure 13***), the said various challenges experienced by DLS relating to the quality of the work previously done by LMT were in respect of metallurgical issues which had nothing to do with LMT.

48. We have not performed any additional procedures relating to the said issues previously experienced involving the work done by LMT as the award of the contract to VR Laser for the provision of Hoefyster platform hulls was not part of our mandate but was rather reviewed as part of the background leading to the conclusion of the MOA with VR Laser which is a subject of our review.

49. The said submission (***Annexure 11***) dated 15 October 2014 concluded, *inter alia*, that "*As reflected in the evaluation matrix above VR Laser has scored the highest points, however the price offered is over the DLS input/budget price. We hereby request permission to negotiate the price in order to bring it in within the DLS budgeted figures.*"

50. In the recommendations section, the submission (***Annexure 11***) states that "*In line with the discussions articulated herein, we hereby recommend the approval of:*

    (a) The Group CEO of Denel approves the DLS recommended selection of the hull supplier

    (b) A mandate to enter into contract negotiations for the manufacturing and supply of the HOEFYSTER platform hulls for the 183 armoured vehicles to ensure that the total contracts (sic) *price fits within the DLS budget.*

(c) *The necessary permission for Mr Stephan Burger to sign the contract for the manufacturing and supply of the HOEFYSTER platform hulls for the 183 armoured vehicles and place the associated Purchase Order when the condition in a is accordingly met.*

(d) *Contracting LMT as single source supplier for the vehicle rear internal fit and the back door*

(e) *After the completion of the Joint Task Force design that the additional 34 vehicle hulls, rear internal fit and back doors be contracted on the same principles".*

Findings in respect of the MOA concluded with VR Laser

51. A copy of an email (***Annexure 14***) dated 10 March 2015 addressed by Mr Drevin to Ms Malahlela titled "*Motivation for single source supply of Hoefyster Turret armour steel fabrications and components.docx*" states *"Find attached a motivation for single source supply of Hoefyster Turret armour steel fabrications and components. I will deliver a signed copy to you as well."*

52. A copy of an unsigned memorandum (***Annexure 15***) dated 9 March 2015 addressed by Mr Drevin to the Executive Manager: Supply Chain titled "*Supplier for Hoefyster turret armour steel components and fabrication*" was attached to the aforesaid email (***Annexure 14***) dated 10 March 2015 addressed by Mr Drevin to Ms Malahlela. The memorandum (***Annexure 15***) indicates that it is a "*Request for Single Source supply of Turret FCMs (hulls)*

and related armour steel components, e.g. Cradle, Outer Shields and Add-on Armour". The memorandum (***Annexure 15***) states that "*The following are the reasons for this request:*

1) *The Turret FCMs and related armour steel components are critical items, as these items are at the core of:*

   a. *The ballistic protection offered to the Turret Crew when used operationally*

   b. *The performance of the main weapon system, which in part relies on the rigidness and accuracy of the welded FCM and cradle.*

2) *Processing, bending, welding and crack-testing of armour steel are specialised processes. It is recommended that the supplier chosen should have all these processes in house. It is also highly recommended that a supplier is chosen with a proven track-record of manufacturing armour steel structures, e.g. hulls, delivering on time to the required quality standards.*

3) *It is also recommended that the chosen supplier have an in-house machining facility or have a very close relationship with a supplier of such services, as we have in the past experienced lengthy delays and resultant schedule over-runs because of the lack thereof.*

4) *The cost of industrialisation at more than one supplier is not budgeted for. The additional cost would include additional sets of Welding Jigs, training of additional welders, and Process*

Qualification at the additional suppliers, which could include the cost of additional FCMs and related components.

5) *Most of the remaining turret components are assembled onto the turret FCM, and therefore the accuracy of this fabricated component is critical. Finding out at a late stage of Turret assembly that there is a problem with the FCM could require that everything need to be stripped off to allow for rework, or scrapping and replacing of the FCM.*

6) *The Outer Shields and Add-on Armour interfaces to the Turret FCM, and by the nature of cutting, bending, and welding of armour steel, accuracy and repeatability is critical to be able to maintain interchangeability. Because of the aforementioned interfaces it is therefore also recommended to use the same manufacturer for the different components. Having multiple suppliers will make it impossible to maintain the high levels of accuracy, repeatability, and interchangeability from turret to turret."*

53. During our consultations with various parties including Mr Burger, Mr Teubes, Mr Drevin and Ms Govender (***Annexures 16, 17, 18*** and ***19***), they informed us that the aforesaid memorandum (***Annexure 15***) was drafted and sent to the SCM by the Hoefyster Programme team as the Programme team felt it was necessary to have a single service provider assisting with the provision of complex steel fabrications in that it was crucial to, amongst others, maintain accuracy, repeatability and interchangeability of the various components involved. The said parties (***Annexures 16, 17, 18 and 19***) also indicated that they understood that this was done in view of the challenges and difficulties previously experienced by DLS with similar programmes in

respect of various issues of quality and turnaround times with regards to complex steel fabrications.

54. A copy of an email (***Annexure 20***) dated 11 March 2015 addressed by Mr Teubes to Ms Malahlela titled "*Motivation for single source supply of Hoefyster Turret armour steel fabrications and components.docx*" states "*Prepare a supply chain motivation for consideration at EXCO and to be approved by Riaz to support this request.*" In sending this email (***Annexure 20***), it appears that Mr Teubes was responding to the aforesaid email (***Annexure 14***) that had been sent by Mr Drevin to Ms Malahlela.

55. A copy of an email (***Annexure 21***) dated 11 March 2015 addressed by Ms Malahlela to Mr Teubes in response to his email (***Annexure 20***) of 11 March 2015 states "*I have accordingly received the document. As discussed on Friday, I recommend that we go out on tender/RFQ for this. Once, we have identified a supplier that meets our requirements through a competitive process, then we can appoint such a supplier for maximum of 3 year* (sic) *as a single source. The spec and evaluation criteria must be sent to all suppliers invited before time so that each one of them knows exactly how they will be evaluated and what is required from the successful company. I would be very uncomfortable selecting any company as a single source without going out into the market.*"

56. In a copy of an email (***Annexure 22***) dated 11 March 2015, Mr Teubes responded to Ms Malahlela and stated "*My suggestion was that before going out into the market get a strategic direction from EXCO and then go into the market to make a final selection*". Ms Malahlela responded to Mr Teubes in an email (***Annexure 23***) dated 11 March 2015 and stated "*.....That makes sense. On it.*"

57. We noted a copy of an email (***Annexure 24***) dated 12 March 2015 addressed by Ms Malahlela to Mr Teubes titled "*GROUP CEO Submission*" which states "*Please find the attached document as requested.*"

58. We further noted a copy of an unsigned submission (***Annexure 25***) dated March 2015 (actual date not specified) titled "*GROUP CHIEF EXECUTIVE OFFICER'S SUPPLY CHAIN SUBMISSION*". The submission (***Annexure 25***) indicates that it was addressed to EXCO by Supply Chain with a subject that states "*REQUEST TO APPOINT A SINGLE SOURCE FOR THE SUPPLY OF TURRET FCMS (HULLS) AND RELATED ARMOUR STEEL COMPONENTS, E.G. CRADLE, OUTER SHIELDS AND ADD-ON ARMOUR.*" In our consultation with Ms Malahlela (***Annexure 26***), she informed us that this was a submission (***Annexure 25***) she had prepared in line with Mr Teubes's recommendation to first obtain a strategic direction from EXCO and thereafter "go to the market" with a view to identifying a suitable service provider.

59. The submission (***Annexure 25***) indicates that its objective was "*To obtain approval from Denel Group Chief Executive Officer to appoint a single source supplier for the supply of Turret FCMs (hulls) and related armour steel components, e.g. Cradle, Outer Shields and Add-on Armour etc.*"

60. In the background section of the submission (***Annexure 25***), it states that "*The Turret FCMs and related armour steel components are critical items, as these items are at the core of: the ballistic protection offered to the Turret Crew when used operationally and the performance of the main weapon system, which in part relies on the rigidness and accuracy of the welded FCM and cradle. It is the opinion of the technical project team that having*

multiple suppliers will make it impossible to maintain the high levels of accuracy, repeatability, and interchange-ability from turret to turret."

61. The submission (***Annexure 25***) states that "*Processing, bending, welding and crack-testing of armour steel are specialised processes. It is recommended that the supplier chosen should have all these processes in house. It is also highly recommended that a supplier is chosen with a proven track-record of manufacturing armour steel structures, e.g. hulls, delivering on time to the required quality standards.*"

62. The submission (***Annexure 25***) further states that "*It is also recommended that the chosen supplier have an in-house machining facility or have a very close relationship with a supplier of such services, as we have in the past experienced lengthy delays and resultant schedule over-runs because of the lack thereof. The cost of industrialisation at more than one supplier is not budgeted for. The additional cost would include additional sets of Welding Jigs, training of additional welder, and Process Qualification at the additional suppliers, which could include the cost of additional FCMs and related components.*"

63. According to the submission (***Annexure 25***), "*Most of the remaining turret components are assembled onto the turret FCM, and therefore the accuracy of this fabricated component is critical. Finding out at a late stage of Turret assembly that there is a problem with the FCM could require that everything need to be stripped off to allow for rework, or scrapping and replacing of the FCM.*" The submission (***Annexure 25***) further states that "*The Outer Shields and Add-on Armour interfaces* (sic) *to the Turret FCM, and by the nature of cutting, bending, and welding of armour steel, accuracy and repeatability is critical to be able to maintain interchangeability. Because of the*

aforementioned interfaces it is therefore also recommended to use the same manufacturer for the different components."

64. In a section named "SUPPLY CHAIN NOTE", the submission (***Annexure 25***) states that "*Should management approve this request, it is recommended that DLS go out on tender/RFQ for the appointment of the single source for this scope of work. Once we have identified a supplier that meets DLS requirements through a competitive process, then we can appoint such a supplier for a maximum of 3 year* (sic) *as a single source. The speciation and evaluation criteria must be sent to all suppliers invited before time so that each one of the suppliers know exactly how they will be evaluated and what is required from the successful company.*"

65. During our consultation with Ms Malahlela, she stated that word "speciation" used in the submission (***Annexure 25***) as indicated above was incorrect and that the correct word she had wanted to use was "specification" rather.

66. A copy of an email (***Annexure 27***) dated 20 March 2015 addressed by Mr Teubes to Ms Malahlela states "*I have changed the angle that we ask for approval from Riaz. Please see attached submission. Any inputs?*"

67. We further noted a copy of another unsigned submission (***Annexure 28***) dated March 2015 (actual date not specified) titled "*GROUP CHIEF EXECUTIVE OFFICER'S SUPPLY CHAIN SUBMISSION*". This submission (***Annexure 28***) also indicates that it was addressed to EXCO by Supply Chain with a subject that states "*REQUEST TO APPOINT A SINGLE SOURCE FOR THE SUPPLY OF TURRET FCMS (HULLS) AND RELATED ARMOUR STEEL COMPONENTS, E.G. CRADLE, OUTER SHIELDS AND ADD-ON ARMOUR*." In our consultation with Ms Malahlela, she informed us

that this was a submission (***Annexure 28***) that was attached to the aforesaid email sent by Mr Teubes to her dated 20 March 2015. According to Ms Malahlela, this submission (***Annexure 28***) was an amended version of the initial submission (***Annexure 25***) she had prepared in line with Mr Teubes's recommendation as referred to in paragraph 54 above.

68. The submission (***Annexure 28***) indicates that its objective was "*To obtain approval from Denel Group Chief Executive Officer to appoint a single source supplier for the supply of fabricated structures including Vehicle hulls, Turret FCMs (hulls) and related armour steel components, e.g. Cradle, Outer Shields and Add-on Armour etc.*"

69. In the background section, the submission (***Annexure 28***) states that "*DLS have embarked on a process to categorize suppliers according to their level of relationship to DLS. One of these categories are Strategic single source suppliers.*"

70. The submission (**Annexure *28***) states that "*Fabricated structures eg Turret FCMs and Vehicle Hulls are at the core of the ballistic protection offered to the crew when used operationally and the performance of the, vehicle, main weapon system, which in part relies on the rigidness and accuracy of the fabricated FCM and cradle. Is the opinion of the technical team that having multiple suppliers will make it impossible to maintain the high levels of accuracy, repeatability, and interchange-ability from fabricated structure to structure. It is also important to note that a set of jigs and fixtures is manufactured to support a specific manufacturing process. These jigs and fixture contribute significantly to the accuracy and repeatability of the cutting and welding processes. This can therefore only be supported by one supplier.*"

71. The information in the "*Motivation*" section of the submission (***Annexure 28***) is similar to that in the same section of the submission (***Annexure 25***) that was compiled by Ms Malahlela as attached in her email dated 12 March 2015 addressed to Mr Teubes as discussed in paragraphs 57 to 63 above with the exception of the following paragraphs (the rest of the paragraphs that are similar have not been repeated here):

"*The Hulls is* (sic) *a key element of the vehicle system and the history has shown that strict control over the manufacturing process is key. Most defence suppliers for vehicles and turrets prefer to have this capacity in house. This is however not a commercial* (sic) *sustainable option just for your owned products and therefore for Denel Land Systems we have made the selection to contract as single source one company that can supply these fabricated structures as per our specifications and processes.*

The decision for a single source strategic supplier is based on capability, capacity and the ability to deliver key components as per requirement. The price can be negotiated on a case by case basis and tested in the industry. Acceptable BBBEE levels and at least 25% black ownership for single source supplier is non negotiable".

72. A new paragraph, which was not in the version (***Annexure 25***) compiled by Ms Malahlela as discussed above, was inserted in the submission (***Annexure 28***) under the section named "*RECOMMENDATION – DLS*". This new paragraph inserted states "*Based on the Supply Chain process followed for the Hoefyster vehicle and the AV8 turrets hulls to date and that both these processes are or will be industrialized at VR Laser it is*

recommend (sic) *that VR Laser is appointed as single source supplier for fabricated structures for a period of 3 years.*"

73. The section named "*SUPPLY CHAIN NOTE*" that was in the initial version (***Annexure 25***) compiled by Ms Malahlela as well as the contents thereof does not appear in the submission (***Annexure 28***) as per the email of 20 March 2015 addressed to Ms Malahlela by Mr Teubes. It therefore appears that this section was removed from the said submission (***Annexure 28***) sent by Mr Teubes to Ms Malahlela.

74. During our consultation with Mr Teubes (***Annexure 17***), he stated that based on the recommendation (***Annexure 15***) made by the Hoefyster Programme team and in view of the fact that the laid down procurement process had apparently been followed for the Hoefyster vehicle and the AV8 turrets hulls contract, as well as the fact that a recommendation (***Annexure 12***) was made by Patria for the use of VR Laser on the hulls contract, he believes that the process followed by DLS in concluding the MOA with VR Laser was in line with the relevant legislative prescripts and laid down processes. He stated that the said MOA was also approved by the then Group CEO who had the necessary authority to do so.

75. In relation to the requirement to use internal Denel divisions where the relevant internal capabilities exist, Mr Teubes stated that LMT was afforded an opportunity to participate in the procurement process relating to the Hoefyster platform hulls contract and that they were unfortunately not successful.

76. As discussed above, Mr Teubes further indicated that various issues of quality were detected in relation to the fabrication of vehicles named

Caspers supplied to the UN where LMT was involved and that the UN later instructed DLS to use VR Laser in the said project.

77. We noted a copy of the said recommendation (***Annexure 29***) made by the UN regarding the use of VR Laser. It is however apparent that this recommendation was specific to the Caspers contract and it would not be appropriate to use this recommendation as a basis for any other fabrication project.

78. We noted a copy of an email (***Annexure 30***) dated 23 March 2015 addressed by Ms Malahlela to Mr Teubes in response to his email (***Annexure 27***) dated 20 March 2015. The email (***Annexure 30***) states "*I have gone through the document and I realised that you have taken out my recommendation and now the document has the name of the supplier specified. I don't mean to belabour the point but I am still of the opinion that should management approve this request, DLS must go on tender/RFQ for the appointment of the single source for this scope of work. Once we have identified a supplier that meets DLS requirements through a competitive process, then we can appoint such a supplier for maximum of 3 year* (sic) *as a single source. The speciation and evaluation criteria must be sent to all suppliers invited before time so that each one of the suppliers know exactly how they will be evaluated and what is required from the successful company.*" As already indicated in paragraph 65 above, in our consultation with Ms Malahlela, she stated that the word "speciation" was incorrectly used herein and that she had intended to use the word "specification" instead.

79. The email (***Annexure 30***) further states that "*Furthermore I think that it will only be fair to allow LMT to compete for this work. Firstly we had a contract with them for Trunnion (FCM) machining which is part of the proposed scope*

of work in this request, which was later cancelled due to reasons unbeknown to me because it was before my time as the exec manager of supply chain. Secondly when we suspended the order for the AV8 FCM we wrote a letter to LMT where we stated that the intent at the time was to continue/finish off the execution of that particular order as part of the Hoefyster FCM order. I am not saying that the work must be given to LMT, all I am saying is that LMT and other capable suppliers must be given a chance to prove themselves through a transparent, competitive and fair RFQ/tender process." The said contract with LMT relating to Trunnion (FCM) that was allegedly terminated as well as the circumstances around the AV8 FCM order that was apparently suspended will be reviewed as part of our extended mandate to be performed in the second phase of our investigation.

80. Additionally, the email (***Annexure 30***) states that *"I don't think we should piggyback on the process that was followed for the platform hull. We should go out on a separate RFQ/Tender process where we invite all suppliers that we think are capable and then do such appointment. I will ask michelle to schedule a meeting to discuss further."* In our consultation with Ms Malahlela, she stated that the meeting referred to in her email (***Annexure 30***) did indeed take place wherein she reiterated what she had stated in the said email (***Annexure 30***) dated 23 March 2015 she addressed to Mr Teubes.

81. We noted a copy of a letter (***Annexure 31)*** dated 16 April 2015 addressed by Mr Burger to Mr Salojee titled "*MOU WITH VR LASERFOR SUPPLY OF FABRICATED STRUCTURES*".

82. The letter (***Annexure 31***) states that "*In the process of sub-contracting the various sub systems for Hoefyster and the AV8 programs it is important for*

DLS to continuously investigate best practices whilst ensuring that, through risk mitigation actions, a quality product will be delivered to our clients within cost and schedule constraints."

83. The letter (***Annexure 31***) further states that "*A category of these sub systems found by the Hoefyster and A8 programs, to be handled differently to the normal multi tender process, was the supply of fabricated turrets, outer shields and add-on armour and vehicle hull structures due to:*

1) Processing, bending, welding and crack-testing of armour steel being specialised processes;

2) Dimensional accuracy of the industrialized sets of welding jigs and the associated fabrication (training and process qualification) processes, at a supplier has a direct impact on the quality and repeatability of products; and

3) Most of the remaining turret and vehicle components are assembled onto the fabricated structure therefore the accuracy of this fabricated component is critical. Finding out at a late stage of the assembly process that there is a problem with the fabricated structure could require that everything needs to be stripped off to allow for rework or scrapping and replacing of the fabricated structure."

84. According to the letter (***Annexure 31***), "*Based on the above-mentioned analysis and facts the program team motived to the Supply Chain department the selection of a single source supplier. The submission of the Supply Chain department was debated and analysed at the DLS EXCO and it was agreed to recommend the conclusion of a Memorandum of Understanding (MOU) with VR Laser for the fabrication of complex*

engineering systems." We have requested copies of the said submission of the Supply Chain department that was apparently "debated and analysed at the DLS EXCO". Furthermore, we requested to be provided with copies of minutes of meeting of DLS EXCO wherein the said submission was apparently "debated and analysed". As of the date of this draft report, this information remains outstanding. Ms Govender (***Annexure 19***) informed us that this was an informal EXCO coffee session and not a procurement meeting. She further stated that there was no formal recommendation that resulted from this session. It is unclear why an important matter as a motivation for single source relating to a crucial programme like Hoefyster would be discussed over a mere coffee session and not appropriately recorded. This appears to be irregular.

85. The letter states "*It is hereby recommended that the attached MOU, which outlines the basis of the working relationship with VR Laser for the industrialization of the fabricated structures, be favorably* (sic) *considered for signature between DLS and VR Laser*".

86. The letter (***Annexure 31***) indicates that it was signed by Mr Burger, as an author. Although spaces were provided in the letter (***Annexure 31***) for both Mr Ntshepe and Mr Wessels to sign for "*RECOMMENDED FOR APPROVAL*" to Mr Saloojee, according to the letter (***Annexure 13***), only Mr Ntshepe signed in the space provided. Mr Saloojee also did not sign in the space provided for his signature as an approval.

87. In our consultation with Mr Mlambo (***Annexure 13***), he stated that he did not understand what the reason was for Mr Ntshepe's signature on the letter (***Annexure 31***), as he had no authority to sign since he was the Head of

Business Development at the time and no contract signing powers were delegated to him in terms of the DoA.

88. Based on our review of a copy of the said DoA (***Annexure 7***), we indeed confirmed that no contract signing powers were delegated to the Head of Business Development. According to DoA (***Annexure 7***), depending on the amounts involved, the procurement transactions should be approved by the relevant Divisional CEO, Group CEO and the Board of Directors. Additionally, all procurement transactions approved by the GCEO should also be counter signed by the GSCE. Furthermore, according to the DoA (***Annexure 7***), all procurement transactions above R20m are to be approved by the GSCE.

89. We further noted a copy of a letter (***Annexure 32***) dated 22 April 2015 addressed by Mr Burger to Mr Salojee also titled "*MOU WITH VR LASERFOR SUPPLY OF FABRICATED STRUCTURES.*"

90. The letter (***Annexure 32***) states that "*The exceptional growth and the number of key current and future large programs in DLS has necessitated the business to reassess our relationship with key and strategic industry partners, considering critical parameters such as:*

- *Sustainable industry development, including key and unique capabilities*
- *Commercial and technical requirements*
- *Enterprise development*
- *Geo-political considerations*
- *BBBEE objectives*"

91. The letter (***Annexure 32***) further states that "*It is clear that the direction and example as set by Rooivalk is also relevant to major programs in DLS. Therefore categorizing the relevant supplier industry and establish associated customized agreement in the following categories, will be followed by DLS:*

- *System OEM – Strategic*
- *Segment OEM – Member of Core industry team, strategic*
- *Strategic supplier of core subsystems, tactical*
- *Normal procurement within operational requirements*"

92. According to the letter (***Annexure 32***), "*In the process of sub-contracting the various sub systems for Hoefyster and the AV8 programs it is important for DLS to continuously investigate best practices whilst ensuring that, through risk mitigation actions and applying the framework of the mentioned parameters above that a quality product will be delivered to our clients within cost and schedule constraints. A group of these sub systems found by the Hoefyster and AV8 programs, to be categorized as indicated above, is the supply of fabricated turrets, outer shields and add-on armour and vehicle hull structures due to…*". The three main factors that were then stated in the letter after this paragraph are similar to those stated in a copy of a letter (***Annexure 31***) dated 16 April 2015 as summarised in paragraph 83 above and have not been repeated here.

93. The letter (***Annexure 32***) indicates that "*Based on the above-mentioned analysis the program team motivated to the Supply Chain department that a process should be followed to the* (sic) *select a strategic supplier for these core subsystems. In the Supply Chain processes in the last couple of years*

various tenders for the indicated subsystems, on the two major programs, were solicited from the local industry and contracts awarded based on the agreed Supply Chain selections criteria. The level of success to comply with the contract parameters were also monitored on the various contracts. The latest contract that was awarded through this process was the Hoefyster platform hull fabrication to VR Laser. It was clear in the adjudication process of the hull sub contract and on all the contracts awarded to date that VR Laser complies with the critical parameters for a strategic industry partner."

94. The letter (***Annexure 32***) further states that "*The submission of the Supply Chain department was debated and analyzed at the DLS EXCO and it was agreed to recommend the conclusion of a Memorandum of Understanding (MOU) with VR Laser for the fabrication of complex engineering systems within the following parameters:*

- *MOA will be balanced and protect long term best interest of both companies*
- *Mechanisms to exit in cases of failure on the critical parameters must be included*
- *Best commercial agreement will be concluded to satisfy the program and company requirements*
- *Separate orders will be placed under the umbrella of the MOU whilst considering all suitable Supply Chain parameters, such as technical, schedule, financial and quality requirements."*

95. Paragraph 11.10 of a copy of unsigned minutes of special DLS EXCO meeting (***Annexure 33***) dated 3 March 2015 states the following in relation to VR Laser, which was discussed under "General" item of the agenda:

"a) A submission must be made to DCO to be signed by the GCEO.

b) An MOU between VR Laser and DLS where DLS is given priority on orders re the fabrication of structures. There will be exclusivity to VR Laser but subject to VR Laser's performance, regular reviews, price competitiveness, quality and preference. This needs to be a mutually beneficial business relationship to enable DLS to execute efficiently on its orders with Armscor and will also ensure VR Laser's investment in DLS as a preferential client."

96. The minutes ***(Annexure 33)*** indicate that the aforesaid special DLS EXCO meeting was attended by the following parties:

Initials and Surname	Position
S. Burger	CEO (Chairman)
M. Makhatini	Deputy CEO (BD)
I. Khoza	Acting CFO
R. Teubes	COO
T. Mahlinza	CHR
A. Williams	GM: Mechem
T. Govender	Executive: Legal (Secretary)

97. It seems that the said minutes (***Annexure 33***) of special DLS EXCO meeting discussed above only reflected the resolutions that were taken in relation to

the proposed MOU with VR Laser and not the debate and analysis thereof as referred to in the two copies of letters (***Annexures 31 and 32***) dated 16 April 2015 and 22 April 2015 addressed by Mr Burger to Mr Salojee.

98. We are yet to conduct consultations with Mr Makhatini, Mr Khoza and Mr. Mahlinza with a view to confirming the nature and extent of the debate and analysis, if any, that took place in the said special DLS EXCO meeting of 3 March 2015.

99. The letter (***Annexure 32***) states "*It is hereby recommended that VR Laser is categorized as a Strategic supplier of Core Sub systems, for the supply of fabricated structures and that the attached MOU, which outlines the basis of the working relationship with VR Laser for the industrialization of the fabricated structures, be favorably* (sic) *considered for signature between DLS and VR Laser*".

100. The letter (***Annexure 32***) indicates that it was signed by Mr Burger, as an author, and approved by Mr Saloojee. The letter (***Annexure 32***) also indicates that it was signed by Mr Ntshepe and Mr Wessels who "*RECOMMENDED FOR APPROVAL*" to Mr Saloojee.

101. In our consultation with Mr Mlambo (***Annexure 13***), he stated that he was not aware what the reason was for Mr Ntshepe's signature on the letter (***Annexure 32***), since, as stated above, no contract signing powers had been delegated to him as the Head of Business Development in terms of the DoA. Furthermore, Mr Mlambo informed us that no contract signing powers had been delegated to Mr Wessels, who was the GCOO, in terms of the DoA.

102. During our consultation with Mr Burger (***Annexure 16***) he informed us that he was advised by Mr Saloojee to make provision for both Mr Ntshepe and Mr Wessels to sign on the aforesaid two (2) letters dated 16 April 2015 and 20 April 2015 (***Annexures 31 and 32***) and that he had no right to question that instruction.

103. Based on our review of a copy of the said DoA (***Annexure 7***), we confirmed that indeed no contract signing powers were delegated to the GCOO.

104. As indicated above, according to DoA (***Annexure 7***), depending on the amounts involved, the procurement transactions should be approved by the relevant Divisional CEO, Group CEO and the Board of Directors. Additionally, all procurement transactions approved by the GCEO should also be counter signed by the GSCE. Furthermore, according to the DoA (***Annexure 7***), all procurement transactions above R20m are to be approved by the GSCE.

105. We noted a copy of a Memorandum of Agreement (***Annexure 34***) entered into between VR Laser and Denel. The Memorandum (***Annexure 34***) indicates that it was signed by Mr Vander Merwe and Mr Burger on behalf of VR Laser and Denel, respectively, on 19 May 2015. It also indicates that it was signed by four (4) unidentified individuals as witnesses, presumably two (2) on behalf of VR Laser and the other two (2) on behalf of Denel.

106. The Memorandum (***Annexure 34***) states "VR Laser *offers vast experience and harnessed specialist skills, in steel servicing particularly unique solutions for vehicle protection which includes, inter alia, laser cutting, armour works, fabrication and machining related to such fabrication which services are supported by the latest technology…*".

107. The Memorandum (***Annexure 34***) indicates the following, under the scope section:

"*a.* *DLS requires the services of a supplier for the fabrication of complex engineering systems as it does not currently have fabrication capabilities within the organisation.*

b. *The fabrication capabilities are critical for DLS to be able to meet its contractual obligations to its Customer and hence a strategic single source supplier needed to be identified.*

c. *A single source supplier for the services as set out in paragraph 1e* (sic) *below is necessary, inter alia, for the fabrication and supply of the turret fighting compartment modules and related armour steel components of vehicles for, inter alia, the following reasons:*

(i) *The jigs and fixtures are manufactured to support a specific manufacturing process and contribute significantly to the accuracy and repeatability of the cutting and welding processes which can only be supported by one supplier.*

(ii) *The significant cost of industrialisation should two or more suppliers be used as this would require additional sets of welding jigs, training of additional welders, associated cost of additional fighting compartment modules and related components and process qualification at additional suppliers.*

(iii) *There is a risk of rework and/or scrapping and/or replacement as a result of inaccuracies in the assembly of the fabricated components.*

(iv) *By the nature of the required cutting, bending, and welding of armour steel, accuracy and repeatability is critical to be able to maintain. interchangeability from fabricated structure to structure and therefore it is important to maintain the same manufacturer for the same components."*

108. According to the Memorandum (***Annexure 34***), "VR Laser, *with its proven its* (sic) *capabilities and quality is considered to be a key supplier and a strategic partner to DLS"* and *"The purpose of this Memorandum of Agreement (MOA) is thus to define the main principles for the basis of VR Laser being a single source supplier to DLS for the subject matter of this MOA. VR Laser shall be the sole strategic supplier for the provision of all fabricated steel services and goods such as fabrication of hulls, fabricated structures and/or turret hulls, subject however to it being commercially viable to both parties as determined independently by each party in respect of its own business."*

109. The Memorandum (***Annexure 34***) states that "*The scope of this MOA will become effective on the signature date and will remain in force for a period of 10 (ten) years subject to any earlier termination or cancellation of this MOA……".*

110. According to Mr Teubes (***Annexure 17***), the MOA period of 10 (ten) years was decided upon after taking into account the estimated duration of the Hoefyster programme. This was confirmed by Ms Govender (***Annexure 19***) who stated that the initial version of the MOA reflected a contract duration of three (3) years and that the revised contract duration of ten (10) years was suggested by VR Laser in a form of tracked changes in the draft MOA that had been sent to them for their input prior to finalisation and signature.

111. Ms Govender stated that she enquired on the proposed 10-year period with Mr Teubes, as opposed to three (3) years which was a standard and best practice, and that Mr Teubes informed her that the 10-year period was agreed upon after having taken into account the estimated duration of the Hoefyster programme and the fact that VR Laser had to make an upfront investment of approximately R10m as part of the industrialisation process which had to be recouped over time and that it, therefore, made sense to align the contract duration of the MOA with the Hoefyster programme.

112. However, in terms of paragraph 6.9.1 of Denel SOC Ltd Group Supply Chain Policy (***Annexure 6***) "*The requirement is that only Suppliers that meet Denel's qualifying criteria be contracted for a maximum period of three years unless a longer period is properly motivated and approved as per the Denel Delegation of Authority.*" We have not been provided with any evidence that the required motivation was made. The fact that the MOA was concluded with VR Laser for a contract period longer than the maximum period of three (3) years as specified in the policy (***Annexure 6***) is irregular and amounts to the contravention of the Denel SOC Ltd Group Supply Chain Policy (***Annexure 6***). Furthermore, this had an effect of committing DLS for an extended period which in turn unnecessarily exposed the entity to an undue risk.

113. We noted a copy of an email (***Annexure 35***) dated 05 June 2015 addressed by Ms Govender to EXCO and copied to Ms Malahlela titled "VR LASER– APPROVAL FROM DCO AS SINGLE SOURCE SUPPLIER".

114. The email (***Annexure 35***) states "*As discussed at this morning's Urgent Supply Chain meeting, please find attached, for your records, the approval from DCO for VR Laser to be a single source supplier.*" The MOA

(***Annexure 34***) as well as the letters (**Annexures *31*** and ***32***) dated 16 April 2015 and 22 April 2015 respectively addressed by Mr Burger to Mr Saloojee were attached to this email (***Annexure 35***). In our consultation with Ms Malahlela (***Annexure 26***), she stated that she was not part of the said "Urgent Supply Chain meeting" held on 05 June 2015 as referred to in the email (***Annexure 35***) from Ms Govender. We have requested a copy of this meeting from Ms Govender and the same remains outstanding.

115. A copy of the minutes (***Annexure 36***) of DLS EXCO meeting held on 07 August 2015 states, under UNOPS Casspirs project (Casspir 2000 B7 Troop Carriers and Casspir 2000 B7 Automatic Recovery vehicles), that "*Denel Vehicle Systems as a Denel division is the preferred service provider for this work. However UNOPS has prescribed VR Laser as the preferred supplier for this order. A copy of the letter is attached to attach to the submission documents.*"

116. The minutes (***Annexure 36***) further state the following:

- *"Following this, DLS entered into preferred supplier agreement with VR Laser for the manufacturing of all complex steel fabrications.*
- *As stated above, DLS having communicated to LMT that it has the intention of placing the Hoefyster order for the FCM on LMT. The concern raised by CM was that DLS is now placing the very same order on VR Laser without going back to LMT.*
- *It was further noted on recent RFQs that LMT was invited for, LMT either came out more expensive or declined to submit proposal/Quotation. The most recent being the withdrawal of their proposal on the rear door for Hoefyster."* We were informed by Ms

Govender that "CM" indicated in the above and any other minutes of DLS EXCO and DLS Procurement EXCO meetings refers to Ms Malahlela.

117. Under conditional approval, the minutes (***Annexure 36***) state, amongst others, that "*DLS CEO will have a discussion with Denel GCOO and Acting GCFO in their capacity as LMT Board Members to gain insight the reasoned decisions taken by LMT and get some guidance on the way forward, This* (sic) *decisions include:- refusing to quote lately and they withdrew their back door proposal.*"

118. The minutes (***Annexure 36***) further state, Under the Fire Compartment Module-Trunnion Manufacturing project, that "*A contract was signed with LMT for Hoefyster phase 2 Trunnion Machining but was cancelled because Armscor had placed the Hoefyster Phase 2 order on DLS at the time.*"

119. A copy of minutes (***Annexure 37***) of DLS Special Procurement EXCO meeting held on 29 October 2015 indicates that a concern was noted with regards to the placement of orders on VR Laser and that "*The predicament here is that the GSCE approved this deviation from the procurement process on the following condition "Under no circumstances shall products or services that can be procured from a Group Entity or Division be procured from an external Supplier or non-Denel company unless there is approval by the Group Supply Chain Executive based on sound business reasons." This is also in line with the Group supply chain policy and the DLS supply chain procedure.*" The minutes (***Annexure 37***) further state that "*The above provisions are in direct conflict with the MOU that DLS signed with VR Laser where VR Laser is the sole supplier for all complex welding and machining work in DLS for the next 10 years.*"

120. It is stated in the resolution section of the minutes (***Annexure 37***) that "*The Committee took a decision that the MOU takes precedence over the GSCE's condition and the Group supply chain policy and the DLS supply chain procedure. The committee stated also that given the resend* (sic) *history with regards to prise* (sic) *and turnaround time VR Laser was the preferred supplier with all opportunities. It was further stated that in terms of the MOU, VR Laser's prices must be market related and in line with the provisions of the MOA before an order can be placed on them. Due to this reason and previous experience with VR Laser, the committee felt confident that the VR Laser's prices will be market related and reasonable. Celia Malahlela was tasked to draft a letter to the GSCE and explain the decision taken in his regard.*" We are yet to identify the parties which attended this meeting as the extract of the minutes of this meeting in our possession does not reflect same.

121. The resolution taken by the DLS EXCO, as per the aforesaid minutes (***Annexure 37***) of meeting held on 29 October 2015, that the MOA entered into with VR Laser takes precedence over the GSCE's condition, the Group Supply Chain policy and the DLS Supply Chain procedure, in relation to the use of Denel Group entity or division, appears to be irregular in that, in terms of best practice, an agreement concluded with a service provider could not be considered to take precedence over the entity's prevailing policies and procedures.

122. In instances where prevailing policies and procedures are not applicable or for whatever reason not considered to be relevant, then in such cases a consideration should be made to amend the said policies and procedures by following a laid down process to do so instead of simply transgressing

prevailing policies and procedures and make pronouncements to the effect that the agreements concluded take precedence over these policies and procedures.

123. Furthermore, the fact that such a resolution was taken by DLS Procurement EXCO suggests that DLS Procurement EXCO was of the view that due procurement processes as per the Group Supply Chain policy and the DLS Supply Chain procedure were not adhered to. Furthermore, this is contradictory to the aforesaid assertion made by Mr Teubes, as stated in paragraph 74, that he believed that due procurement processes were followed in concluding the MOA with VR Laser.

124. The assertion by Mr Teubes was also confirmed by Ms Govender who believed that due processes were followed in concluding the MOA with VR Laser. This apparent suggestion by the DLS Procurement EXCO to contravening Denel's due processes as well as the apparent contradictory assertions by Mr Teubes and Ms Govender in this regard appear to be irregular.

125. A copy of a memorandum (***Annexure 38***) dated 29 October 2015 addressed by Ms Malahlela to Mr Mlambo titled "*Conflict between policy and signed MOU*" was noted. According to the Memorandum (**Annexure *38***), "*In giving the approval for the deviation from the normal procurement process and a list of suppliers to be used for the T5 Demo, the group supply chain executive gave an instruction that DLS must first explore how Denel Vehicle Systems – Gear Ratio and LMT (Intergroup companies) will be used in the project on condition that they meet the quality, price and delivery requirements.*"

126. The Memorandum (***Annexure 38***) states "*Furthermore, In terms of the approved Denel Supply Chain Policy and DLS supply chain procedure, DLS must first approach intergroup companies before procuring outside the group. In terms of the Denel Group Supply Chain Policy "Under no circumstances shall products or services that can be procured from a Group Entity or Division be procured from an external Supplier or non-Denel company unless there is approval by the Group Supply Chain Executive based on sound business reasons.*"

127. The Memorandum (***Annexure 38***) further states "*Having identified a need for a single source supplier for the supply of STEEL COMPONENTS AND FABRICATIONS, In May 2015 DLS signed an MOA with VR Laser for this Scope of work. VR Laser is a 100% Black owned entity. In terms of the MOA, VR Laser's prices must be market related and in line with the provisions of the MOA before an order can be placed on them.*" During our consultation with Mr Mlambo (***Annexure 13***), he stated that he was not entirely certain whether VR Laser was indeed 100% Black owned as suggested.

128. We however have not performed any necessary additional procedures to verify this suggestion by Mr Mlambo as this was not part of our mandate.

129. According to the Memorandum (***Annexure 38***), "*Due to these contradicting positions, Supply Chain approached DLS EXCO to make a decision as to whether to honour the MOA and place the order on VR Laser or to follow the supply chain policy and procedure from (intergroup) viz, DVS or LMT for this project. Given the timeframe, urgency and history EXCO has recommended that the work be done by VR Laser*".

130. The Memorandum (***Annexure 38***) concluded by stating *"I hereby request permission to implement the EXCO decision in this regard."*

131. We noted that the Memorandum (***Annexure 38***) was not signed by Mr Mlambo in the space provided therein for him to sign and that a handwritten comment was instead appended thereon stating "*NB: DVS and LMT must submit proof that they cannot meet the requirements prior to the contract being awarded to VR Laser*". In our consultation with Mr Mlambo (***Annexure 13***), he confirmed that this handwritten comment was appended by him after he rejected the Memorandum (***Annexure 38***). Mr Mlambo stated that he believed that DVS and LMT, as Denel's divisions, should have first been considered in terms of the Denel's policies and procedures.

132. We further noted that "*Approved*" comment was appended at the bottom of the Memorandum (***Annexure 38***) and a signature indicated as that of Mr Ntshepe was appended next to the said "Approved" comment made. Mr Ntshepe confirmed, during our consultation, that this Memorandum (***Annexure 38***) was approved by him after Mr Mlambo rejected same. Mr Ntshepe informed us that had to make a decision at the time and he believes this was a right decision under the circumstances as he understood that due procurement processes had been followed in concluding the MOA with VR Laser.

133. During our consultation with Mr Mlambo (***Annexure 13***), he informed us that no engagement was had with him by anyone, including Mr Ntshepe, subsequent to his refusal to approve the Memorandum (***Annexure 38***). This was confirmed by Mr Ntshepe who stated that he saw no need to engage Mr Mlambo on his refusal to approve this request in that, as stated above, he believed that due procurement processes had been followed in concluding

the MOA with VR Laser. He further stated that he was not willing to waste time on this matter that could delay the programme resulting in DLS having to pay penalties for failing to meet agreed upon timeframes.

134. During our consultation with Mr Mlambo, he stated that he would have handed the Memorandum (***Annexure 38***) back to the DLS Supply Chain Executive after he appended his comment thereon and was not sure how the Memorandum (***Annexure 38***) would have then got to Mr Ntshepe who subsequently approved same. Mr Ntshepe informed us that he would not recall who he received this Memorandum (***Annexure 38***) from as, like all the other documents forwarded to his office, this Memorandum (***Annexure 38***) would have been sent through his personal assistant.

135. As stated above, according to the DoA (***Annexure 7***), all procurement transactions for the GCEO's approval should be counter signed by the GSCE. Consequently, the fact that the GCEO approved the Memorandum (***Annexure 38***) which was rejected by the GSCE without engaging him on his reasons for rejecting same appears to be irregular and in contravention of the DoA (***Annexure 7***) which requires the GSCE to have counter signed with the Group CEO.

136. The conditional approval section of a copy of DLS Procurement EXCO minutes (***Annexure 39***) of meeting held on 22 March 2016 states, amongst others, that "*CM voiced concern and sought clarity from the committee on whether SC should comply with the Procurement Policy or the Single Source agreement in cases where these two are in conflict. CEO averred that the Single Source agreement was signed by the Group CEO and should therefore supersede the Policy in those instances where these two are in conflict subject to the Single Source prices being market-related. To this end*

it was resolved that the Single Source agreement between DLS and VR Laser shall prevails (sic) *over the current Supply chain Policy. In order to align the policy with this decision, DLS will approach GSCE to amend the relevant provisions of the policy to address the conflict going forward."*

137. The assertion made above that "*the Single Source agreement between DLS and VR Laser shall prevails* (sic) *over the current Supply chain Policy*" appears to be irregular (refer to paragraphs 119 to 120 above for a discussion on this).

138. According to the minutes (***Annexure 40***) of DLS EXCO meeting held on 21 April 2016 "*The submission was forwarded to GSCE for approval. GSCE said the submission could not be approved as he is not aware of the Single Source Agreement between DLS and VR Laser. SCE referred the submission back to the CEO and feedback is awaited. SCE confirmed that risk mitigation plan is in place to ensure that the delay does not impact negatively on the Project delivery."*

139. A copy of an email (***Annexure 41***) dated 20 April 2016 addressed by Ms Malahlela to Mr Burger states "*Having signed the preferred supplier agreement with VR Laser, Denel having been in the media with regard to its strategic alliance with VR Laser, Having read several media reports about allegations of state capture by the Gupta family, more concerns are raised about the viability of the partnership and the risks that Denel will be exposed to should Denel decide to continue its relationship with VR Laser. I am struggling to turn a blind eye to this phenomenon.*"

140. The email (***Annexure 41***) further states that "*I would like to reiterate that it is my humble opinion that DLS failed to follow the correct process when*

appointing VR Laser as a preferred supplier for the supply of steel components and fabrications. Amongst other irregularities, there was no RFQ or tender issued for the award of this contract. In this regard, I believe that DLS should have approached the market to ensure good governance. I would also like to bring it to your attention that the current CEO of VR Laser has acknowledged their ties with the Gupta family and the president's son (through indirect shareholding as alleged by the media) in the meeting we had yesterday 19 April 2016 at 15:00."

141. According to the email (***Annexure 41***), *"In light of all these facts I would like to request that DLS carefully reconsider the relationship with VR Laser as a preferred/strategic supplier……".*

142. We noted a copy of an email (***Annexure 42***) dated 20 April 2016 addressed by Mr Burger to Ms Malahlela in response to her email (***Annexure 41***) of 20 April 2016.

143. The email (***Annexure 42***) states *"I must say, I am very surprised and disappointed in having to receive an email of this gravity whilst I am abroad and also given the fact that the appointment of VR Laser was done a very long time ago. And in a time you were intimately involved in the process of the selection of VR Laser as our strategic supplier of complex fabricated components. I also question the fact that you want to "reiterate" that the correct processes were not followed. The first time I heard you say that was very recently (in the passing), and was after the media was questioning the Gupta's involvement and painting a negative picture of Denel. However, I do agree that it is not pleasant to hear the Denel name in a negative connotation. And I am equally proud of the successes of DLS."*

144. The assertion by Mr Burger that Ms Malahlela raised her concerns over the process followed in concluding the MOA with VR Laser for the first time very recently is untrue. As discussed above, Ms Malahlela repeatedly cautioned Mr Teubes, as her immediate report at the time, against not following due processes in this regard. Furthermore, as indicated above, our review of copies of various DLS Procurement EXCO also reveal that Ms Malahlela constantly raised her discomfort on the fact that the MOA was in conflict with Denel's processes and procedures.

145. The email (***Annexure 42***) further states that "*But I want to categorically state that I do not agree with your statement that proper processes were not followed. Surely, we did not send out an RFP for the appointment of a strategic supplier. But we did identify the most complex of complex fabricated systems and went out on open tender. And we did this twice. And this VR Laser won by following the correct processes". "Only thereafter VR Laser was selected and motivated as a strategic supplier. The approval thereof at DCO was done by following due processes". To now say that processes were not followed just because we don't like the owners, or what is written in the papers, or that the CEO of VR Laser is acknowledging certain connections with the Gupta family, is also a concern to me."* We will confirm whether DLS indeed went out on open tender twice in the past and that VR Laser won the said tenders as alleged by Mr Burger above as part of our extended scope forming part of the second phase of our investigation.

146. According to the email (***Annexure 42***), "*I am convinced that the successes DLS recently had, was* (sic) *amongst others, also due to VR Laser's sterling performance as a strategic supplier. The production and fabrication of the Turret hulls in Malaysia, after the technology transfer by VR Laser, went*

extremely well. I am doubtful if any other current supplier could have achieved this. Also, the awarding of the long term agreement by the UN for the supply of Casspirs, was specifically awarded to DLS on condition that VR Laser is used for the fabrication of the hulls, given the past experiences with other suppliers of hulls. Patria also did an evaluation of SA's hull fabrication competency for the Badger hulls, and found VR Laser to be the most competent."

147. The email (***Annexure 42***) states that "*Therefore Celia, what I am trying to say is that VR Laser is widely acknowledged as one of our very best suppliers, they are black owned, and I believe that proper processes were followed in their selection. We cannot now cancel their contract just because the papers paint a negative picture of their involvement with the Guptas. And the possible risks on our reputation in dealing with the VR Laser is not something we are suppose* (sic) *to take a view on. This is something for DCO to consider and I will take it up with them. So Celia, my* (sic) *I please request that we discuss this matter when I am back in the office on Monday.*"

148. We further noted a copy of an email (***Annexure 43***) dated 20 April 2016 addressed by Ms Malahlela to Mr Burger in response to the aforesaid email (***Annexure 42***) sent to her by Mr Burger. The email (***Annexure 43***) states "*Can I arrange a meeting for Friday or Monday? I wold also like to invite Reenen to our discussion to give this matter context and fill you in on some additional information you might not have been aware of. I have just had a brief discussion with him and we have few suggestions on how we can resolve this issue.*"

149. During our consultation with Mr Burger (***Annexure 16***), he stated that the aforesaid proposed meeting with Ms Malahlela did take place and that she

instead focused mainly on the issues raised in the media relating to the ownership of VR Laser and not necessarily on the issues relating to the process followed in concluding the MOA with VR Laser.

150. We noted a copy of a letter (***Annexure 44***) dated 29 April 2016 addressed by Mr Burger to Mr Mlambo titled "*VR LASER: SUPPLY OF FABRICATED STRUCTURES*". The space was provided at the end of the letter (***Annexure 44***) for Mr Mlambo to sign as evidence of his approval.

151. The letter (***Annexure 44***) states "*Firstly, thank you for the constructive meeting held at DCO with Mr. Odwa Mhlwana and yourself on 28 April 2016.*"

152. The letter (***Annexure 44***) further states "*I confirm our discussion that a Single Source Agreement (hereinafter referred to as the "MOA") was entered into with VR Laser on 19 May 2015 pursuant to a motivation being submitted to DCO. The motivation was recommended for approval by both the Group Executive: Business Development, Mr. Zwelakhe Ntshepe and the Group Chief Operations Officer, Mr Jan Wessels whereupon it was approved by the Group CEO at the time namely Mr Riaz Saloojee. The approval by the Group CEO of VR Laser as a single source supplier is in accordance with Regulation 16A16.4 of the National Treasury Regulations (2005). A copy of the approval dated 22 April 2015, the signed MOA and the applicable National Treasury regulation is attached hereto marked "A", "B" and "C" respectively.*"

153. The letter (***Annexure 44***) states "*As indicated during the meeting and in terms of the abovementioned approval, the rationale for appointing VR Laser as a sole supplier was based on, inter alia, the following:*

1. *its unparalleled expertise on fabrication of complex engineering systems which includes but is not limited to turrets, outer shields, add on armour and vehicle hull structures;*
2. *it is a key supplier and strategic partner to DLS;*
3. *it offers the best value having, inter alia, committed to invest capital and resources in its facilities in order to ensure that the capability remains intact and available to DLS for a minimum period of 10 (ten) years;*
4. *it is prepared to assist and has assisted DLS with its obligations in foreign jurisdictions (such as Malaysia) in transferring skills relating to its manufacturing process (hereinafter referred to as Intellectual Property (IP)); and*
5. *it promotes a black industrialist entrepreneurial company within the defence industry."*

154. The letter (***Annexure 44***) further states that "*It is hereby recommended that the attached submissions relating to the Fire Compartment Module (FCM) and the Outer Shield marked "D" and "C" respectively be sourced via VR Laser in accordance with the terms and conditions of the MOA.*"

155. We noted a handwritten comment appended on the letter (***Annexure 44***) below the space provided for the signature of Mr Mlambo. In our consultation with Mr Mlambo (***Annexure 13***), he confirmed that this comment was appended by him and that he also cancelled out the space provided for his signature.

156. The said comment on the letter (***Annexure 44***) states as follows:

"NB! 1. The evidence on how VR Laser was selected is not available to support its appointment as a single-source supplier.

2. The approval process of the MOA excluded Supply Chain and the reasons thereof have not been furnished.

3. The recommendation is, given the fact that Denel Executives committed the company to place orders on VR Laser for specified products for 10 years, to have the same Executives approve future orders.

4. The paragraph in Treasury Regulations that has been cited in the motivation memo is irrelevant because it was not impractical to test the supply market."

157. We noted a signature that appears to be that of Mr Ntshepe on the letter (***Annexure 44***) that purports to be an approving signature as a handwritten comment "Approved" was appended next to the said signature. In our consultation with Mr Ntshepe, he confirmed that he signed the letter (***Annexure 44***) approving the specified submissions when Mr Mlambo rejected same.

158. During our consultation with Mr Mlambo (***Annexure 13***), he informed us that no engagement was had with him by anyone, including Mr Ntshepe, subsequent to his refusal to approve the letter (***Annexure 44***). This was confirmed by Mr Ntshepe who stated that he saw no need to engage Mr Mlambo on his refusal to approve this request in that, as stated above, he believed that due procurement processes had been followed in concluding the MOA with VR Laser. He further stated that he was not willing to waste

time on this matter that could delay the programme resulting in DLS having to pay penalties for failing to meet agreed upon timeframes.

159. Mr Mlambo further stated that he would have handed the letter (***Annexure 44***) back to the DLS Supply Chain Executive after he appended his comment thereon and was not sure how the letter (***Annexure 44***) would have then got to Mr Ntshepe who subsequently approved same. Mr Ntshepe informed us that he would not recall who he received this letter (***Annexure 44***) from as, like all the other documents forwarded to his office, this letter (***Annexure 44***) would have been sent through his personal assistant.

160. As stated above, according to the DoA (***Annexure 7***), all procurement transactions for the GCEO's approval should be countersigned by the GSCE. Consequently, the fact that the GCEO approved the letter (***Annexure 44***) which was rejected by the GSCE without engaging him on his reasons for rejecting same appears to be irregular and in contravention of the DoA (***Annexure 7***) which requires the GSCE to have counter signed with the Group CEO.

161. In relation to the approval of an order for VR Laser amounting to R26,782,159.05 for the rear door assemblies in respect of the "HY Phase 2 Section Variant" project, a copy of minutes (***Annexure 45***) of DLS EXCO meeting held on 04 July 2016, states "*Approved in line with the MOU and e* (sic) *decision taken in the Supply Chain EXCO Procurement meeting of 3rd June 2016, (i.e EM (Supply Chain) enquire if the signature of the GCEO will suffice as the necessary approval required for this transaction to go through, and the Committee averred that the approval suffices due to the fact that GCEO is a higher authority than GSCE, has delegated his powers*

to GSCE and has overall accountability. CEO signed the approval of the order.)"

162. We noted a copy of Denel's response (***Annexure 46***) to the Parliament relating to question number 1569 that was asked of the Minister by a specified MP on 06 June 2017.

163. According to the Parliament response document (***Annexure 46***), the said MP requested the Minister to provide full details (contents, dates contracts were signed, scope of the contracts and the value thereof) of each contract that Denel signed with VR Laser and to state whether each contract complied with the National Treasury requirements with relevant details of such. In instances where the contract did not comply with the National Treasury requirements, the MP requested the Minister to provide reasons for this.

164. The following table reflects a summary of the various contracts that were awarded to VR Laser as per the Parliament response document (***Annexure 46***) which was authored by DLS:

Contract	Procurement Method	Reason	Compliance with SOC Governance	Total Order Value R
Casspir (Historical contracts), for the period 16 October 2003 to 22	RFQ	Industrialised by VR Laser	*Yes*	*176 467 542.79*

Contract	Procurement Method	Reason	Compliance with SOC Governance	Total Order Value R
May 2017				
Casspir (Current contracts), for the period 2016 to 2017	RFQ	Industrialised by VR Laser	*Yes*	*16 437 626.62*
Badger Hulls, for the period 05 August 2014 to 21 October 2016	Closed Tender	Patria Recommended	*Yes*	*235 858 970.57*
Other Spend, for the period 27 August 2009 to 05	RFQ and Single Source	Approved Armour Supplier and Approved Single Source	*Yes*	*98 902 084.38*

Contract	Procurement Method	Reason	Compliance with SOC Governance	Total Order Value R
June 2017		Supplier		
Total				**527 666 224.36**

165. As indicated in the table above, according to the Parliament response document ***(Annexure 46)*** contracts amounting to R527 666 224.36 were awarded to VR Laser during the period 16 October 2003 to 05 June 2017.

166. Furthermore, as indicated in the table above, the total amount of R527 666 224.36 includes a total amount of R98 902 084.38 (last line item in the table above) in respect of which "Approved Armour Supplier" and "Approved Single Source Supplier" were stated as reasons for the award. In our consultation with Mr Masuku, he confirmed that the contracts indicated as having been awarded to VR Laser as a single source supplier relate to the contracts awarded pursuant to the MOA under review. The said contracts awarded pursuant to the MOA under review amounted to R71,318,429.17, according to the Parliament response document ***(Annexure 46)***.

167. In respect of the question whether each contract complied with the National Treasury requirements, the Parliament response document (***Annexure 46***) stated that "*All of the above contracts were in compliance to*

SOC governance in terms of Denel's internal policies and procedures as well as its approval processes."

168. In stating that all the contracts in the table above were in compliance with Denel's internal policies and procedures, DLS misrepresented to the Parliament, insofar as this assertion relates to orders amounting to R71,318,429.17 issued pursuant to the MOA. As already stated above, the process followed in concluding the MOA with VR Laser was in contravention of Denel's due processes and the relevant legislative prescripts.

169. During our consultation with Ms Govender (***Annexure 19***), she stated that the response document (***Annexure 46***) was compiled by her with the assistance of Mr Masuku and other relevant parties within the DLS. She further stated that this document (***Annexure 46***) was then provided to Mr Burger who reviewed and forwarded same to Ms Qinga, the Group Executive: Communications & Public Affairs.

170. The fact that DLS misrepresented to the Parliament as aforesaid is irregular.

171. The following table depicts a chronology of events based on our aforesaid review of documentary evidence provided:

Description	Annexure Reference	Related to MOA or Background information	Date
Email sent by Mr Wessels to Mr Burger titled "*DLS recent request to contract VR Laser*". In this email, Mr Wessels stated that he had been considering the submission to contract VR Laser for Hoefyster received last Thursday and that based on their discussion of Monday he was not ready to recommend it	***Annexure 8***	MOA	17 July 2014
Email titled "*Round robin on VR Laser*" sent by Mr Burger to EXCO in which he referred to the discussion they had had the same morning relating to the award of Hoefyster Hulls contract to VR Laser. In this email, Mr Burger then included his proposed email that was to be sent to DCO for EXCO to provide input prior to him sending same to the Group CEO	***Annexure 9***	Background (separate hulls contract)	18 July 2014
Email sent by Mr Burger to Mr Wessels and Mr Mhlontlo and copied to Mr Saloojee, Ms Tribelhorn and Mr Ntshepe titled "*DLS recent request to*	***Annexure 10***	Background (separate hulls	18 July 2014

Description	Annexure Reference	Related to MOA or Background information	Date
contract VR Laser". The contents of this email are similar to those of the email referred to above sent by Mr Burger to EXCO on 18 July 2014		contract)	
Submission made by DLS EXCO to Group EXCO titled "*Industrialisation and Production of 183 Vehicle Platform Hulls at VR Laser*".	***Annexure 11***	Background (separate hulls contract)	15 October 2014
Email titled "*Motivation for single source supply of Hoefyster Turret armour steel fabrications and components.docx*" sent by Mr Drevin to Ms Malahlela. Attached to this email was an unsigned memorandum dated 9 March 2015 addressed by Mr Drevin to the Executive Manager: Supply Chain titled "Supplier for Hoefyster turret armour steel components and fabrication". The said memorandum indicates that it is a "Request for Single Source supply of Turret FCMs (hulls) and related armour steel	***Annexure 14***	MOA	10 March 2015

Description	Annexure Reference	Related to MOA or Background information	Date
components, e.g. Cradle, Outer Shields and Add-on Armour"			
Email titled "*Motivation for single source supply of Hoefyster Turret armour steel fabrications and components.docx*" sent by Mr Teubes to Ms Malahlela wherein Mr Teubes requested Ms Malahlela to "Prepare a supply chain motivation for consideration at EXCO and to be approved by Riaz to support this request."	***Annexure 20***	MOA	11 March 2015
Email sent by Ms Malahlela to Mr Teubes in response to his aforesaid email of 11 March 2015. In this email Ms Malahlela stated that DLS goes out on tender/RFQ to identify a supplier that meets DLS's requirements and that she would be very uncomfortable selecting any entity as a single source supplier without the tender/RFQ process	***Annexure 21***	MOA	11 March 2015

Description	Annexure Reference	Related to MOA or Background information	Date
Mr Teubes sent an email responding to Ms Malahlela's aforesaid email and stated that "*My suggestion was that before going out into the market get a strategic direction from EXCO and then go into the market to make a final selection*"	***Annexure 22***	MOA	11 March 2015
Ms Malahlela sent an email responding to Mr Teubes's aforesaid email stating "*Aaahhh!!! That makes sense. On it.*"	***Annexure 23***	MOA	11 March 2015
Email titled "*GROUP CEO Submission*" sent by Ms Malahlela to Mr Teubes. Attached to this email was an unsigned submission dated March 2015 (actual date not specified) titled "*GROUP CHIEF EXECUTIVE OFFICER'S SUPPLY CHAIN SUBMISSION*". This submission, addressed to EXCO by Supply Chain, was a request to appoint a single source supplier for the supply of turret FCM's (hulls) and related armour steel	***Annexure 24***	MOA	12 March 2015

Description	Annexure Reference	Related to MOA or Background information	Date
components. Ms Malahlela informed us that this was a submission she had prepared in line with Mr Teubes's recommendation to first obtain a strategic direction from EXCO and thereafter "go to the market" with a view to identifying a suitable service provider			
Email sent by Mr Teubes to Ms Malahlela stating "*I have changed the angle that we ask for approval from Riaz. Please see attached submission. Any inputs?*" Attached to this email was unsigned submission dated March 2015 (actual date not specified) titled "*GROUP CHIEF EXECUTIVE OFFICER'S SUPPLY CHAIN SUBMISSION*". This submission, which was addressed to EXCO by Supply Chain, also related to the appointment of a single source supplier for the supply of turret FCM's (hulls) and related armour steel components. Ms Malahlela informed us that this submission	***Annexure 27***	MOA	20 March 2015

Description	Annexure Reference	Related to MOA or Background information	Date
was an amended version of the initial submission she had prepared in line with Mr Teubes's recommendation as referred to above			
Ms Malahlela sent an email to Mr Teubes in response to his aforesaid email of 20 March 2015 informing Mr Teubes that she had realised that he had taken out her recommendation from the revised submission and that the submission also specified the name of a supplier. She also stated that she was still of the opinion that, should management approve the request, DLS must go on tender/RFQ for the appointment of a single source supplier for this scope of work	***Annexure 30***	MOA	23 March 2015
Letter titled *"MOU WITH VR LASERFOR SUPPLY OF FABRICATED STRUCTURES"* sent by Mr Burger to Mr Salojee recommending that the attached MOU, which outlined the basis of the working relationship with	***Annexure 31***	MOA	16 April 2015

Description	Annexure Reference	Related to MOA or Background information	Date
VR Laser for the industrialisation of the fabricated structures be favourably considered for signature between DLS and VR Laser			
Letter titled "*MOU WITH VR LASER FOR SUPPLY OF FABRICATED STRUCTURES*" sent by Mr Burger to Mr Salojee recommending that VR Laser be categorized as a strategic supplier of Core Sub systems for the supply of fabricated structures and that the attached MOU, which outlined the basis of the working relationship with VR Laser for the industrialisation of the fabricated structures be favourably considered for signature between DLS and VR Laser	***Annexure 32***	MOA	22 April 2015
Memorandum of Agreement between VR Laser and Denel signed by Mr Vander Merwe and Mr Burger on behalf of VR Laser and Denel	***Annexure 34***	MOA	19 May 2015

Description	Annexure Reference	Related to MOA or Background information	Date
respectively			
Urgent DLS Supply Chain meeting wherein, amongst others, DCO's approval of VR Laser as a single source supplier was apparently discussed	***Annexure 33***	MOA	05 June 2015
Email titled *"VR LASER– APPROVAL FROM DCO AS SINGLE SOURCE SUPPLIER"* sent by Ms Govender to EXCO and copied to Ms Malahlela. Attached to this email was a signed MOA and the aforesaid two letters dated 16 April 2015 and 22 April 2015 sent by Mr Burger to Mr Saloojee	***Annexure 35***	MOA	05 June 2015
DLS EXCO meeting wherein its was discussed, amongst others, that DVS was a preferred service provider for the Casspirs project and that, however, UNOPS prescribed VR Laser as the preferred supplier for this	***Annexure 36***	Background (various)	07 August 2015

Description	Annexure Reference	Related to MOA or Background information	Date
order			
DLS Special Procurement EXCO wherein, amongst others, an alleged conflict between the MOA with VR Laser and the Denel Supply Chain Policy as well as DLS Supply Chain Procedure was discussed. In this meeting it was resolved, inter alia, that the MOA takes precedence over the GSCE's condition, Denel Supply Chain Policy and DLS Supply Chain Procedure	***Annexure 37***	Partly MOA and Background	29 October 2015
Memorandum titled "*Conflict between policy and signed MOU*" was sent by Ms Malahlela to Mr Mlambo requesting permission to implement the EXCO decision to allocate work to VR Laser. This was after Ms Malahlela "approached DLS EXCO to make a decision as to whether to honour the MOA and place the order on VR Laser or to follow the supply chain policy	***Annexure 38***	MOA	29 October 2015

Description	Annexure Reference	Related to MOA or Background information	Date
and procedure from (intergroup) viz, DVS or LMT for this project."			
Mr Mlambo rejected the aforesaid Memorandum sent to him by Ms Malahlela on 29 October 2015 and instead appended a handwritten comment thereon stating that DVS and LMT must submit proof that they cannot meet the requirements prior to the contract being awarded to VR Laser	***Annexure 38***	MOA	Unidentified
Mr Ntshepe approved the aforesaid Memorandum sent by Ms Malahlela on 29 October 2015 and rejected by Mr Mlambo	***Annexure 38***	MOA	Unidentified
DLS Procurement EXCO meeting wherein Ms Malahlela raised her concern and sought clarity from the committee on whether SC should comply with the Procurement Policy of the Single Source Agreement with	***Annexure 39***	Partly MOA and Background	22 March 2016

Description	Annexure Reference	Related to MOA or Background information	Date
VR Laser in instances where these are in conflict			
Email sent by Ms Malahlela to Mr Burger in which she referred to several media reports about allegations of state capture by the Gupta family and "reiterated" that DLS had failed to follow the correct process when appointing VR Laser as a preferred supplier for the supply of steel components and fabrications	***Annexure 41***	MOA	20 April 2016
Mr Burger sent an email to Ms Malahlela responding to her aforesaid email of 20 April 2016 addressed to Mr Burger	***Annexure 42***	MOA	20 April 2016
Ms Malahlela sent an email to Mr Burger responding to the aforesaid email of 20 April 2016 addressed to her by Mr Burger	***Annexure 43***	MOA	20 April 2016

Description	Annexure Reference	Related to MOA or Background information	Date
DLS EXCO meeting wherein it was discussed, *inter alia*, that the submission submitted to the GCSE for approval was not approved as the GSCE was not aware of the Single Source Agreement between DLS and VR Laser	***Annexure 40***	Partly MOA and Background	21 April 2016
Meeting held at DCO with Mr Mhlwana and Mr Mlambo in relation to the MOA concluded with VR Laser (Presumably attended by Mr Burger)	***Annexure 38***	MOA	28 April 2016
Letter titled "*VR LASER: SUPPLY OF FABRICATED STRUCTURES*" sent by Mr Burger to Mr Mlambo recommending that the attached submissions relating to the Fire Compartment Module and the Outer Shield be sourced from VR Laser in accordance with the terms and conditions of the MOA	***Annexure 44***	MOA	29 April 2016

Description	Annexure Reference	Related to MOA or Background information	Date
Mr Mlambo rejected the aforesaid submissions sent to him by Mr Burger relating to the Fire Compartment Module and the Outer Shield to be sourced from VR Laser and stated, inter alia, that the evidence on how VR Laser was selected was not available to support its appointment as a single-source supplier	***Annexure 44***	MOA	Unidentified
Mr Ntshepe approved the aforesaid submissions sent to Mr Mlambo by Mr Burger relating to the Fire Compartment Module and the Outer Shield to be sourced from VR Laser	***Annexure 44***	MOA	Unidentified

Description	Annexure Reference	Related to MOA or Background information	Date
DLS EXCO meting wherein, amongst others, Supply Chain enquired whether the signature of GCEO would suffice as the necessary approval required for VR Laser order in respect of the rear door assemblies pertaining to Hoefyster Phase 2	***Annexure 45***	Partly MOA and Background	04 July 2016
The specified MP requested the Minister to provide full details of each contract that Denel signed with VR Laser and to state whether each contract had complied with the National Treasury requirements (question number 1569)	***Annexure 46***	Partly MOA and Background	06 June 2017

Description	Annexure Reference	Related to MOA or Background information	Date
Denel responded to the questions asked by the specified MP. In responding to these, Denel provided the details of various contracts concluded with VR Laser, also stating that all the stated contracts were in "compliance to SOC governance in terms of Denel's internal policies and procedures as well as its approval processes."	***Annexure 46***	Partly MOA and Background	Unidentified

COMMISSION OF INQUIRY
INTO STATE CAPTURE

172. As indicated above, paragraph 6.3.2 of Denel Group Supply Chain Policy (***Annexure 6***) states that "*In instances where the value is above five hundred thousand rand (R500k) and there are many potential suppliers, an open tender process must be followed unless there are compelling good business reasons to follow a closed tender process. In the case of the latter example, approval must still be obtained from Group Supply Chain Executive…..*"

173. As indicated in paragraphs 162 to 166 above, based on our review of the Parliament response document (***Annexure 46***) provided to us in respect of question 1569 that was asked of the Minister by a specified MP on 06 June 2017, we noted that as at 05 June 2017, when this 10-year MOA had only been in force for just over two (2) years (i.e. from 19 May 2015 to 05 June 2017), orders amounting to R71,318,429.17 had been issued to VR Laser pursuant to this MOA. This suggests that the value of this MOA concluded with VR Laser is in excess of the threshold of R500,000.00 in respect of which an open tender process must be followed according to the policy (***Annexure 6***).

174. According to the policy (***Annexure 6***) in instances where there are compelling good business reasons to deviate from the open tender process and follow a closed tender process, an approval must be obtained from GSCE.

175. Based on our review procedures as discussed above, there was no open tender process that was followed in concluding the MOA with VR Laser. Furthermore, not only was an approval of the GSCE not obtained, there was also no closed tender process followed in concluding this MOA.

176. According to Mr Mlambo (***Annexure 13***), subsequent to his refusal to approve the conclusion of the contract with VR Laser in respect of the Hoefyster platform hulls, he was out of office for approximately a week. According to him, when he returned to office, he learnt that the contract had been concluded with VR Laser for the Hoefyster platform hulls and that there was also a signed MOA in place with VR Laser.

177. Mr Mlambo stated that he suspected that both the Hoefyster platform hulls contract and the MOA were concluded with VR Laser in his absence as the parties involved were fully aware that he would not approve these for various reasons as stated above including the requirement for use of Denel internal divisions, amongst others.

178. Our review procedures as outlined above indicate that the MOA was concluded and signed on the basis of letters (***Annexures 31*** and ***32***) dated 16 April 2015 and 22 April 2015 addressed by Mr Burger to Mr Saloojee. This was despite Ms Malahlela's repeated advice to Mr Teubes, amongst others, to follow a tender/RFQ process to conclude the MOA.

179. According to Treasury Regulations 16A6.4 (***Annexure 4***) and paragraph 9.10 of the Gauteng Provincial Government Supply Chain Management policy model (***Annexure 5***) "*If in a specific case it is impractical to invite competitive bids, the accounting officer or accounting authority may procure the required goods or services by other means, provided that the reasons for deviating from inviting competitive bids must be recorded and approved by the accounting officer or accounting authority.*"

180. The provisions of Treasury Regulations 16A6.4 (***Annexure 4***) and paragraph 9.10 of the Gauteng Provincial Government Supply Chain Management

policy model (***Annexure 5***) were not relevant in respect of the conclusion of the MOA with VR Laser as it was not impractical to invite competitive bids.

181. Consequently, the process followed by DLS to conclude the MOA with VR Laser was not in line with the provisions of paragraph 6.3.2 of Denel Group Supply Chain Policy (***Annexure 6***). This is irregular.

182. Furthermore, the process as described above followed in concluded the MOA with VR Laser was in contravention with section 217 of the Constitution (***Annexure 3***) that states that: *"(1) When an organ of state in the national, provincial or local sphere of government, or any other institution identified in national legislation, contracts for goods or services, it must do so in accordance with a system which is fair, equitable, transparent, competitive and cost-effective"* in that the said process followed was not fair and competitive since an opportunity was not afforded to other potential service providers to participate in this process.

183. The fact that external parties (i.e. UN and Patria) recommended the use of VR Laser does not mean that DLS should not have adhered to internal laid down processes and legislative prescripts. Moreover, the said recommendations made by UN and Patria were project specific and could therefore not have been used to justify non-compliance with internal policies and relevant legislative prescripts on any other projects.

184. The process followed was also not transparent in that it was concluded on the basis of the letters (**Annexures 31** and ***32***) sent by Mr Burger to Mr Saloojee with no involvement of SCM. This was after SCM, through Ms Malahlela, cautioned against the use of any other process other than the tender/RFQ process, subsequent to which the process was progressed

without her involvement. The fact that this MOA was concluded in contravention of the provisions of section 217 of the Constitution is irregular.

185. For the same reasons as stated above, the process followed in concluding the MOA with VR Laser was in direct contravention of the paragraph 38(1)(a)(iii) of the PFMA (***Annexure 2***) which states that "*The accounting officer for a department, trading entity or constitutional institution must ensure that the department, trading entity or constitutional institution has and maintains an appropriate procurement and provisioning system which is fair, equitable, transparent, competitive and cost-effective.*" As discussed above, the process followed by DLS was not fair, transparent and competitive. There is also no evidence that this process was equitable and cost effective as required by the provisions of section 217 of the Constitution (***Annexure 3***) and paragraph 38(1)(a)(iii) of the PFMA (***Annexure 2***). This is irregular.

186. Chapter 1 of the PFMA (***Annexure 2***) defines irregular expenditure as follows:

> ***"irregular expenditure*** *means 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*
>
> *(b) the State Tender Board Act, 1968 (Act 86 of 1968), or any regulations made in terms of that Act"*

187. Consequently, the total orders amounting to R71,318,429.17 issued to VR Laser as at 05 June 2017 pursuant to the MOA concluded amount to

irregular expenditure in that, as discussed above, the MOA was concluded in contravention of the provisions of paragraph 38(1)(a)(iii) of the PFMA (***Annexure 2***) and section 217 of the Constitution (***Annexure 3***).

188. In terms of paragraph 81(1)(b) of the PFMA (***Annexure 2***), by signing the MOA with VR Laser which was irregularly concluded, Mr Saloojee as the then Accounting Officer, committed an act of financial misconduct as he permitted, whether wilfully or negligently, the conclusion of this MOA resulting in irregular expenditure amounting to R71,318,429.17 as at 05 June 2017. This is irregular.

189. Furthermore, the parties involved in the process leading to the conclusion of the MOA with VR Laser, as discussed above, resulting in the aforesaid irregular expenditure amounting to R71,318,429.17 are in breach of the provisions of paragraph 57(c) of the PFMA (***Annexure 2***) which requires an official in a public entity to take effective and appropriate steps to prevent, within that official's area of responsibility, any irregular expenditure.

190. The above irregularity relating to irregular expenditure incurred also amounts to a direct contravention of the provisions of paragraphs 45(c), 38(1)(c)(ii) and 51(1)(b)(ii) of the PFMA. Paragraph 45(c) of the PFMA (***Annexure 2***) states that "*An official in a department, trading entity or constitutional institution must take effective and appropriate steps to prevent, within that official's area of responsibility, any unauthorised expenditure, irregular expenditure and fruitless and wasteful expenditure and any under collection of revenue due.*"

191. Paragraph 38(1)(c)(ii) of the PFMA (***Annexure 2***) states that "*The accounting officer for a department, trading entity or constitutional institution*

must take effective and appropriate steps to prevent unauthorised, irregular and fruitless and wasteful expenditure and losses resulting from criminal conduct."

192. According to paragraph 51(1)(b)(ii) of the PFMA (***Annexure 2***) "*An accounting authority for a public entity must take effective and appropriate steps to prevent irregular expenditure, fruitless and wasteful expenditure, losses resulting from criminal conduct, and expenditure not complying with the operational policies of the public entity.*"

193. Furthermore, we have not been provided with any evidence that the provisions of paragraphs 38(1)(g) and 38(1)(h)(iii) of the PFMA were complied with. Paragraph 38(1)(g) of the PFMA (***Annexure 2***) states that "*The accounting officer for a department, trading entity or constitutional institution on discovery of any unauthorised, irregular or fruitless and wasteful expenditure, must immediately report, in writing, particulars of the expenditure to the treasury and in the case of irregular expenditure involving the procurement of goods or services, also to the relevant tender board*".

194. According to paragraph 38(1)(h)(iii) of the PFMA (***Annexure 2***), "*The accounting officer for a department, trading entity or constitutional institution must take effective and appropriate disciplinary steps against any official in the service of the department, trading entity or constitutional institution who makes or permits an unauthorised expenditure, irregular expenditure or fruitless and wasteful expenditure*".

195. The conclusion of the MOA with VR Laser was also in contravention of paragraph 6.10.1 of Denel SOC Ltd Group Supply Chain Policy (***Annexure 6***) which states that, under no circumstances shall products or services that

can be procured from a Group entity or division be procured from an external supplier or non-Denel company unless there is approval by the GSCE based on sound business reasons. LMT, a division of Denel that had capabilities to provide steel fabrications for the Hoefyster programme, was overlooked on account of historical issues of quality that were apparently experienced without securing the necessary approval of the GSCE. In fact, Mr Mlambo believes that he was excluded from this process as the parties involved might have known that he would not approve the conclusion of this MOA with VR Laser.

196. Furthermore, the MOA with VR Laser was concluded in contravention of paragraph 6.9.1 of Denel SOC Ltd Group Supply Chain Policy (***Annexure 6***) which requires suppliers that meet Denel's qualifying criteria to be contracted for a maximum period of three (3) years, unless a longer period is properly motivated and approved as per the DoA.

197. We have not been provided with any evidence of the aforesaid motivation done and approved as required in support of the contract period of ten (10) years relating to the MOA which is in excess of the maximum period of three (3) years provided for in the policy (***Annexure 3***). During our consultation with Mr Teubes and Ms Govender the period of ten (10) years was agreed upon as there was a need to align this period with the estimated duration of the Hoefyster programme.

198. Additionally, according to Ms Govender, the 10-year period was suggested by VR Laser to amended a contract period of three (3) years per standard practice in the draft MOA that was provided to VR Laser for their input. The fact that DLS agreed to this extended period for the MOA with VR Laser is

irregular in that this exposed DLS to an undue risk of being committed to an extended contract period in contravention of the prevailing internal policies.

199. According to the DoA (***Annexure 7***), it is mandatory that any agreement creating an obligation for Denel should follow due process and be approved at the appropriate level of authority. This requirement was not adhered to in that, as already stated above, due processes were not adhered to in concluding the MOA of VR Laser.

200. Additionally, the DoA (***Annexure 7***) was not observed as the GSCE did not approve the MOA. In terms of the DoA (***Annexure 7***), all procurement transactions above R20m are to be approved by the GSCE. Although the conclusion of the MOA was approved by the then GCEO, amongst others, according to the DoA (***Annexure 7***), all procurement transactions approved by the GCEO should also be counter signed by the GSCE. Therefore, the MOA with VR Laser was not approved in line with the DoA (***Annexure 7***). This is irregular.

V CONCLUSIONS

1. Based on our factual findings stemming from procedures as discussed above, which include review of relevant documentary evidence and consultations with relevant parties within Denel, we conclude as follows:

   1.1. The MOA with VR Laser was concluded in contravention of the laid down internal processes and the provisions of the relevant legislative prescripts including the Constitution and the PFMA. The provisions of Treasury Regulations 16A6.4 and paragraph 9.10 of the Gauteng Provincial Government SCM policy model were not relevant in respect of the conclusion of the MOA with VR Laser as it was not impractical to invite competitive bids;

   1.2. Although the value of the MOA is excess of the threshold of R500,000.00, an open tender process was not followed in concluding this MOA. In terms of the Denel Group Supply Chain Policy, an open tender process should be followed where the value is above R500,000.00 unless there are compelling good business reasons to follow a closed tender process. In the case of a closed tender, approval must also be obtained from the GSCE. Not only was an approval of the GSCE not obtained, there was also no closed tender process followed in concluding this MOA;

   1.3. The MOA was concluded based on the letters sent by Mr Burger to Mr Saloojee with no involvement of SCM. This was after SCM, through Ms Malahlela, cautioned against the use of any other process other than the tender/RFQ process, subsequent to which the process was progressed without her involvement;

1.4. The MOA was not approved by the GSCE as required by the DoA. Additionally, although the MOA was signed by Mr Saloojee, in his capacity as the GCEO at the time, in terms of the DoA and by virtue of the amount involved, this transaction needed to be approved by the GSCE as well;

1.5. LMT, the division of Denel, was overlooked on account of certain alleged historical issues of non-performance relating to other programmes in contravention of the prevailing policies and procedures;

1.6. The contract period of ten (10) years in respect of the MOA is in contravention of the provisions of the Denel Group Supply Chain Policy which require qualifying suppliers to be contracted for a maximum period of three (3) years unless a longer period is properly motivated and approved as per DoA. We have not been provided with any evidence of conformance to this requirement;

1.7. In fact, based on our consultations with relevant parties with DLS, the contract period of ten (10) years was suggested by VR Laser. Allowing this extended contract period in contravention of the prevailing Denel's policy and thereby unnecessarily exposing DLS to undue risk of being committed to this MOA for a much longer period was irregular on the part of DLS;

1.8. Furthermore, the process as described above followed in concluded the MOA with VR Laser was in contravention with section 217 of the Constitution that required this MOA to have been concluded in a system which is fair, equitable, transparent, competitive and cost-effective, in that the said process followed was not fair and

competitive since an opportunity was not afforded to other potential service providers to participate in this process;

1.9. The fact that external parties (i.e. UN and Patria) recommended the use of VR Laser does not mean that DLS should not have adhered to internal laid down processes and legislative prescripts. Moreover, the said recommendations made by UN and Patria were project specific and could therefore not have been used to justify non-compliance with internal policies and relevant legislative prescripts on any other projects;

1.10. The process followed was also not transparent in that, as stated above, it was concluded based on the letters sent by Mr Burger to Mr Saloojee with no involvement of SCM. The fact that this MOA was concluded in contravention of the provisions of section 217 of the Constitution is irregular;

1.11. For the same reasons as stated above, the process followed in concluding the MOA was in direct contravention of the paragraph 38(1)(a)(iii) of the PFMA which requires Denel to maintain an appropriate procurement system which is fair, equitable, transparent, competitive and cost-effective. As discussed above, the process followed by DLS was not fair, transparent and competitive. There is also no evidence that this process was equitable and cost effective as required by the provisions of section 217 of the Constitution and paragraph 38(1)(a)(iii) of the PFMA. This is irregular;

1.12. Consequently, the orders amounting to R71,318,429.17 issued to VR Laser as at 05 June 2017 pursuant to the MOA concluded amount to irregular expenditure in that, as discussed above, the

MOA was concluded in contravention of the relevant provisions of the PFMA and the Constitution;

1.13. In terms of paragraph 81(1)(b) of the PFMA, by signing the MOA with VR Laser which was irregularly concluded, Mr Saloojee as the then Accounting Officer, committed an act of financial misconduct as he permitted, whether wilfully or negligently, the conclusion of this MOA resulting in irregular expenditure amounting to R71,318,429.17 as at 05 June 2017. This is irregular;

1.14. Furthermore, the parties involved in the process leading to the conclusion of the MOA with VR Laser, as discussed above, resulting in the aforesaid irregular expenditure amounting to R71,318,429.17 are in breach of the provisions of paragraph 57(c) of the PFMA which requires an official in a public entity to take effective and appropriate steps to prevent, within that official's area of responsibility, any irregular expenditure;

1.15. The above irregularity relating to irregular expenditure incurred also amounts to a direct contravention of the provisions of paragraphs 38(1)(c)(ii) and 51(1)(b)(ii) of the PFMA which require the accounting officer and accounting authority of Denel to take effective and appropriate steps to prevent irregular expenditure;

1.16. In stating that all the contracts awarded to VR Laser were in compliance with Denel's internal policies and procedures, DLS misrepresented to the Parliament, insofar as this assertion relates to orders amounting to R71,318,429.17 issued pursuant to the MOA. As already stated above, the process followed in concluding the MOA with VR Laser was in contravention of Denel's due processes and the relevant legislative prescripts. The fact that DLS

misrepresented to the Parliament in this regard is irregular. The responses to Parliament were provided by Mr Burger with the assistance of Ms Govender and Mr Masuku;

1.17. We were not provided with copies of minutes of DLS EXCO meeting where the SCM submission relating to the motivation of a single source supplier was apparently "debated and analysed". During our consultations with relevant parties within DLS we were informed that this was an informal EXCO coffee session and not a procurement meeting. Furthermore, there was apparently no formal recommendation that resulted from this session. It is unclear why an important matter as a motivation for single source relating to a crucial programme like Hoefyster would be discussed over a mere coffee session and not appropriately recorded; and

1.18. Consequently, it would appear that the assertion made by Mr Burger in the said communication to Denel that an SCM submission was "debated and analysed" in a meeting which we now understand was merely a coffee session with no formal recommendation taken was a misrepresentation.

VI RECOMMENDATIONS

1. Based on our investigative findings and conclusions above, we recommend that Denel considers the following:

1.1. Obtaining legal advice on appropriate corrective measures to be considered by Denel in view of the irregularities identified relating to the conclusion of the MOA with VR Laser. The MOA was concluded in contravention of Denel laid down processes and relevant legislative prescripts;

1.2. Taking appropriate corrective action against the following parties involved in the irregularities identified:

Mr Burger

1.2.1. For concluding the MOA with VR Laser in contravention of the laid down internal processes and the provisions of the relevant legislative prescripts including the Constitution and the PFMA, in that he signed the letters dated 16 April 2015 and 22 April 2015 which resulted in the conclusion of the MOA;

1.2.2. For concluding the MOA with VR Laser in contravention of the laid down internal processes and the provisions of the relevant legislative prescripts including the Constitution and the PFMA, in that he signed the said MOA on behalf of DLS;

1.2.3. For incurring irregular expenditure amounting to R71,318,429.17 in contravention of the PFMA provisions, in that he concluded the MOA with VR Laser in contravention of the laid down internal processes and the provisions of the relevant legislative prescripts including the Constitution and the PFMA;

1.2.4. For committing DLS to a period of ten (10) years, in terms of the MOA with VR Laser, in contravention of the Denel's prevailing policies that required qualifying suppliers to be contracted for a maximum period of three (3) years; and

1.2.5. For misrepresenting to Parliament that due processes were followed in concluding the MOA with VR Laser.

Mr Saloojee

1.2.6. For concluding the MOA with VR Laser in contravention of the laid down internal processes and the provisions of the relevant legislative prescripts including the Constitution and the PFMA, in that he approved the letter dated 22 April 2015 which resulted in the conclusion of the MOA; and

1.2.7. For incurring irregular expenditure amounting to R71,318,429.17 in contravention of the PFMA provisions, in that he concluded the MOA with VR Laser in contravention of the laid down internal processes and the provisions of the relevant legislative prescripts including the Constitution and the PFMA.

Mr Burger, Mr Makhatini, Mr Khoza, Mr Teubes, Mr Mahlinza, Mr Williams and Ms Govender

1.2.8. For concluding the MOA with VR Laser in contravention of the laid down internal processes and the provisions of the relevant legislative prescripts including the Constitution and the PFMA, in that they were part of the DLS EXCO meeting of 3 March 2015 wherein the resolution was taken to conclude the MOA with VR Laser.

Mr Teubes

1.2.9. For his involvement in the conclusion of the MOA with VR Laser in contravention of the laid down internal processes and the provisions of the relevant legislative prescripts including the Constitution and the PFMA, in that he consistently ignored the SCM recommendation to follow a competitive process in concluding the MOA with VR Laser and instead recommended the conclusion of the said MOA with VR Laser, as per the submission dated March 2015 addressed to EXCO, as the SCM process had allegedly been followed for the Hoefyster vehicle and the AV8 turrets;

1.2.10. For incurring irregular expenditure amounting to R71,318,429.17 in contravention of the PFMA provisions, in that he was involved in the conclusion of the MOA with VR Laser in contravention of the laid down internal processes and the provisions of the relevant legislative prescripts including the Constitution and the PFMA; and

1.2.11. For committing DLS to a period of ten (10) years, in terms of the MOA with VR Laser, in contravention of the Denel's prevailing policies that required qualifying suppliers to be contracted for a maximum period of three (3) years.

Mr Wessels

1.2.12. For his involvement in the conclusion of the MOA with VR Laser in contravention of the laid down internal processes and the provisions of the relevant legislative prescripts including the Constitution and the PFMA, in that he approved the letter dated 22 April 2015 recommending the conclusion of the MOA.

Mr Ntshepe

1.2.13. For his involvement in the conclusion of the MOA with VR Laser in contravention of the laid down internal processes and the provisions of the relevant legislative prescripts including the Constitution and the PFMA, in that he signed the letters dated 16 April 2015 and 22 April 2015 recommending the conclusion of the MOA.

Ms Govender

1.2.14. For committing DLS to a period of ten (10) years, in terms of the MOA with VR Laser, in contravention of the Denel's prevailing policies that required qualifying suppliers to be contracted for a maximum period of three (3) years; and

1.2.15. For misrepresenting to Parliament that due processes were followed in concluding the MOA with VR Laser.

Mr Masuku

1.2.16. For misrepresenting to Parliament that due processes were followed in concluding the MOA with VR Laser.

1.3. Reporting the irregular expenditure amounting to R71,318,429.17 incurred pursuant to the conclusion of the MOA with VR Laser to the National Treasury in line with the provisions of paragraph 38(1)(g) of the PFMA and the requirements of the Gauteng Provincial Government Supply Chain Management Policy model;

1.4. Quantifying the irregular expenditure that will be potentially incurred for the remainder of the contract duration in respect of the MOA concluded with VR Laser in contravention of Denel laid down processes and relevant legislative prescripts and take appropriate corrective measures to prevent incurrence thereof as per the provisions of paragraphs 38(1)(c)(ii), 51(1)(b)(ii) and 57(c) of the PFMA;

1.5. Reviewing orders issued to VR Laser pursuant to the MOA, in view of the irregularities identified in the process followed in concluding the MOA. As at 05 June 2017, orders amounting to R71,318,429.17 had been issued to VR Laser pursuant to the MOA;

1.6. Reviewing payments made to date to VR Laser pursuant to the MOA, in view of the irregularities identified in the process followed in concluding the MOA. The review should determine whether all payments made were in accordance with the terms and conditions of the signed MOA, whether these were approved in line with the DoA and whether all payments made are in respect of services rendered and products delivered to DLS;

1.7. Reviewing the processes followed in awarding the following contracts to VR Laser, in view of the irregularities identified in the process followed in concluding the MOA with VR Laser:

Contract Description	Amount R
Casspir, historical contracts for the period 16 October 2003 to 22 May 2017	176 467 542.79
Casspir, current contracts for the period 2016 to 2017	16 437 626.62
Badger Hulls, for the period 05 August 2014 to 21 October 2016	235 858 970.57
Other Spend, for the period 27 August 2009 to 05 June 2017 (R98 902 084.38 - R71,318,429.17)	27 583 655.21
Total	**456 347 795.10**

1.8. We have since been requested to review the process followed in concluding the contract with VR Laser in respect of the Badger hulls amounting to R235,858,970.57, as indicated in the table above, as part of our extended mandate to be performed in the second phase of our investigation.

VII OUTSTANDING ITEMS

1. Copies of minutes of Hoefyster tender meeting apparently held with VR Laser on 26 June 2014 remain outstanding as at the date of this draft report.

2. Imaging of the computers/laptops allocated to Mr Burger and Mr Teubes and review of relevant information extracted therefrom.